Commissioner of Income Tax, Gujarat III Vs Arvind Narottam Lalbhai Dalpatbhai Vada

Income-tax Reference No. 52 of 1974 with Income Tax Application No. 46 of 1975

Court: Gujarat High Court

Date of Decision: Oct. 6, 1975

Acts Referred:
Income Tax Act, 1961 â€" Section 22, 23, 23(1), 23(2), 24(1)

Citation: (1976) 105 ITR 378

Hon'ble Judges: B.J. Divan, C.J

Bench: Single Bench

Advocate: K.H. Kaji, for the Appellant; J.P. Shah, for the Respondent

Judgement

Divan, C.J.
In this reference at the instance of the revenue, the following question has been referred to us by the Tribunal :

Whether, on the facts and in the circumstances of the case, the Tribunal was justified in law in holding that while calculating the annual letting value

of the property in question in the occupation of the owner for the purpose of his residence, municipal taxes have to be deducted ?

2. At the time when the revenue applied for reference to the High Court. The questions for which the reference was sought were four in all. The

other three questions which the Tribunal declined to refer to the High Court were :

(1) Whether, on the facts and in the circumstances of the case, the bonus shares in respect of ordinary shares held by the assessee in the company

must be valued spreading the cost of the old shares over the old shares and the bonus shares taken together as both rank pari passu, as held by the

Supreme Court in Commissioner of Income Tax v. Dalmia Investment Co. Ltd. ?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal erred in law in holding that the ratio of the decision of the Supreme

Court in Shekhawati General Traders Ltd. v. Income Tax Officer applied to the facts of this case ?

(3) Whether, on the facts and in the circumstances of the case, the loss computed by the Appellate Assistant Commissioner of Income Tax and

confirmed by the Tribunal on the sale of bonus shares held by the assessee in the company was erroneous in law ?

3. The Commissioner of Income Tax has applied by the Income Tax application, which we are now disposing of, that the three questions which

were not referred by the Tribunal on the ground that they were questions of fact and application of law in the light of the facts of the particular case,

particularly the law as explained by the Supreme Court in Commissioner of Income Tax v. Dalmia Investment Co. Ltd., and Shekhawati General

Traders Ltd. v. Income Tax Officer, to direct the Income Tax Appellate Tribunal to draw up a statement of the case and to raise and refer to this

court the three questions which the Tribunal declined to refer. Since both these matters arise out of one and the same order of the Tribunal, we will

dispose of both the matters by this common judgment.

4. The assessment year under consideration is 1965-66. The assessee is an individual and he derives income from property, business. Dividend

and directors'' fees. During the year under reference the assessee claimed capital loss of Rs. 95,371 in respect of investment in shares. This loss,

inter alia, included capital loss of Rs. 1,01,100 on sale of 700 shares of Raipur Manufacturing Co. Ltd. The Income Tax Officer noticed that prior

to January 1, 1954, the assessee was holding 620 shares in this company and he, therefore, accepted the contention of the assessee that he was

entitled to substitute fair market value as on January 1, 1954, as the cost of acquisition of the said 620 shares. The Income Tax Officer, however,

observed that after January 1, 1954, the assessee received 1,860 bonus shares in the ratio of three bonus shares per every on share held by him.

Thus, the total shares held by him before the beginning of the previous year relevant to the year under reference was 2,480 shares, that is 620

original plus 1,860 bonus shares. The assessee contended before the Income Tax Officer that for the purpose of the capital gains, the fair market

value as on January 1, 1954, of Rs. 670 per share should be substituted as cost u/s 55(2) of the Income Tax Act, 1961. Ultimately, what the

assessee was claiming was that the market value of 620 shares at Rs. 670 per share as on January 1, 1954, was Rs. 4,15,400. The value of 80

bonus shares, according to the assessee, was nil and taking the sale price of 700 shares at Rs. 449 per share, that is, Rs. 3,14,300, the capital loss

which was claimed in connection with these 700 shares was Rs. 1,01,100. The Income Tax Officer rejected the claim of the assessee regarding

the mode of calculating the capital loss and, according to the Income Tax Officer, the fair market value of 700 shares taken together as on January

1, 1954, at Rs. 167.50 per share came to Rs. 1,17,250 and he, therefore, computed capital gain at Rs. 1,97,050. The assessee took the matter in

appeal before the Appellate Assistant Commissioner who determined the capital loss at Rs. 1,01,900. The market value of 620 shares as on

January 1, 1954, was held to be Rs. 4,15,400. The Appellate Assistant Commissioner held that remaining 80 shares out of the 700 shares which

were sold during the relevant year were bonus shares received by the assessee after January 1, 1954. He ascertained that originally the assessee

had acquired 248 shares at the cost of Rs. 24,800 and between the date of the original issue and January 1, 1954, 372 bonus shares were issued

with the result that the 248 shares originally held by him had become 620 shares (248 plus 372). Therefor, the Appellate Assistant Commissioner

took the cost of 80 bonus shares at Rs. 10 per share, that is Rs. 24,800 original cost of acquisition, spread over the total of 2,480 shares held on

the first day of previous year and he added the cost of these 80 bonus shares, that is, Rs. 800 to the market value of 620 shares as on January 1,

1954. Thus, he calculated the total value of 700 shares (620 plus 80) at Rs. 4,16,200 and deducting the sale proceeds of Rs. 3,14,300 from this

figure, he ascertained the capital loss at Rs. 1,01,900. The matter was carried in appeal before the Tribunal and the Tribunal, following the decision

of the Supreme Court in Shekhawati General Traders Ltd. v. Income Tax Officer, rejected the contention of the revenue that the cost of

acquisition on the basis of substituted value as on January 1, 1954, under the provisions of section 55(2) of the Act has to be calculated by

averaging the value of original shares and bonus shares taken together, even though the bonus shares were issued after January 1, 1954. The first

three questions which all arose out of this part of the decision of the Tribunal were not referred to this High Court and the question is, whether we

should issue any directions in the Income Tax application regarding these three questions pertaining to the bonus issue.

5. In Commissioner of Income Tax v. Dalmia Investment Co. Ltd., the Supreme Court held that where bonus shares are issued in respect of

ordinary shares held in a company by an assessee who is a dealer in shares, their real cost to the assessee cannot be taken to be nil or their face

value. The majority of the learned judges constituting the Bench held that these shares have to be valued by spreading the cost of old shares over

the old shares and the new issue (viz., the bonus shares) taken together if they rank pari passu, and if they do not, the price may have to be

adjusted either in proportion to the face value they bear (if there is no other circumstance to differentiate them) or on equitable considerations

based on the market price before and after issue. The Tribunal has found that the bonus shares issued in this company were to rank pari passu and,

therefore, the Appellate Assistant Commissioner and the Tribunal have accepted the contention of the assessee that the 80 bonus shares which

were the balance of the 700 shares should be valued at Rs. 10 per share. Even the 620 shares were not the original shares. Those 620 shares

consisted of 248 original shares and 372 bonus shares. Therefore, the original cost of acquisition of the old shares or the original 248 shares,

namely, Rs. 24,800 had to be spread over the total number of shares as the commencement of the previous year and it seems to us that all that the

Appellate Assistant Commissioner and the Appellate Tribunal have done in this case is to apply the principle laid down by the Supreme Court in

Commissioner of Income Tax v. Dalmia Investment Co. Ltd., to the facts of this case and once it is found, as a matter of fact, that the old shares

and the new shares were to rank pari passu, the only way the cost of 80 bonus shares could have been ascertained was in the manner in which the

Appellate Assistant Commissioner made his calculations. Under these circumstances it seems to us that the Tribunal was right in declining to refer

the three questions arising out of the sale of the 700 shares and the valuation of the 80 bonus shares. We, therefore decline to issue any directions

to the Tribunal regarding the three questions which were not referred and in respect of which Income Tax Application No. 46 of 1975 has been

made to this court. Rule issued, the Income Tax application of July 7, 1975, is, therefore, discharged with no order as to costs.

6. Coming to the question which is actually referred to us, the facts are that the assessee occupies his own property for the purposes of his

residence and the question before the Income Tax Officer, the Appellate Assistant Commissioner and the Tribunal was whether the assessee could

claim deduction on account of municipal taxes from the annual letting value of the property on which the Income Tax is to be charged.

7. The Tribunal following its own earlier decision in Income Tax officer, Group Circle II(1), Ahmedabad v. Hansa Niranjan, Ahmedabad, came to

the conclusion that while computing the annual letting value of the property in occupation of the owner, for the purpose of his residence, municipal

taxes were deductible. It is in these circumstances that the question set out hereinabove came to be referred to us.

8. In order to appreciate the rival contentions it is necessary to set out in verbatim the provisions of sections 22 and 23 of the Income Tax Act,

1961, since they relate to income from house property. u/s 22, income from house property is to be calculated in the following manner :

The annual value of property consisting of any buildings or lands appurtenant thereto of which the assessee is the owner, other than such portions

of such property as he may occupy for the purposes of any business or profession carried on by him the profits of which are chargeable to Income

Tax under the head ''Income from house property''.

9. u/s 23 provision is made regarding determination of the annual value and under sub-section (1) it is provided -

For the purposes of section 22, the annual value of any property shall be deemed to be the sum for which the property might reasonably be

expected to let from year to year :

Provided that where the property is in the occupation of a tenant and the taxes levied by any local authority in respect of the property are, under

the law authorising such levy, payable wholly by the owner, or partly by the owner and partly by the tenant, a deduction shall be made equal to the

part, if any, of the tenant''s liability borne by the owner.

10. The rest of sub-section (1) of section 23 is not material for the purposes of this judgment. Sub-section (2) is in these terms :-

Where the property is in the occupation of the owner for the purposes of his own residence, the annual value shall first be determined as in sub-

section (1) and further be reduced by one-half of the amount so determined or one thousand eight hundred rupees, whichever is less.

11. The proviso to sub-section (2) is not material for the purpose of this judgment and the Explanation to sub-section (2) is in these terms :

Explanation. - Where any such residential unit as is referred to in the second proviso to sub-section (1) is in the occupation of the owner for the

purposes of his own residence, nothing contained in that proviso shall apply in computing the annual value of that residential unit.

12. u/s 24, sub-section (1), income chargeable under the head ""Income from house property"" shall, subject to the provisions of sub-section (2), be

computed after making the following deductions, namely :-

(i) in respect of repairs, -

(a) where the property is in the occupation of the owner, or where the property is let to a tenant and the owner has undertaken to bear the cost of

repairs, a sum equal to one-sixth of the annual value.

13. In order to appreciate the rival contentions, a brief history of the provisions relating to what is known in the language of taxation law as ""self-

occupied property"" should be set out here.

14. Under the Indian Income Tax Act, 1922 (hereinafter referred to as ""the 1922 Act""), in the Act as originally enacted, there was no provision

whatsoever till 1939 regarding deduction of municipal taxes and even after the 1939 amendments there was no provision for deduction of

municipal taxes. By the amendments which came into effect from assessment year 1950-51, it was provided that if a tenant was liable to pay the

taxes but the owner paid the taxes, deduction was to be granted and the fiction was that the tenant''s liability was to be one-half and there was no

deduction for self-occupied properties. By an amendment in 1953, the self-occupied properties also became entitled to deduction for municipal

taxes but a fiction was created in the statue by using the words ""as if the property was let"" and thus one-half of the taxes was to be deducted in

respect of self-occupied properties also as in the case of tenant-occupied properties. Thereafter, in 1955, the restriction which was in force till

then, namely, that deduction was not to exceed one-eighth of the annual letting value was remove. By the amendment of 1960 in respect of

properties constructed prior to April 1, 1950, full deduction of municipal taxes was to be granted and in respect of properties constructed after

April 1, 1950, one-half of the municipal taxes were to be deducted. Under the 1961 Act the provision in respect of tenant-occupied property is as

set out in sub-section (1) of section 23 and in respect of self-occupied property, under sub-section (2) of section 23, the annual value was to be

determined as in sub-section (1) and further be reduced by one-half of the amount so determined or one BXBD thousand eight hundred rupees,

whichever as less. Thereafter, with effect from April 1, 1969, an amendment was effected and by this amendment, the first proviso to section 23(1)

was recast and ful deduction was granted for the tenant-occupied property and under the new proviso where the property is in the occupation of a

tenant and the taxes levied by any local authority in respect of the property was to the extent such taxes are borne by the owner, to be deducted in

determining the annual value of the property. Thereafter, a further amendment was carried out which was to take effect with assessment year

1971-72 the sub-section (2) of section 23 has been amended and the words ""as if let"" have been substituted for the words ""as in sub-section (1)

so that the position so far as terminology is concerned is the same as prevailed since 1953 under the Act of 1922.

15. It must be stated at the outset that there is no direct authority of any High Court or of the Supreme Court which will throw any light on this

problem of construction which we have to deal with in the present case. However, some assistance is available from the decision of the Calcutta

High Court in Liquidator, Mahmudabad Properties Ltd. v. Commissioner of Income Tax. The Calcutta High Court has observed at page 477 of

the report :

We shall dispose of the question of municipal taxes as deductions at this stage. The relevant provision which governs this question of municipal tax

deduction is the proviso to section 23 of the Income Tax Act, 1961, whose crucial expression is ''provided that where the property is in the

occupation of a tenant''. It is only then, when such property is in the occupation of a tenant, that the municipal taxes can qualify for deduction in

determining the annual value of the property. The basic fact is wanting in the present reference. This property, 3, Gun Foundry Road, was not in

the occupation of a tenant within the meaning of those words in the proviso to section 23 if the Income Tax Act, 1961. We have already discussed

the finding on record that the property was not let at the relevant time. That finding binds us. Besides, the facts show, as we have indicated, that the

property was requisitioned by the Government and was there question before the assessment in question and in any event in the case of such a

requisition, under the West Bengal Premises Requisition and Control (Temporary Provisions) Act, 1947, the Government by requisition does not

become a tenant and it is not a letting. We would also like to emphasise that both vacancy remission and deduction of municipal taxes cannot be

claimed at the same time by reasons of the language in the proviso to section 23 of the Income Tax Act, 1961, as quoted above. That is one of the

basic contradictions in the case made by Mr. Mitter, learned counsel for the assessee. The second fundamental contradiction in the assessee''s

case on this point has been that in one breath the assessee claims vacancy remission and in the other breath claims that there is no annual value for

this property. The quantum of vacancy remission will ipso facto or ex hypothesis mean the proportionate amount of rent which would normally,

though not conclusively, be the annual value. Therefore, we hold that municipal taxes cannot be deducted in the facts and circumstances of this

reference.

16. The problem before the Calcutta High Court was not in respect of property occupied by the assessee for his own residence but it was pointed

out that under sections 22 and 23 what is charged is the annual value of the property. That annual value is deemed to be the sum for which the

property might reasonably be expected to let from year to year. These are deeming provisions and are based on the idea of hypothetical tenancy.

These provisions also show that the property has to be considered as it is at the time of the determination of its annual value. The impact of section

23(2) which provides for self-occupied property for purpose of residence was not considered by the Calcutta High Court and we will have to

apply the well-known canons of construction to the provisions of sub-section (2) of section 23 in order to decide the question before us.

17. In the proviso to sub-section (1) of section 23, as it stood at the relevant time, the deduction of municipal taxes was to be granted where the

property was in the occupation of a tenant and the taxes levied by any local authority in respect of the property were, under the law authorising

such levy, payable wholly by the owner or partly by the owner and partly by the tenant, then the deduction was to be made equal to the part, if

any, of the tenant''s liability borne by the owner. By virtue of the Explanation, for the purposes of the sub-section, in the case of a property the

construction of which was completed before April 1, 1950, total amount of such taxes and in the case of any other property, one-half of the total

amount of such taxes shall be deemed to be the tenant''s liability. By virtue of this fiction created by the Explanation, the whole of the total amount

of the taxes paid to the local authority in respect of the property in the occupation of the tenant was top be deducted because that was deemed to

be the tenant''s liability and it is, therefore, clear that in the light of the proviso read with the Explanation, since the particular property was

constructed before April 1, 1950, if the property had been occupied by a tenant, the whole amount of municipal taxes were to be deducted from

the annual letting value for the purpose of arriving at the annual value of the property. The words which require interpretation in section 23(2) are

two phrases : the first phrase being ""the annual value shall first be determined as in sub-section (1)"" and the second phrase is ""and further be

reduced by one-half of the amount....."" Therefore, the question that we have to ask ourselves is as to what is meant by the words ""determined as

in sub-section (1)"". It is obvious that what the main part of sub-section (1) provides for is the determination of the annual value of all properties,

whether tenant-occupied or self-occupied, and by the main body of sub-section (1) of section 23, the annual value of any property is to be

deemed to be the sum for which the property might reasonably be expected to let from year to year. This notional or hypothetical annual letting

value is the annual value and if any taxes of any local authority are paid, then as laid down in the proviso read with the Explanation as it stood prior

to April 1, 1969, the whole or half of the municipal taxes were to be deducted depending upon whether the property was constructed before April

1, 1950, or after April 1, 1950. But the proviso and the Explanation only applied in the case of property in the occupation of a tenant and under

the proviso to sub-section (1) the requirements for the occupation of a tenant; (2) the taxes levied by the local authorising such levy payable wholly

by the owner or partly by the owner and partly by the tenant; and (3) the deduction was to be made equal to the part, if any, of the tenant''s liability

borne by the owner and by the legal fiction created by the Explanation, the whole or half of the municipal taxes were deemed to be the tenant''s

liability. It is obvious that, on the face of it, if a mere prima facie view were to be taken, the condition about deduction of the municipal taxes laid

down in the proviso to sub-section (1), namely, that the property should be in the occupation of a tenant, would not apply to property in the

occupation of the owner for the purpose of his own residence and there is a great deal of substance in the submission made by Mr. Kaji that the

words ""shall first be determined"" as in sub-section (1) refer to the main body of sub-section (1) and not to the proviso because it would be a

contradiction in terms to say that the property which is in the occupation of the owner himself for the purpose of his own residence, shall be treated

as if it were in the occupation of a tenant without there being a legal fiction. If the words are ""as determined in sub-section (1)"", then the main body

of sub-section (1) will only apply, namely, that the annual value should be considered to be the same for which the property could reasonably be

let from year to year.

18. However, we must also take notice of the words ""and further be reduced"". The words ""further be reduced"" indicate that some reduction from

the annual letting value has already been carried out before further reduction contemplated by sub-section (2) of section 23 can be considered and

that further reduction can only be of the municipal taxes as contemplated by the proviso to sub-section (1) read with the Explanation to that

proviso. There is no other meaning that can possibly be attached to the words ""further be reduced"". If these words had not been there in sub-

section (2), we would have had no hesitation in accepting the contention urged on behalf of the revenue by Mr. Kaji. However, sub-section (2) of

section 23 must be read as a whole and in the light of the words ""further be reduced"". It must be held that some reduction, namely, the deduction

of the municipal taxes, half or full, as the case might be, has to be first carried out and, thereafter, the reduction contemplated by sub-section (2),

namely, one-half of the amount so determined or one thousand eight hundred rupees, whichever is less, has to be carried out. It is, therefore, clear

that by the use of the words ""further be reduced"", the legislature has clearly indicated that the deduction of municipal taxes contemplated by the

proviso and the Explanation to sub-section (1) as they existed prior to April 1, 1969, has to be made and, thereafter, the amount so determined

has to be further reduced as contemplated by sub-section (2) of section 23, so far as self-occupied properties are concerned.

19. Under these circumstances the conclusion reached by the Tribunal regarding the legal effect of section 23, sub-section (2), in respect of self-

occupied property is correct and it must be held that the Tribunal was right in law in holding that while calculating the annual letting value of the

property in question in the occupation of the owner for the purpose of his residence, municipal taxes have to be deducted. We, therefore, answer

the question referred to us in the affirmative and against the revenue. The Commissioner will pay the costs of this reference to the assessee.