

F. Hoffman-la Roche and Co. Ltd. Vs. Inspecting Assistant

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Court : Income Tax Appellate Tribunal ITAT Mumbai

Decided On : Jan-20-1988

Reported in : (1988)27ITD17(Mum.)

Judge : R Garg, L Aggarwal

Appellant : F. Hoffman-la Roche and Co. Ltd.

Respondent : inspecting Assistant

Judgement :

1. This is an appeal by the assessee against the order of the Commissioner of Income-tax (Appeals) for the assessment year 1980-81.

The only point involved in this appeal is about the determination of the cost of acquisition of the bonus shares acquired by the assessee after 1-1-1964.

2. The assessee acquired 160 shares of Anglo-French Drug Co. (Eastern) Ltd. in November 1959 at the rate of Rs. 12,000 per share, the total cost being Rs. 19,20,000. In July 1979, the assessee received 38,240 bonus shares in the ratio of 239: 1. Out of these bonus shares, the assessee had sold 13,600 shares on 31-8-1979 to the financial institution at the rate of Rs. 50 per share with the approval of the Reserve Bank of India, In order to find out the cost of acquisition of these bonus shares the assessee has divided the market value of the original shares as on 1-1-1964 by the total number of shares, i.e., 38,400 (160 original shares plus 38,240 bonus shares). The average price so worked out was claimed to be the

cost of acquisition while computing the income under the head 'Capital gains'. The assessing officer observing that the shares sold were only bonus shares which were allotted to the assessee in July 1979, held that the assessee could not claim the benefit of Section 55(2) of the Income-tax Act. He, therefore, worked out the average cost of bonus shares in the light of the decision of the Supreme Court in the cases of CIT v. Dalmia Investment Co. Ltd. [1964] 52 ITR 567 and CIT v. Gold Mohore Investment Co. Ltd. [1969] 74 ITR 62 by spreading over the price paid on the acquisition of the original shares divided by the total number of the shares. The Commissioner of Income-tax (Appeals) has rejected the appeal of the assessee and held that the assessee was not entitled to the option of substituting the fair market value as on 1-1-1964 in accordance with the provisions of Section 55(2)(i) of the Income-tax Act since the bonus shares, which were sold in the previous year relevant for the year under consideration, were not acquired by the assessee prior to 1-1-1964. Aggrieved by the order of the Commissioner of Income-tax (Appeals), the assessee is in appeal before us.

3. The learned counsel for the assessee, Shri T. Pooran, submitted that the Commissioner of Income-tax (Appeals) has proceeded altogether in a wrong direction. The question in dispute before him was not whether the assessee could substitute the market value of the bonus shares as on 1-1-1964, but whether the assessee was entitled to work out the average cost of acquisition of the bonus shares by adopting the market value of the original shares as on 1-1-1964 and dividing the same by the total number of shares. He further submitted that by the decision of their Lordships of the Supreme Court in the case of Dalmia Investment Co.

Ltd. (supra), the bonus shares are to be valued by spreading the cost of the old shares over the old and the new shares (namely, bonus shares) taken together. The cost of acquisition which according to him is to be taken into consideration in arriving at the average price is the cost of acquisition as defined in Section 55(2)(i) of the Act, which provides that where the capital asset became the property of the assessee before the 1st day of January, 1964, the cost of acquisition means the cost of acquisition of the assets to the assessee or the fair market value of the assets as on the 1st day of January, 1964 at the option of the assessee. The case

of the revenue, on the other hand, is that the substitution of the fair market value of the assets in place of its cost of acquisition is only in relation to the original shares and that is available only if they are sold. This substituted market price cannot be taken into consideration in arriving at the average cost of acquisition when the bonus shares are sold.⁴ We have considered the rival submissions very carefully. What is the cost of acquisition for the bonus shares is not defined in the Income-tax Act. We, therefore, have to find its meaning with reference to the decided cases on the point. In the case of Dalmia Investment Co.

Ltd. (supra), their Lordships of the Supreme Court examined four possible methods for determining the cost of bonus shares. The first method is to take the cost as the equivalent of the face value of the bonus shares. The second method is that as the assessee pays nothing in cash for the shares, the cost should be taken as nil. The third method is to take the cost of the original shares and to spread it over the original shares and the bonus shares taken collectively and the fourth method is to find out the price of the original shares on the stock exchange and to attribute the same to the bonus shares. After considering at length their Lordships rejected the first two methods and held that if the bonus shares rank *pari passu* with the old shares they should be valued by spreading the original cost over the old and new shares and if the shares do not rank *pari passu* assistance may have to be taken of other evidences to fix the cost of the bonus shares and in such cases it might be necessary to compare the resultant price of the two kinds of the shares in the market to arrive at a proper cost valuation. The said decision was approved in a later decision in the case of Gold Mohore Investment Co. Ltd. (supra). In the present case the bonus shares rank *pari passu* to the original shares and, therefore, in view of the aforesaid two decisions of the Supreme Court the average is to be worked out by spreading the cost of the original shares over the original as well as the bonus shares.

5. The cost of acquisition is defined in Section 55(2) for the purposes of computing the capital gains in relation to a capital asset. It provides that where the capital asset became the property of the assessee before the 1st day of January, 1964, the cost of acquisition means the cost of acquisition of the assets to the assessee or the fair market value of the assets as on the 1st day of January, 1964 at the

option of the assessee. Admittedly, the bonus shares did not become the property of the assessee before 1-1-1964. Therefore, the market value of the bonus shares as on 1-1-1964 cannot be opted by the assessee and this is what the Commissioner of Income-tax (Appeals) had held. The assessee's case however is that in working out the average cost of the acquisition in the light of the aforesaid two decisions of the Supreme Court in the cases of Dalmia Investment Co. Ltd. (supra) and Gold Mohore Investment Co. Ltd. (supra), the cost of acquisition of the original shares as substituted by the market value as on 1-1-1964 under Section 55(2) should be taken into consideration. In our opinion, when a particular meaning has been assigned to a word under the Act, the same should be carried to its logical conclusion and necessary implication. It is stated in an often repeated passage of Lord Asquith in the case of East End Dwellings Co. Ltd. v. Flinsbury Borough Council [1951] 2 All. ER 587 at 599 that "if you are bidden to treat an imaginary state of affairs as real, you must, surely unless prohibited from doing so, also imagine as real the consequences and incidents which, if the putative state of affairs had in fact existed, must inevitably have flowed from or accompanied it ... The statute says that you must imagine a certain state of affairs; it does not say that having done so, you must cause or permit your imagination to boggle when it comes to the inevitable corollaries of that state of affairs".

6. In this case, the market value as on 1-1-1964 has been deemed as the cost of acquisition of the original shares. Therefore, that substituted cost of acquisition should be adopted for all purposes while computing the capital gains, including for the purpose of finding out the average cost of acquisition of the bonus shares. It would even otherwise be illogical to say that the cost of acquisition so far as the original shares is concerned, is its market value as on 1-1-1964 but while adopting the said cost of acquisition for finding out the average cost of acquisition of the bonus shares one says that its cost of acquisition is not that but what the assessee had actually paid at the time of its acquisition. The moment an assessee exercises his option for substituting the market value as on 1-1-1964 as cost of acquisition of the original shares that value is deemed to be the cost of acquisition after that date, i.e., 1-1-1964 and all the incidents prior to that date are to be ignored. We, therefore, accept the contention of the assessee that the market value of the original shares as on 1-1-1964 as against the original cost should be

spread over to arrive at the cost of acquisition of the bonus shares in the present case and direct the authorities below accordingly.

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