THE HIGH COURT OF DELHI AT NEW DELHI

% Judgment delivered on: 30.04.2015

+ ITA 1105/2010

COMMISSIONER OF INCOME TAX ..... Appellant

versus

VISHISHTH CHAY VYAPAR LTD. ..... Respondent

+ ITA 1106/2010

COMMISSIONER OF INCOME TAX ..... Appellant

versus

VISHISHTH CHAY VYAPAR LTD. ..... Respondent

+ ITA 1107/2010

COMMISSIONER OF INCOME TAX ..... Appellant

versus

VISHISHTH CHAY VYAPAR LTD. ..... Respondent

Advocates who appeared in these cases:

For the Appellant : Mr Rohit Madan and Mr Ruchir Bhatia.
For the Respondent : Mr Ajay Vohra, Sr Adv. with Ms Kavita Jha and Mr Vaibhav Kulkarni.

CORAM:-
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR JUSTICE VIBHU BAKHRU

JUDGMENT

VIBHU BAKHRU, J

1. These appeals, preferred by the Revenue under Section 260A of the Income Tax Act, 1961 (hereinafter the 'Act'), impugn a common order dated 30.06.2009 passed by the Income Tax Appellate Tribunal (hereinafter

the 'Tribunal') to the extent that the appeals preferred by the Revenue (being ITA 3763/Del/2007, ITA 3764/Del/2007 and ITA 3732/Del/2007) against the orders passed by the Commissioner of Income Tax (Appeals) (hereafter 'CIT (A)') in respect of assessment years 1997-1998, 1998-1999 and 1999-2000, have been rejected. The said common order dated 30.06.2009 also disposed of an appeal preferred by the Revenue in respect of assessment year 1996-97, however the same is not subject matter of these appeals.

2. The principal controversy involved in the present appeals relates to disallowance of loss on account of alleged transactions entered into by the assessee in respect of the shares of certain companies and further the loss claimed on account of diminution in value of those shares.

3. Briefly stated, the relevant facts leading to the present appeals are as under:-

3.1 The assessee filed its return for the assessment year 1997-98 declaring an income of ₹1,05,518/-. The said income was calculated after claiming a loss of ₹4,64,82,500/- on account of purchase and sale of shares and diminution in the value of shares held by the assessee. By an assessment order dated 14.03.2000, the Assessing Officer (hereafter 'AO') disallowed the said loss of ₹4,64,82,500/- and assessed the income of the assessee as ₹8,72,20,744/- for the assessment year 1997-98. The assessee preferred an appeal before the CIT(A) which, was rejected by an order dated 05.03.2001. The assessee carried the said order in appeal, being ITA No.2978/Del/2001, before the Tribunal.

3.2 The assessee filed a return for the assessment year 1998-99 declaring an income of ₹59,070/-. The said income was calculated after claiming a loss of ₹5,36,23,950/- on account of sale and purchase of shares of certain companies. By an assessment order dated 07.03.2001, the AO disallowed the said loss of ₹5,36,23,950/- and assessed the income of the asseesse as ₹11,06,81,611/- for the assessment year 1998-99. The assessee preferred an appeal before the CIT(A), which was dismissed by an order dated 13.01.2003. The assessee appealed against this order, being ITA No.2836/Del/2003, before the Tribunal.

3.3 The assessee filed a return for the assessment year 1999-2000 declaring an income of ₹70,120/-. The said income was calculated after claiming a loss of ₹6,16,86,500/- on account of sale and purchase of shares of certain companies. By an assessment order dated 27.03.2002, the AO disallowed the said loss of ₹6,16,86,500/- and assessed the income of the asseesse as ₹17,04,95,139/- for the assessment year 1999-2000. The assessee preferred an appeal before the CIT(A) which was dismissed by an order dated 13.01.2003. The assessee appealed against this order (ITA No.2837/Del/2003) before the Tribunal.

3.4 The Tribunal, by its order dated 19.10.2004, disposed of the said appeals (being ITA No.2978/Del/2001 for AY 1997-98, ITA No.2836/Del/2003 for AY 1998-99 and ITA No.2837/Del/2003 for AY 1999-2000) along with appeal (ITA No.2835/Del/2003 for AY 1996-97). By the said order, the Tribunal deleted most of the additions made by the AO to the assessed income of the assessee but insofar as the losses claimed by the assessee, in relation to the shares of companies, the Tribunal

remanded the matter to the AO to consider it afresh. The Tribunal held that the statements of persons relied upon by the AO justified entertaining suspicion as to the transaction of sale/purchase of shares. However, since the assessee was not confronted with material collected by AO, the same had resulted in a material irregularity in respect of the three assessments (being assessments relating to the assessment years 1997-98 to 1999-2000). The Tribunal also held that the documents relied upon by the assessee - confirmation memos/contract notes, bills, letters confirming registration of shares etc. - were required to be considered.

3.5 Pursuant to the order dated 19.10.2004 passed by the Tribunal, the AO considered the question with regard to the loss on account of shares claimed by the assessee in various years and disallowed the same. The AO found that the assessee had purchased most shares of certain companies from one Sh Nem Chand Jain, who was stated to be a broker with the Gauhati Stock Exchange. Although the value of these transactions was large, no payments for the same were made and the consideration for purchase of the said shares was reflected as outstanding and payable to Sh. Nem Chand Jain. Sh. Nem Chand Jain had neither charged any interest nor instituted any proceedings for recovery of the said amount. The AO had found that Sh. Nem Chand Jain was not a person of means and the transactions in question were bogus.

3.6 The assessee filed appeals (being Appeal No.47/2007-08 for AY 1997-98, Appeal No.48/2007-08 for AY 1998-99 and Appeal No.49/2007-08 for AY 1999-2000), *inter alia*, against the assessment orders framed with respect to the assessment years 1997-98 to 1999-00. The CIT(A)

accepted the contract notes and other documents produced by the assessee as evidence of the genuineness of the transactions of sale and purchase of shares as well as reduction in their value at the end of the relevant year and allowed the aforesaid appeals filed by the assessee by three separate orders - two orders dated 29.06.2007 in respect of assessment years 1997-98 and 1999-00 and an order dated 22.06.2007 in respect of the assessment order 1998-99.

3.7 The Revenue preferred appeals before the Tribunal assailing the decision of the CIT(A) to allow the loss claimed by the assessee. The Revenue urged that the loss claimed by the assessee on account of sale and purchase of shares and diminution in their value could not be set off from business income in view of Section 73 of the Act. These appeals preferred by the Revenue were rejected by the Tribunal by the common order dated 30.06.2009, which is impugned herein. The Tribunal found that the purchase bills for the shares purchased along with brokers contract note and copy of the confirmation from the respective companies indicating the transfer of shares in the name of the assessee evidenced the genuineness of the losses claimed by the assessee. The Tribunal further noted that the shares were bought through the Gauhati Stock Exchange and their transfers in the name of the assessee were confirmed by letters received from the respective companies. The Tribunal was of the view that as the shares were held in stock in trade, the same could be valued at cost or market price, whichever is lower, and a loss on account of diminution in value of the stocks could be set off by the assessee against its other income. The Tribunal noted that the companies whose shares were purchased by the

assessee were genuine companies and regularly assessed to tax in their respective wards. Since the Tribunal held that the transaction in purchases of the shares were genuine, the decisions of the CIT(A) were upheld.

3.8 The Revenue's contention that the losses claimed by the assessee could not be set off against income by way of interest by virtue of Section 73 of the Act was rejected. The Tribunal held that as the said contention had not been urged either before the authorities below or before the Tribunal, in the first round, the Revenue could not be permitted to raise the said contention for the first time in the second round.

4. In the aforesaid facts, the controversy to be addressed is whether the Tribunal has erred in holding that the loss of ₹4,64,82,500/- for the assessment year 1997-98; the loss of ₹5,36,23,950/- for the assessment year 1998-99; and the loss of ₹6,16,86,500/- for the assessment year 1999-2000, on account of sale and purchase of shares of certain companies and on account of diminution in their value were allowable.

5. By an order dated 03.09.2014, this Court had indicated that the following substantial question of law arose for consideration in these appeals:-

> "Whether the finding of the Income Tax Appellate Tribunal accepting the genuineness of the loss as declared in respect of shares purchased and sold or held as stock-in-trade is perverse?"

6. The AO had concluded that the transactions of sale and purchase of shares of certain companies, on the basis of which losses were being claimed by the Assessee, were not genuine and, accordingly, the said losses

had been disallowed. Before proceedings to examine the decision rendered by the Tribunal, it would be essential to note the reasons which led the AO to conclude that the transactions in shares were not genuine.

7. The nature of transactions in each of the assessment years involved i.e. 1997-98 to 1999-2000 are, essentially, similar. Thus, for the sake of brevity, the transactions relating to the previous year 1996-97 relevant to the assessment year 1997-98 are being referred to for the purpose of appreciating the AO's findings and reasoning.

8. The following shares were reflected as opening stock–in- trade as on 01.04.1996:-

Name of the Company	No. of shares	Rate(₹)	Value(₹)
Baba Business Services Ltd.	91300	2.0	1,82,600
Sangrahalaya Timber & Crafts Limited	30800	2.0	61,600
Premier Auto Finance Ltd	50000	10	500,000
Pulp Products Limited	10000	2	20,000
Mather & Platt India Ltd	38500	13.5	5,19,750

9. Out of the aforesaid shares, the shares of Baba Business Services Ltd. were sold during the year at the value reflected. Thus, no profit or loss was claimed with respect to that transaction. No transactions in shares of Sangrahalaya Timber & Crafts Limited and Premier Auto Finance Limited, were reported during the year. The shares of Pulp Products Ltd. were purportedly sold at ₹3.00 per share and, therefore, a profit of ₹10,000 was reported in respect of the said transaction. One thousand shares of Mather

& Platt India Limited were purportedly sold at ₹13.10 each and an aggregate loss of ₹400/- was reported with respect to that transaction. As is apparent from the above, the effect of aforesaid transactions was a net profit of ₹9,600/-, which is not significant. The paper book filed before this court also does not contain any documents relating to the said transactions.

10. During the previous year ended 31.03.1997 the assessee claimed to have purchased shares of the following companies for a value of ₹5,35,49,550/-:-

S. No.	**Name of the Coy.**	**Qty**	**Rate(₹)**	**Amount(₹)**
1.	M/s Hotahoti Wood Products Ltd.	96125	15.60	14,99,550
2.	M/s Purbanchal Pre stressed Ltd.	1240000	15.60	1,92,29,000
3.	M/s Kamini Finance & Inv. Ltd.	1635000	20.00	3,27,00,000
4.	M/s Doyang Wood Products Ltd.	13000	10/-	1,30,000
			TOTAL	**₹5,35,49,550**

11. All the aforesaid shares, except shares of M/s Doyang Wood Products. Ltd. amounting to ₹1,30,000, were purchased from one Shri Nem Chand Jain. Thus, the assessee claimed that it had purchased shares of a value of ₹5,34,19,550/- from Shri Nem Chand Jain. These shares were not sold during the year and were reflected as a part of the closing stock of shares as on 31.03.1997. The shares of Doyang Wood Products were stated to be purchased from one Shama Holdings Private Limited at the rate of

₹10 each aggregating ₹1,30,000 (Rupees One Lac thirty thousand). These shares of Doyang Wood Products Ltd were claimed to have been sold during the year at the rate of ₹2.50 each aggregating ₹32,500/-. The copy of the ledger produced by the assessee indicates that the said shares were purchased on credit but the same were sold in cash. Plainly, the transactions for sale and purchase of these shares, which resulted in loss of ₹98,500/-, were 'off market' transactions and not through any stock exchange or through any stock broker.

12. For the previous year ending 31.03.1997, the assessee had claimed a loss of ₹4,64,82,500/-. This loss has two components; the first being, loss relating to sale and purchase of shares and the second being loss on account of diminution in value of the stock of shares held by the assessee at the end of the year. Whilst an amount of ₹88,900/- was claimed as loss on sale of shares, the bulk of the loss claimed, that is ₹4,63,93,600/-, was on account of reduction in value of the closing stock of shares. Out of the aforesaid loss only a sum of ₹56,250/- was on account of reduction in value of the shares of Mather & Platt India Limited and the remaining amount of ₹4,63,28,350/- was shown as loss on account of fall in the value of shares, as on the closing date i.e. 31.03.1997, purportedly purchased by the assessee during the course of the year. The break-up of the aforesaid amount is as under:-

S. No.	**Name of the Coy. (M/s)**	**No. of Shares**	**Rate (₹)**	**Value (₹)**	**Losses (₹)**
1.	M/s Hotahoti Wood Products Ltd.	96125	15.60	2.40	1,26,88,50

2.	M/s Purbanchal Prestressed Ltd.	124000	15.60	2.50	1,61,20,000
3.	M/s Kamini Finance & Inv. Ltd.	1635000	20.00	2.30	2,89,39,500
				Total	**4,63,28,350**

13. As indicated earlier, the abovementioned shares, which are claimed to have resulted in loss on account of reduction in their value, were claimed to have been purchased by the assessee from one Shri Nem Chand Jain for a sum ₹5,34,19,550/-.

14. The assessee claims the aforesaid transactions to be genuine and in support of the said claim, the assessee produced:

a) confirmation memo from Shri Nem Chand Jain;

b) purchase bills from Nem Chand Jain;

c) letters of transfer from the companies, whose shares had been purchased, confirming that the shares had been transferred in the name of the assessee;

d) a bill indicating sale of 13000 shares of M/s Doyang Wood Products Ltd. to one Shri Ram Lal Ashoka of Chandni Chowk, Delhi;

e) copy of the ledger accounts; and

f) certificate dated 12.02.2000 from Gauhati Stock Exchange indicating the prices at which the shares of the companies involved were traded.

15. The assessee further asserted that Shri Nem Chand Jain was a broker with the Gauhati Stock Exchange and the memos of confirmation as well as the bills produced evidenced the genuineness of the purchase transactions. In addition, the assessee also produced a certificate indicating the value of

the quotations of the shares in question from the Gauhati Stock Exchange. This, according to the assessee, evidenced the value of the shares.

16. In order to examine the genuineness of the transactions, the AO made a reference to the Additional Director of Investigation, Income Tax and requested the income tax authority to inquire and report on, *inter alia*, the financial position of Shri Nem Chand Jain.

17. In response to the aforesaid inquiry, the AO was informed that search and seizure operations were conducted in the case of Shri Nem Chand Jain on 14.10.1996. During the course of the said search and further proceedings, statement of Shri Nem Chand Jain was recorded under Section 132(4) and Section 131 of the Act and the same were forwarded to the AO. Shri Nem Chand Jain had stated that he was a Director/Managing Director of M/s Doyang Wood Products Ltd., M/s Kamini Finance & Investment Ltd., M/s Hotahoti Wood Products Ltd. in addition to other companies. He had stated that he was not aware of affairs of those companies but had acted at the instruction of one Mr R. R. Modi. He further stated that he received expenses from Shri R. R. Modi in lieu of services rendered.

18. The AO was informed that Sh. R.R. Modi had made a disclosure that he had promoted the following companies by introducing share application money in different names aggregating ₹170,00,000/-:-

1. M/s Kamala Kal Ltd.
2. M/s Gulmohar Estates Ltd.
3. Dass Apartments Ltd.

4. Manipur Pharmaceuticals Ltd.

5. Pulp Products Ltd.

6. M/s Raksha Audio Ltd.

7. Sangrahalaya Timber & Crafts Ltd.

8. M/s Doyang Wood Products Ltd.

9. M/s North Eastern Publishing & Advertising Co. Ltd.

10. Hotahoti Wood Products Ltd.

11. Purbanchal Presstressed Ltd.

12. Kamini Finance & Investment Co. Ltd.

Mr R.R. Modi had further admitted that the companies mentioned at serial no. 7 to 12 above were not genuine companies.

19. The AO took note of the above statements received from the Income Tax Authorities in Gauhati and also examined the books of accounts produced by the assessee. The AO concluded that the transactions claimed by the assessee were not genuine. The facts that led him to come to this conclusion are summarized as under:-

a) The assessee had not paid for the shares that he had purchased and the consideration was only reflected as book entries. During the previous year ended 31.03.1997 the assessee had purchased shares for a sum of ₹5,35,49,550/- including shares of a value of ₹5,34,19,550/- from Shri Nem Chand Jain. And, the said consideration was shown as credit in the name of the sellers.

b) Although Shri Nem Chand Jain had financed almost the entire purchase of shares, there was no agreement with Shri Nem Chand Jain for this financing arrangement. He had also not charged any interest on the amounts outstanding.

c) Shri Nem Chand was not a person of means and his creditworthiness was not established. The report of the Income Tax Authorities from Gauhati indicated that Shri Nem Chand Jain had returned income of ₹40,000/- by way of salary. The assessee did not produce any material to establish the creditworthiness of Shri Nem Chand Jain

d) Trading in shares of the companies in question, on the Gauhati Stock Exchange, were to be on "spot basis" and thus the transactions claimed by the assessee were contrary to the practice of the said Stock Exchange; admittedly, there was no settlement of accounts through the Stock Exchange.

e) The AO further noted that the shares of the companies which were involved were not actively traded and thus the quotations indicating the value of the shares could not be accepted. No material was produced to controvert the finding that the shares of the companies were not actively traded.

f) The assessee and the companies in question were interlinked. Shri R. R. Modi had floated certain number of companies by introducing his undisclosed capital and he was also a Director on the Board of the assessee company. In addition, the assessee also owed money to certain companies, whose shares it held/purchased. These companies

also held shares of the assessee company. The fact that the companies in question and the assessee were connected was also not disputed.

g) The assessee explained that since it was facing a financial crisis, it could not pay the amount due to Shri Nem Chand Jain for the transactions executed during the year. However, this did not explain as to why Shri Nem Chand Jain continued to sell shares to the assessee even in the following year, i.e., year ended 31.3.1998. No explanation was provided as to why Shri Nem Chand Jain, inspite of being an unpaid seller would physically deliver the shares sold by him.

20. In the first round, the Tribunal remanded the matter to the AO (by an order dated 19.10.2004) principally on the ground that the assessee had not been confronted with the material relied upon by the AO and further to examine the effect of contract notes bills, stock exchange quotations and confirmation statement filed by the brokers. On remand, the AO again found against the assessee disbelieving the documents produced by it. The AO noted that the memos relating to the transaction were serially numbered or signed by Shri Nem Chand Jain. The assessee further noted that no evidence from the Gauhati Stock Exchange had been produced. The quotations indicated by the Gauhati Stock Exchange were also rejected as the AO found that except some transaction done by assessee, the shares in question were not quoted and thus, they did not reflect the true value of the shares in question. It was held that the documents produced by the assessee

were only for the purpose of misleading the authorities and could not establish that the transactions were genuine.

21. The nature of transactions relating to the assessment years 1998-99 and 1999-2000 are not materially different.

22. During the year ended 31.03.1998, 30800 number of shares of Sangrahalaya Timber and Crafts Limited that were reflected as closing stock as on 31.03.1997 at a value of ₹2/- each, were purportedly sold at the said book value, i.e. at the rate of ₹2/- per share. The memo of confirmation dated 23.04.1997, issued by N.C. Jain in respect of the aforesaid transaction indicates that he had purchased the said shares - as opposed to selling the shares on behalf of the assessee through the stock exchange - and the transaction was on principal to principal basis. Thereafter, on 15.05.1997 the assessee is stated to have purchased 27,50,000 shares of Sangrahalaya Timber and Crafts Limited @ ₹10/- each. These shares were also purchased from Mr N.C. Jain and the memo of confirmation also indicates that the transaction between assessee and Mr N.C. Jain was on principal to principal basis. The said shares were valued at the rate of ₹2.25/- each at the end of the year and on this basis the assessee claimed a loss of ₹2,13,12,500/-.

23. The shares of Hotahoti Wood Products Ltd., Purbanchal Prestressed Ltd. and Kamini Finance and Investment Company Ltd. which had been purchased in the earlier year were sold during the year ending 31.03.1998 at ₹2/- each and a further losses aggregating ₹11,48,950/- were booked by the assessee.

24. During the year ended 31.03.1998, the assessee purportedly purchased the shares of Sangrahalaya Timber and Crafts Limited, Doyang Wood Products Ltd. and North Eastern Publishing & Advertising Company Limited. The memos of confirmation relied upon by the assessee reflect that the shares of the abovementioned companies were purchased from Mr N.C. Jain on a principal to principal basis. These transactions were not through stock exchange; the certificate produced by the assessee from the Gauhati Stock Exchange indicates that these transactions were *"off the floor transactions"* and were merely informed to the said stock exchange. The assessee valued these shares at a fraction of its purchase price and claimed loss on account of diminution in their value. A statement indicating the losses claimed by the assessee on the reduction of value of shares for the year ended 31.03.1998 relevant to assessment year 1998-99 is indicated below:-

NAME OF THE SCRIPTS	SHARE		PURCHASE	LOSS
	No. of shares	Rate (₹)	Amount (₹)	Amount (₹)
Sangrahalaya Timber and Crafts Limited	2750000	10.00	27500000	21312500
Doyang Wood Products Ltd.	640000	10.00	6400000	4800000
North Eastern Publishing & Advertising Company Ltd.	3500000	10.00	35000000	26250000
Total				52362500

25. In addition to the above, the assessee also claimed a loss of ₹1,12,500/- on account of diminution in the value of 37,500 shares of

Mather & Platt India Ltd. as on 31.03.1998. Thus, the total loss claimed by the assessee for the year ended 31.03.1998 was ₹5,36,23,950/- out of which ₹11,48,950/- was loss on account of sale of shares and ₹5,24,75,000 on account of diminution in value of shares.

26. During the year ended 31.03.1999, relevant to assessment year 1999-00, the assessee sold the shares held in Sangrahalaya Timber and Crafts Ltd. and Premier Auto Finance Ltd. at their book value i.e. at the rate ₹ 2.25 each. The shares of North Eastern Publishing and Advertising Company Ltd. were purportedly sold at a loss of ₹7,00,000/- and the shares of Doyang Wood Products Ltd. were purportedly sold and a loss of ₹1,92,000/-.

27. The assessee purchased 86,85,000 shares of Hotahoti Wood Products Ltd. at the rate of ₹10/- each, the details of which are as under:-

Name of Seller	No. of shares	Date	Value
Purbanchal Prestressed Ltd.	50,00,000	14.05.1998	5,00,00,000
Sangrahalaya Timber and Crafts Limited	36,85,000	13.05.1998	3,68,50,000

28. Out of the aforementioned, 82,16,750 shares of Hotahoti Wood Products Ltd. were purportedly sold for an aggregate amount of ₹2,46,50,250/- thus resulting in a loss of ₹5,75,17,250/-. Out of these shares 66,29,850 shares were sold to Mr N.C. Jain. The balance shares were sold to Toko Fin & Associates, P.L. Mittal, Doyang Wood Products Ltd., Sangrahalaya Timber and Crafts Ltd., Kamini Finance and Investment

Company Ltd. The certificate produced from the Gauhati Exchange Ltd. also indicates that none of the transactions were through stock exchange but were off market transactions and were merely reported to the stock exchange.

29. It is apparent from the above that the shares of companies in respect of which losses were booked were floated by Mr R.R. Modi by introducing his undisclosed income. The assessee had not only purchased shares of the companies floated by Mr Modi but had also purchased and sold shares of the said companies. In addition, the said companies also held substantial shares of the assessee.

30. In our view, the facts as outlined by the AO clearly indicate an established link between the companies floated by Shri R. R. Modi and the assessee. This fact has also not been disputed by the assessee in the present proceedings. The AO found that the shares of those companies were not actively traded; there is no material on record, which would indicate otherwise. The certificate of Gauhati Stock Exchange enclosed by the assessee in the paper book filed in ITA 3763/Del/2007 (i.e. in respect of assessment year 1997-98) is dated 12.02.2000. The said certificate does not indicate the volume of shares traded but only indicates quotation of shares on certain dates. The only inference that can be drawn is that there was no trading on other dates and this confirms the view that there was hardly any trading on the shares of the company in question. Since the shares in question are not actively traded, their quotations at the Stock Exchange could easily be manipulated by showing transaction in small number of shares. And, in any case would not be reflective of their value. The stock

certificates of Gauhati Stock Exchange for the assessment years 1998-99 and 1999-00 also indicate that the traded prices related to off the floor transactions which were reported to the exchange. Thus, the transactions entered into by the assessee and/or the related entities were itself the basis of the quotations; obviously, no reliance could be placed on these quotations for justifying the value of the shares in question. Since the companies in question had been floated by Shri R. R. Modi and share application money was introduced through other names, it is obvious that he owned/controlled a good part of the share holding. The shares, which are alleged to have been purchased by the assessee, were not paid for and only book entries were passed. Although, it is stated that the shares were through a broker of the Guwhati Stock Exchange. There is no evidence to show that the transaction of purchase of shares was done through the Gauhati Stock Exchange. On the contrary, the certificates issued by the Gauhati stock exchange put it beyond any pail of doubt that the transactions in question were "off the floor transaction".

31. The inescapable conclusion is that through a series of transactions - which were, essentially, book entries - the assessee had devised a loss to set off against its other income. In our view, the AO's reasoning that the transactions were not genuine was based on cogent material and after examining the entire facts.

32. The CIT(A) set aside the assessment orders, without considering the above facts but by simply relying on the following decisions:-

> "CIT Vs Dhawan Investment and Trading Co. Ltd. (1999) 238 ITR 486 (Cal);

CIT Vs Currency Investment Co. Ltd. (2000) 244 ITR 494 (Cal);

CIT Vs Carbo Industrial Holdings Ltd. (2000) 244 ITR 422 (Cal);

CIT Vs Kundan Investment Ltd. (2003) 263 ITR 626: &

CIT Vs Janki Textiles & Industries Ltd.(2003) 132 Taxman 231 (Gau)."

33. The CIT(A) failed to consider any of the reasons provided by the AO for holding the transactions to be not genuine; CIT(A) did not address any of the following aspects.

a) That the assessee company and the companies whose shares were bought by the company were interlinked. The companies in question owned shares of the assessee company. Mr R. R. Modi who was a Director of the assessee company was also closely connected with the companies in question. These companies owned shares of the assessee and also had entered into transactions with the assessee.

b) Even though the companies in question may have been listed on the Gauhati Stock Exchange, their shares were not actively traded and the transactions were amongst inter related parties. Thus, the quotations reflected on the Gauhati Stock Exchange could not be relied upon to reflect their value.

c) There was no evidence produced to show that Shri Nem Chand Jain who is stated to have funded the purchase of shares by the assessee, had any means to do so. The AO had found that Shri Nem Chand

Jain was not a man of means. The assessee had produced no evidence to contradict this.

d) Admittedly, the transactions were done by book entries and no payment was made for the purchase of shares during the year.

34. In our view, the aforesaid aspects were important and clearly indicated that the transactions entered by purchase and sale of shares were, in fact, sham transactions and could not be relied upon. The CIT (A) failed to apply its mind to the aforesaid aspects and therefore, in our view, the orders passed by the CIT(A) were clearly unsustainable.

35. Given the facts of this case, the decisions referred to by CIT(A) are also, plainly, not applicable. In case of ***Janki Textiles and Industries Ltd.*** *(supra)*, there was no allegation that payments for the shares in question had not been made and the transaction consisted of only book entries. On the contrary, the Court found that all payments had been made and received through account payee cheques and/or drafts. In that case, the Court specifically noted that no evidence was placed by the Revenue to indicate that the disputed share transactions were entered into between parties that were related or had common interest. In the present case, the AO had clearly brought on record that the transactions were of companies that were linked with the assessee company. The companies in question were promoted by one Mr R.R Modi who was also a Director of the assessee company. The shares of assessee company were also held by some of the companies whose shares had been purchased by the assessee. The AO had further found that Mr N.C. Jain was not a person of means and his declared

income was only ₹40,000/- by way of salaries. The assessee sought to dispute this by producing a balance sheet of Mr N.C. Jain. However, that also indicated that he owed a large sum of money - ₹7.5 crores to his creditors. There was no finding as to the net worth of Mr. N.C. Jain. In addition to the above, no payment had been made for the purchase of shares during the relevant period. Mr N.C. Jain was stated to be a broker. No explanation was provided as to why a broker would extend credit without any interest. The explanation given by the assessee was that the assessee was undergoing financial crises and, therefore, although it owed the money to N.C. Jain, it could not discharge its debts at the material time. Even if this is accepted, there is no plausible explanation why despite not being paid for the shares sold, Mr N.C. Jain would continue to sell and deliver further shares to the assessee, specially when he knew the assessee to be financially constrained. Shri NC Jain is stated to have sold shares for ₹6,89,00,000/- in the year ended 31.03.1998 thus swelling his outstanding credit to ₹12,22,57,950/- as on 31.03.1998 after adjusting ₹60,600/- on account of shares purportedly purchased by Sh. N. C. Jain.

36. In our view, the CIT(A) completely ignored the aforesaid facts and merely cited the judgments where contract notes had been accepted as evidence of genuine transaction. Undoubtedly, contract notes, confirmation memos, bills, books of accounts are evidence of genuine transactions. However, where the fundamental transaction is shown to be a sham transaction, the same cannot necessarily be accepted as genuine merely because a broker's confirmation and invoices have been produced. In our

view, the CIT(A) erred in the applying the decision in ***Janki Textiles*** *(supra)* in the facts of this case.

37. In ***Cargo Industrial Holdings Ltd.*** *(supra)*, the Court upheld the decision of the Tribunal in accepting the transactions in shares to be genuine as the assessee had furnished the names and addresses of brokers and also shown payments made to them by account payee cheques. The companies whose shares were subject matter of transaction were blue chip companies and extensively traded on the stock exchange. The Revenue had rejected the transactions only on the ground that the assessee could not produce certain brokers. The Court held that even if the share brokers did not appear the claim of the assessee could not be denied as neither the existence of the broker nor the payments made to them were in dispute. The Court held that the assessee could not be punished for fault of the broker.

38. In ***Dhawan Investment and Trading Co. Ltd.*** *(supra)*, the AO had disallowed a loss on account of purchase and sale of shares on the ground that the record was inadequate in respect of the share dealings. The said conclusion was rejected by the Tribunal as it found that the transactions were genuine and made through registered brokers. There was no allegation that the consideration for the sale and purchase was not paid through banking channels or that the transactions in question concerned related companies.

39. In ***Kundan Investment Co. Ltd.*** *(supra)*, the Court found that the sale and purchase transactions, which were questioned by the Revenue, were in

respect of shares of reputed companies which were quoted on the stock exchange. The transactions were supported by contract notes and bills and the payments made through cheques. The Calcutta High Court did not find the decision of the Tribunal to be perverse in the given facts.

40. It is apparent from the above that the aforesaid decisions have no application in the facts of this case. The factual controversy involved in these appeals is materially different from the issues involved in the cases referred by the CIT(A).

41. In our view, the Tribunal also erred in upholding the orders of CIT(A) and failed to consider the controversy in issue. The Tribunal proceeded on an erroneous footing that all shares have been *"bought through the recognised stock exchange through the main broker of the exchange"*. There was no evidence to indicate that all shares were bought through the stock exchange. The assessee also did not claim this; the assessee had claimed before the AO that all shares were *"bought from the broker of Gauhati Stock Exchange"*. In the submissions filed before the AO, the assessee contended that *"the transaction for purchase of shares were carried out by the assessee company through main broker of Gauhati Stock Exchange"*. Thus, it was not the assessee's claim that all shares were purchased through the Gauhati Stock Exchange. This aspect is material as, admittedly, the transactions in question could not have been made through Gauhati Stock Exchange. In case of transactions through a stock exchange the selling broker is required to submit the share scrips with the clearing system of the stock exchange. The purchasing brokers are required to pay the consideration on the "pay in date". The consideration for the shares

transacted through the stock exchange is paid to the selling broker on the "pay out date". Thus, in cases of transaction through a stock exchange a purchasing broker is required to deposit the consideration with the clearing system of the stock exchange. However, in the present case bulk of the shares in question were claimed to have been sold/purchased by Mr N.C. Jain. The memos of confirmations by Mr N.C. Jain in respect of shares purportedly purchased by the assessee indicate that Mr N.C. Jain had sold the shares to the assessee. Similarly the memos of confirmation regarding the shares purportedly purchased by the assessee reflected that the shares had been sold by Nem Chand Jain to the assessee. These memos of confirmations were not contract notes evidencing purchase or sale of shares by Mr N.C. Jain through the stock exchange for and on behalf of the assessee. In case, Mr N.C. Jain had purchased the shares through the stock exchange for the assessee, in the normal course, he would have issued a contract note indicating the shares bought for the assessee. The assessee had also produced bills from Mr N.C. Jain evidencing sale of shares to the assessee. These documents produced by the assessee clearly indicated that the transactions for purchase of shares were not being claimed as transactions done through the stock exchange. The AO had, therefore, found and in our view rightly so, that the transactions were not through the stock exchange.

42. The AO had also found that the shares of companies in question were listed on spot basis i.e. the transactions on the stock exchange in respect of shares in question were required to be settled on the day of the trade itself.

However, in the present case, the assessee had admittedly not made payment for the said shares and this was contrary to the prevalent practice.

43. Thus, the finding of the Tribunal, to the effect that all shares were transacted through Gauhati stock exchange, is not supported by any material and is perverse. The Tribunal held that *"All documentary evidences itself prove that assessee had bought/sold these shares at the prevailing market price and based on the same, the genuineness of the transactions could not be doubted"*. This finding is also patently erroneous.

44. None of the material produced by the assessee could be relied upon to indicate the market value of the shares. The certificates issued by the Gauhati Stock exchange for the previous years 1997-98 and 1998-99 certified the *"traded prices of the shares.. as intimated by a member as off the floor transactions"*. This, clearly, indicated that: (a) the transactions were not conducted through the stock exchange but merely reported as off market transactions; and (b) the transaction was reported by a singular member – thus, the transaction did not involve any other broker. Further the dates and quotations certified, clearly pertained to the transactions involving the assessee and or related companies as parties. The dates of the memos of confirmation and the date of transaction reported to the stock exchange are the same in almost all instances. Thus, these certificates, which only certify the prices at which transactions in question were reported cannot prove that the transactions were executed at market value. Since these transactions in question were not done in open market, but between related concerns and no other transactions in those shares were

reported, any price at which the assessee transacted would, obviously, be reflected as a quotation by the Gauhati Stock Exchange.

45. The AO had found that Mr N.C. Jain was not a person of means. His returns disclosed income of ₹40,000 by way of salaries. The Tribunal rejected the AO's finding that N.C. Jain was not a person of means by holding that the issue of Mr N.C. Jain creditworthiness was covered by the Tribunal's order dated 19.10.2004. A perusal of the said order indicates that the Tribunal had noted the following submission on behalf of the assessee:-

> "Shri Vohra also drew our attention to the audited balance sheet of Shri N.C. Jain (Pages 64 to 67 of the Paper Book) to show that Mr. Jain was man of means having a closing stock of shares worth Rs.1.70 crores and a liability of Rs.7.50 crores to its creditors."

However the Tribunal did not return any finding on the question of Mr N.C. Jain's creditworthiness. In our view, the Tribunal grossly erred in holding that this issue was covered by its earlier decision of 19.10.2004.

46. The Tribunal has held that the amount payable to Mr N.C. Jain had been discharged by the assessee in the year 2005-06 and, therefore, found that the transactions in question were genuine. It is relevant to note that Mr N.C. Jain had expired in the year 1999 and the material placed on record indicated that he was not a person of means and had been acting at the instance of Mr R.R. Modi. Mr R.R. Modi had created several entities which were involved or connected with the transactions in question. In the circumstances, the payment of money to Mr N.C. Jain was required to be investigated further to ascertain as to the ultimate recipient of those funds.

No such exercise has been done in this case. Thus, in our view, the fact that certain payments were shown to have been made to Mr N.C. Jain in 2005-06, would not be sufficient to conclude that the transactions in question were genuine.

47. The AO had found that the assessee and the companies whose shares purchased were related. It was pointed out that those companies were promoted by Mr Modi who had disclosed that he had used his undisclosed funds to promote those companies. The assessee had argued that the fact that undisclosed funds were used in promoting companies did not mean that the companies did not carry on its business or were not genuine. However, it was apparent that Mr Modi was the prime mover of the companies in question. The assessee had booked losses in respect of shares of certain companies. The close link between the said companies and the assessee was clearly established. In our view, the link established between the assessee and these companies was important in considering the question whether the transactions of shares were genuine or not. It is relevant to take note of the following:-

(a) That the assessee had booked losses in respect of shares of the following companies:-

(i) Sangrahalaya Timber & Crafts Ltd.

(ii) Matther & Platt India Ltd.

(iii) Hotahoti Wood Products Ltd.

(iv) Purbanchal Presstressed Ltd.

(v) Kamini Finance & Investment Co. Ltd.

(vi) M/s Doyang Wood Products Ltd.

(vii) M/s North Eastern Publishing & Advertising Co. Ltd.

Out of the above companies, all except Mather & Platt India Ltd. were companies promoted by Mr R.R. Modi by introduction of his undisclosed funds as share application money in various names.

(b) The fact that the share application money was introduced in different names by Mr R.R. Modi indicates that although there may have been a number of shareholders, the *de facto* control of the companies as well as its shares vested with Mr R.R. Modi.

(c) Sh. R.R. Modi was also a Director of the assessee company.

(d) The aforesaid companies also held substantial shares of the assessee.

(e) The assessee had not only dealt with shares of the aforementioned companies but also had purchased certain shares from some of the companies.

(f) Although the shares of these companies were listed, there is no evidence that the shares were traded through the stock exchange or there was any other genuine transaction not involving these companies, the assessee and the named brokers.

(g) The AO had found that *"except the assessee's own transaction the value of shares were never quoted at the Guwahati Stock Exchange on any other date"*.

48. In view of the above, the AO had further concluded that *"the purchases of shares and valuation was done through series of steps involving inter-related companies, which accommodated one another and made fictitious dealing through convenient book entries in their respective books of accounts"*

49. In our view, the Tribunal grossly erred in completely ignoring the aspect of inter linked entities and overlooking the perspective outlined by the AO.

50. Insofar as the loss in relation to shares of Mather & Platt India Ltd. is concerned, there is no allegation that the assessee is related in any manner to the said company. In this view, the losses as claimed by the assessee in respect of Mather & Platt India Ltd. cannot be rejected. The losses claimed by the assessee, except the losses relating to the shares of Mather and Platt India Ltd. i.e. ₹56,650/- in the assessment year 1997-98, ₹1,12,500 in the assessment year 1998-99; and ₹67,500/- in the assessment year 1999-00, are liable to be disallowed.

51. We find that the Tribunal erred in ignoring certain relevant facts and its finding that transactions for purchase and sale of shares are genuine, is perverse. Accordingly, the question of law as indicated in paragraph 5 above, is answered in the affirmative and in favour of the Revenue.

52. The appeals are allowed. No order as to costs.

VIBHU BAKHRU, J

S. RAVINDRA BHAT, J

APRIL 30, 2015
MK/RK

HIGH COURT OF DELHI
सत्यमेव जयते