2026 INSC 46

REPORTABLE

IN THE SUPREME COURT OF INDIA
CIVIL APPELLATE JURISDICTION

CIVIL APPEAL NO. 152 OF 2026
[Arising out of S.L.P. (C) No. 2028 of 2021]

M/S JINDAL EQUIPMENT LEASING CONSULTANCY SERVICES LTD ... APPELLANT(S)

VERSUS

COMMISSIONER OF INCOME TAX DELHI – II, NEW DELHI ... RESPONDENT(S)

WITH

CIVIL APPEAL NO. 153 OF 2026
[Arising out of S.L.P. (C) No. 2190 of 2021]

M/S NALWA INVESTMENT LTD. ... APPELLANT(S)

VERSUS

COMMISSIONER OF INCOME TAX – V NEW DELHI ... RESPONDENT(S)

WITH

CIVIL APPEAL NO. 154 OF 2026
[Arising out of S.L.P. (C) No. 2188 of 2021]

M/S ABHINANDAN TRADEX LTD. (EARLIER KNOWN AS M/S ABHINANDAN INVESTMENT LTD) ... APPELLANT(S)

VERSUS

COMMISSIONER OF INCOME TAX DELHI – I, NEW DELHI ... RESPONDENT(S)

WITH

CIVIL APPEAL NO. 155 OF 2026
[Arising out of S.L.P. (C) No. 2197 of 2021]

M/S MANSAROVER TRADEX LTD (EARLIER KNOWN AS M/S MANSAROVER INVESTMENT LTD) ... APPELLANT(S)

VERSUS

COMMISSIONER OF INCOME TAX DELHI – II, NEW DELHI ... RESPONDENT(S)

J U D G M E N T

R. MAHADEVAN, J.

Leave granted.

2. The present appeals arise out of a common judgment and final order dated 07.08.2020 passed by the High Court of Delhi[1] in ITA Nos. 935, 822, 853, and 961 of 2005, pertaining to the Assessment Year 1997-98. By the

[1] Hereinafter referred to as "the High Court"

impugned judgment, the High Court remanded the matters to the Income Tax Appellate Tribunal[2] for fresh adjudication on the question of whether the shares held in the amalgamating company constituted stock-in-trade or capital assets, upon observing that, if the shares were, in fact, held as stock-in-trade, the transaction would fall outside the purview of Section 47(vii) of the Income Tax Act, 1961[3], and its taxability would consequently be governed by Section 28 under the head "profits and gains of business or profession".

FACTUAL MATRIX

3. The facts, which are common to all these appeals, may be briefly stated as under:

3.1. The appellants are investment companies of the Jindal Group. The shares of the operating companies, namely Jindal Ferro Alloys Limited (JFAL) and Jindal Strips Limited (JSL), were held as part of the promoter holding, representing controlling interest. The appellants had also furnished non-disposal undertakings to the financial institutions / lenders who had advanced loans to the operating companies. These shares were reflected as investments in the balance sheets of the appellants.

3.2. During the previous year relevant to the assessment year 1997-98, pursuant to a scheme of amalgamation approved by orders dated 19.09.1996

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[2] For short, "the Tribunal"
[3] For short, "the I.T. Act"

and 03.10.1996 of the High Courts of Andhra Pradesh and Punjab & Haryana respectively, under Sections 391 – 394 of the Companies Act, 2013, JFAL was amalgamated with JSL. As per the sanctioned scheme, the appointed date of amalgamation was 01.04.1995, and the orders sanctioning the amalgamation were filed with the Registrar of Companies on 22.11.1996 (the effective date). Under the scheme of amalgamation, the shareholders of JFAL were allotted 45 shares of JSL for every 100 shares of JFAL held by them. Accordingly, the appellants were allotted shares of JSL in lieu of the shares of JFAL.

3.3. The appellants, in their returns of income filed for the assessment year in question, claimed exemption under Section 47(vii) of the I.T. Act in respect of the receipt of JSL shares in lieu of JFAL shares, treating the same to be capital assets. However, in the assessment completed under Section 143(3) *vide* order dated 29.02.2000, the Assessing Officer treated the shares of JFAL as stock-in-trade, denied the exemption under Section 47(vii), and brought to tax the value of JSL shares as business income, computed with reference to their market value. The said order was upheld by the Commissioner of Income Tax (Appeals).

3.4. On further appeals, the Tribunal *vide* order dated 17.02.2005, allowed the assessees' appeals by observing that it was unnecessary to decide whether the shares were held as stock-in-trade or capital assets since no profit accrues unless the shares held by the appellants are either sold or transferred for consideration, irrespective of the nature of holding. It was further observed that there was

admittedly no sale of shares and, therefore, the only question for consideration was whether the allotment of JSL shares in lieu of JFAL shares under the scheme of amalgamation amounted to a "transfer". Following the decision of this Court in ***Commissioner of Income Tax, Bombay v. Rasiklal Maneklal (HUF) and others***[4], the Tribunal concluded that there was no transfer of shares and, consequently, no taxable profit could be said to have accrued to the appellants.

3.5. The Revenue challenged the Tribunal's decision before the High Court, raising the following substantial questions of law:

> *"1. Whether shares received by the assesses on amalgamation are entitled to the benefit of section 47(vii) without the Tribunal concluding that the said shares were held by the assesses as capital assets?*
>
> *2. Whether the benefit of Section 47(vii) is limited to determination of capital gains and only in regard to capital assets?*
>
> *3. Whether income would accrue to the assesses on shares received by amalgamations and will be taxable in view of non-applicability of Section 47(vii)?"*

3.6. After hearing both sides, the High Court, by the impugned judgment, disposed of the appeals in favour of the Revenue and against the assessees. In doing so, it held that the Tribunal had erred in placing reliance on ***Rasiklal Maneklal*** while failing to consider the later and binding decision of this Court in ***Commissioner of Income-tax, Cochin v. Grace Collis and others***[5]. The High

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[4] (1989) 177 ITR 198 : (1989) 2 SCC 454
[5] (2001) 248 ITR 323 (SC) : (2001) 3 SCC 430

Court observed that where the shares of the amalgamating company were held as capital assets, the receipt of shares of the amalgamated company would constitute a "transfer" within the meaning of Section 2(47) of the I.T. Act, though such transfer would be exempt under Section 47(vii). However, in the alternative scenario where the shares were held as stock-in-trade, the High Court held that upon the assessees receiving shares of the amalgamated company in lieu of those held in the amalgamating company, the assesses had, in effect, realised the value of their trading assets, and the difference in value would be taxable as business profit under Section 28. In reaching this conclusion, the High Court relied upon the decision of this Court in ***Orient Trading Company Ltd. v. Commissioner of Income Tax, Calcutta***[6]. Accordingly, the matter was remanded to the Tribunal for determination of the nature of the appellants' holding of JFAL shares, i.e., whether such holdings constituted capital assets or stock-in-trade.

3.7. Aggrieved thereby, the appellants have preferred the present appeals before this Court.

CONTENTIONS OF THE PARTIES

4. Mr. Ajay Vohra, learned Senior Counsel for the appellants, primarily submitted that the impugned judgment of the High Court is liable to be set aside as it travels beyond the jurisdiction conferred under Section 260A of the I.T.

[6] (1997) 224 ITR 371 (SC) : (1997) 3 SCC 340

Act. It was pointed out that the appeals before the High Court were admitted on a limited question, namely, whether the Tribunal was correct in holding that where the assessees get shares of the amalgamated company in lieu of shares of the amalgamating company, no transfer takes place. However, while disposing of the appeals, the High Court went further and proceeded to examine the taxability of such receipt, treating it as stock-in-trade or a capital asset. Since that issue was neither specifically raised nor framed at the time of admission, the adjudication was impermissible and contrary to the framework laid down by this Court in ***Shiv Raj Gupta v. Commissioner of Income-Tax, Delhi***[7].

4.1. It was further submitted that the receipt of shares of the amalgamated company does not amount to either a "sale" or an "exchange". It was urged that upon amalgamation, the amalgamating company stands dissolved and consequently, its shares cease to exist. Therefore, when shareholders receive shares of the amalgamated company in lieu of the extinguished shares of the amalgamating company, there is no subsisting property capable of being exchanged and accordingly, no taxable business income arises from such transaction. Moreover, the definition of "transfer" under Section 2(47) is relevant only for the purpose of computing capital gains and has no application to stock-in-trade. Only the exploitation or realisation of stock-in-trade gives rise

[7] (2020) 425 ITR 420 (SC)

to business income, which is to be computed strictly in accordance with Section 28 of the I.T. Act.

4.2. Reliance was placed on the decision of this Court in ***Vania Silk Mills P. Ltd v. Commissioner of Income-Tax*** [8], wherein it was held that the mere destruction or loss of an asset does not constitute a "transfer". The term "transfer" in Section 45 connotes that there must be something transferred to someone – some property, right, or interest passing from one person to another. When an asset ceases to exist, there can be no such transfer. Further reliance was placed on ***Commissioner of Income-Tax, Andhra Pradesh v. Motors & General Stores (P) Ltd***[9] wherein, it was held that to constitute an "exchange", there must be a subsisting property capable of being transferred or exchanged. Reference was also made to ***Rasiklal Maneklal,*** in which, it was held that the receipt of shares of an amalgamated company in lieu of shares held in the amalgamating company under an approved scheme of amalgamation, does not amount to an "exchange". Consequently, it was submitted that the allotment of shares in the amalgamated company, in substitution for the shares held in the amalgamating company, does not amount to a realisation of stock-in-trade by way of sale or exchange, so as to give rise to taxable business income.

4.3. The learned Senior Counsel submitted that the authorities relied upon by the High Court were distinguishable from the present case. In ***Orient Trading***,

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[8] (1991) 191 ITR 647 (SC)
[9] (1967) 66 ITR 692 (SC)

the assessee had exchanged shares of one existing company for shares of another; that case did not involve amalgamation or dissolution of the company whose shares were exchanged. Likewise, the English decision in ***Royal Insurance Co. Ltd v. Stephen***[10] dealt with realisation of investments, not stock-in-trade by an insurance company assessed under a special statutory regime, and is inapplicable under Indian law. Similarly, ***Hindustan Lever and another v. State of Maharashtra and another***[11] concerned the legislative competence to levy stamp duty on an order of amalgamation. Observations therein as to the transfer of property between amalgamating and amalgamated companies were made in a wholly different context and cannot govern the computation of business income.

4.4. On the concept of accrual of business income, it was urged that taxable income arises only when a debt *in praesenti* is created in favour of the assessee, though payable in future, as laid down in ***E.D. Sassoon & Co. Ltd v. Commissioner of Income-Tax***[12]. Hypothetical or illusory benefits cannot constitute taxable income, as held in ***Commissioner of Income Tax, Bombay City I v. Shoorji Vallabhdas & Co.***[13], ***State Bank of Travancore v. Commissioner of Income-Tax, Kerala***[14], ***Godhra Electricity Co. Ltd v.***

[10] 14 Tax Cases 22
[11] (2004) 9 SCC 438
[12] (1954) 26 ITR 27 (SC)
[13] (1962) 46 ITR 144 (SC)
[14] (1986) 158 ITR 102 (SC)

Commissioner of Income-Tax[15] and ***Commissioner of Income-Tax v. Excel Industries Ltd. and another***[16]. Even if the fair market value of the shares allotted in the amalgamated company on the date of allotment exceeds the book value of the shares in the amalgamating company, such appreciation is purely notional. Real income would arise only upon the actual sale of the allotted shares, and until such realisation no business income accrues.

4.5. It was also emphasized that the scheme of the Act itself supports this view. Wherever the legislature intends to tax notional or deemed income, it has enacted specific provisions, for example, Section 28(iv) or valuation rules such as Rule 11UAB. Further, Section 49(1)(iii)(e) specifically provides that for capital gains, the cost of shares in the amalgamated company shall be deemed to be the cost of shares in the amalgamating company. By parity of reasoning, in the case of stock-in-trade also, the original cost must be preserved and any profit should be recognized only at the time of realisation.

4.6. It was finally submitted that the receipt of shares of the amalgamated company in lieu of shares held in the amalgamating company, even when such shares are held as stock-in-trade, does not constitute a "sale" or "exchange" giving rise to taxable business income. Any benefit is, at best, hypothetical until the shares are actually sold. The impugned judgment of the High Court, which

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[15] (1997) 225 ITR 746 (SC)
[16] (2013) 358 ITR 295 (SC)

disregards settled principles and binding precedents, is erroneous and liable to be set aside.

5. On the other hand, the learned Additional Solicitor General appearing for the respondent(s) – Department opposed the present appeals and supported the impugned judgment of the High Court. It was submitted that if shares are held as stock-in-trade, the profit accruing from the receipt of shares of the amalgamated company in lieu of those of the amalgamating company would be taxable under the head "profits and gains of business or profession". For the purpose of analyzing this issue, it is assumed that the assessees held the shares of the amalgamating company as stock-in-trade prior to the amalgamation, though this issue remains to be decided by the Tribunal on remand.

5.1. It was submitted that the Tribunal fell in error in holding that no profit accrues unless the shares held by an assessee are either sold or transferred otherwise for consideration, irrespective of the nature of holding. The Tribunal did not refer to any sub-section of Section 28 of the I.T. Act to support its conclusion that a sale or transfer alone can give rise to "profits and gains of business or profession". It failed to engage with Section 28 entirely, relying instead solely on ***Rasiklal Maneklal***. That decision, it was pointed out, is relevant only to the taxation of capital gains under the Income- tax Act, 1922, and has been clarified to be inapplicable by this Court in ***Grace Collis***. Since the

issue of Section 45 is not under contest in these proceedings, ***Rasiklal Maneklal*** has no further bearing.

5.2. It was submitted that the High Court rightly held that the spotlight should not entirely be on the concept of "transfer" but instead on whether there is business income in the hands of the assessee, and further that income is recognised when it is earned or realized, irrespective of whether it is in cash or kind". This finding demonstrates that transfer is not a necessary precondition for taxation of business income under Section 28.

5.3. According to the learned Senior Counsel, the appellants themselves admitted in their written submissions that the definition of "transfer" under Section 2(47) has no application to the computation of business income. To this extent, the appellants do not dispute the High Court's finding. Yet, the appellants continue to contend that realisation of stock-in-trade giving rise to taxable business income can only be through sale or exchange. Such a submission has no basis in light of Section 28.

5.4. It was further submitted that the plain language of Section 28 makes it clear that profits and gains of business or profession are chargeable irrespective of whether they arise by way of sale, exchange, or otherwise. Unlike Section 45, which specifically requires a transfer of a capital asset, Section 28 is agnostic to the manner in which income accrues. In particular, Sections 28(i) and 28(iv)

bring out this position, covering profits, gains, and benefits arising from business activities, whether convertible into money or not.

5.5. Reliance was placed on ***Orient Trading***, where this Court held that the exchange of securities by a share dealer amounted to realisation of stock-in-trade, resulting in taxable profits. The said decision directly answers the appellants' contention as it involved stock-in-trade and upheld that realisation may occur upon exchange, and not merely upon sale.

5.6. Applying the above legal principles, the learned Senior Counsel submitted that the High Court was correct in concluding that upon amalgamation, the shares of the amalgamating company cease to exist and their value stands realised either in cash (for dissenting shareholders) or in shares of the amalgamated company (for approving shareholders). Such realisation, when resulting in profit, is taxable under Section 28.

5.7. The learned Senior Counsel submitted that the appellants' reliance on cases such as ***E.D. Sassoon & Co. Ltd*** and ***Motors & General Stores (P) Ltd*** is misplaced. ***E.D. Sassoon,*** in fact, supports the Revenue's case by holding that income accrues when the right to receive is acquired, even if actual receipt is later. ***Motors & General Stores*** has already been distinguished in ***Orient Trading*** as being confined to the meaning of "sale" in Section 10(2)(vii) of the 1922 Act, and is therefore inapplicable. Similarly, ***Rasiklal Maneklal*** and

Vania Silk Mills pertain to capital gains and transfer under Section 45, which the appellants themselves concede, have no bearing on the computation of business income.

5.8. It was further submitted that the levy in the present case is not on hypothetical income. As explained in ***Excel Industries***, income accrues when it becomes due and when there exists a corresponding liability on the other party. Here, by virtue of the amalgamation scheme sanctioned by the Court, there was a corresponding liability on the amalgamated company to issue shares (or pay cash to dissenters) in exchange for the extinguished shares of the amalgamating company. This satisfies the test of real income under ***Excel Industries***.

5.9. Even assuming, without conceding, that the Tribunal was correct in requiring a "sale" or "transfer", it was argued that a scheme of amalgamation itself has "all the trappings of a sale", as held in ***Hindustan Lever.*** Thus, even on the appellants' theory, the taxable event occurred.

5.10. Finally, on the appellants' contention regarding valuation of shares, the learned Senior Counsel submitted that this issue was considered and rejected by the CIT(A) with cogent reasoning, and that the Tribunal may examine this factual issue afresh on remand, if necessary. That issue, however, need not detain this Court, which is concerned only with the legal question.

5.11. Accordingly, the learned Senior Counsel submitted that the High Court's reasoning is sound, the Tribunal's judgment is unsustainable, and the present appeals deserve to be dismissed.

ANALYSIS AND FINDINGS

6. We have heard learned counsel appearing for the parties and perused the materials available on record.

7. By order dated 10.02.2021, this Court stayed the effect and operation of the impugned judgment and order under challenge.

8. Apparently, the appellants were shareholders of JFAL. Pursuant to the orders of the High Courts of Andhra Pradesh and Punjab and Haryana dated 19.09.1996 and 03.10.1996, JFAL merged with JSL, a widely held public company. Upon the amalgamation become effective, JFAL ceased to exist as a legal entity. In terms of the share exchange ratio approved under the scheme, shareholders were allotted 45 shares of JSL against 100 shares of JFAL.

8.1. During the relevant assessment year, the appellants claimed exemption under Section 47(vii) of the I.T. Act in respect of the receipt of JSL shares, contending that the shares of JFAL were held as capital assets. The Assessing Officer, however, denied exemption, holding that the shares of JFAL constituted stock-in-trade in the hands of the appellants. He accordingly taxed the difference between the value of the JSL shares (as on the appointed date) and the book value of JFAL shares. The CIT(A) upheld this view, dismissing the appeals on the finding that the appellants' acquisition of shares was an adventure in the nature of trade, attracting taxation under Section 28 of the I.T.

Act. Thus, there were concurrent findings that the assessees belonging to the same group which controlled JFAL, engaged in a scheme for profit-making by exchanging their stock-in-trade holdings in JFAL for shares of JSL.

8.2. On further appeals, the Tribunal, by order dated 17.02.2005, allowed the assessees' claims. It declined to decide the factual question whether the JFAL shares were held as capital assets or as stock-in-trade, holding instead that no profit accrues unless the shares are either sold or transferred for consideration, irrespective of the nature of holding.

8.3. In the Revenue's appeals, the High Court by the impugned judgment, set aside the Tribunal's order and remitted the matter for fresh consideration. The High Court returned two findings: first, that if shares are held as capital assets, an amalgamation is indeed a transfer within the meaning of Section 2(47) of the I.T. Act, though exempt under Section 47(vii). The assessees no longer dispute this finding before this Court. Second, the High Court held that if the shares are held as stock-in-trade, the profit arising to the assessees from the receipt of JSL shares in lieu of JFAL shares would be taxable as "profits and gains of business or profession" under Section 28. It is the second finding, which has necessitated the present appeals before this Court.

9. At the outset, the learned Senior Counsel appearing for the appellants raised a preliminary objection that the High Court had transgressed its jurisdiction in remitting the matter to the Tribunal with an observation that, if

the shares were stock-in-trade, the taxability would arise under Section 28 of the I.T. Act. It was urged that such an issue was neither expressly framed as a substantial question of law by the High Court nor raised by the Revenue in its appeals. Reliance was placed on ***Shiv Raj Gupta***, where this Court held that the High Court cannot decide a new question of law without formally framing it under Section 260A (4) and without affording the parties an opportunity to meet that case. The following paragraphs are apposite in this context:

> ***"18. It can be seen that the substantial question of law that was raised by the High Court did not contain any question as to whether the non-compete fee could be taxed under any provision other than Section 28(ii)(a) of the Income Tax Act, 1961. Without giving an opportunity to the parties followed by reasons for framing any other substantial question of law as to the taxability of such amount as a capital receipt in the hands of the assessee, the High Court answered the substantial question of law raised as follows****: (Shiv Raj Gupta case [CIT v. Shiv Raj Gupta, 2014 SCC OnLine Del 7305: (2015) 372 ITR 337], SCC OnLine Del paras 63 & 65)*
>
> > *"63. In view of the aforesaid discussion, we deem it appropriate and proper to treat Rs 6.60 crores as consideration paid for sale of shares, rather than a payment under Section 28(ii)(a) of the Act. ...*
> > *...*
> > *65. The substantial question of law is accordingly answered in favour of the appellant Revenue and against the respondent-assessee but holding that Rs 6.60 crores was taxable as capital gains in the hands of the respondent-assessee being a part of the full value sale consideration paid for transfer of shares. The appellant Revenue will be entitled to costs as per the Delhi High Court Rules."*
>
> ***Clearly, without any recorded reasons and without framing any substantial question of law on whether the said amount could be taxed under any other provision of the Income Tax Act, the High Court went ahead and held that the amount of INR 6.6 crores received by the assessee was received as part of the full value of the sale consideration paid for transfer of shares — and not for handing over management and control of CDBL and is consequently not taxable under Section 28(ii)(a) of the Income Tax Act.*** *Nor is it exempt as a capital receipt being non-compete fee, as it is taxable as a capital gain in the*

hands of the respondent-assessee as part of the full value of the sale consideration paid for transfer of shares. This finding would clearly be in the teeth of Section 260-A (4), requiring the judgment to be set aside on this score."

9.1. Undoubtedly, Section 260A envisages that an appeal to the High Court lies only where a substantial question of law arises. Sub-sections (3) and (4) mandate the formulation of such questions, while the proviso to sub-section (4) preserves the Court's power, for recorded reasons, to entertain any other substantial question of law not earlier framed. For ease of reference, the said provision is reproduced as follows:

*"**260-A. Appeal to High Court**.—(1) An appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal before the date of establishment of the National Tax Tribunal, if the High Court is satisfied that the case involves a substantial question of law.*

(2) The Principal Chief Commissioner or Chief Commissioner or the Principal Commissioner or Commissioner or an assessee aggrieved by any order passed by the Appellate Tribunal may file an appeal to the High Court and such appeal under this sub-section shall be—
(a) filed within one hundred and twenty days from the date on which the order appealed against is received by the assessee or the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner;
(b)….
(c) in the form of a memorandum of appeal precisely stating therein the substantial question of law involved.
(2-A) The High Court may admit an appeal after the expiry of the period of one hundred and twenty days referred to in clause (a) of sub-section (2), if it is satisfied that there was sufficient cause for not filing the same within that period.

(3) Where the High Court is satisfied that a substantial question of law is involved in any case, it shall formulate that question.

> *(4) The appeal shall be heard only on the question so formulated, and the respondents shall, at the hearing of the appeal, be allowed to argue that the case does not involve such question:*
> *Provided that nothing in this sub-section shall be deemed to take away or abridge the power of the court to hear, for reasons to be recorded, the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.*
>
> *(5) The High Court shall decide the question of law so formulated and deliver such judgment thereon containing the grounds on which such decision is founded and may award such cost as it deems fit.*
>
> *(6) The High Court may determine any issue which—*
> *(a) has not been determined by the Appellate Tribunal; or*
> *(b) has been wrongly determined by the Appellate Tribunal, by reason of a decision on such question of law as is referred to in sub-section (1).*
>
> *(7) Save as otherwise provided in this Act, the provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the High Court shall, as far as may be, apply in the case of appeals under this section."*

9.2. The scheme is consciously modelled on Section 100 of the Code of Civil Procedure, 1908, which similarly confines jurisdiction in second appeal to substantial questions of law. Both provisions embody the legislative policy of limiting higher appellate interference to questions of law, while at the same time, permitting the Court to deal with necessary or incidental questions that arise, provided reasons are recorded and parties are heard. In a recent judgment in ***R. Nagaraj (dead) through legal heirs and another v. Rajamani and others***[17], this Court held that although a separate issue need not be framed on every point, a finding on a disputed question, while deciding a connected issue, is sufficient.

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[17] 2025 Livelaw SC 416

9.3. In the present case, the High Court did not specifically frame the question of law as to whether the substitution of shares was taxable under Section 28 of the I.T. Act. However, the said issue went to the very root of the matter, and the High Court was bound to consider it in view of the issue already framed by the Tribunal and the submissions advanced by both sides before the Tribunal as well as before the High Court. Such a question was incidental or collateral to the main issue, and the absence of a formal formulation would not vitiate the impugned judgment of the High Court.

9.4. Furthermore, the present case does not fall within the mischief noticed in ***Shiv Raj Gupta*** for the following reasons:

- First, the Tribunal itself had framed the substantial issue as "*whether any income accrues to the appellants on the event of substitution of shares of Jindal Ferro Alloys Ltd. by the shares of Jindal Strips Ltd. under the scheme of amalgamation approved by the High Court of Andhra Pradesh and High Court of Punjab & Haryana*". While answering this question in the negative, the Tribunal left open the determination of whether the shares were held as investments or as stock-in-trade. Once such a finding was recorded, the real question of law was not merely the applicability of Section 47, but more broadly the taxability of the amalgamation transaction under the Act.
- Second, in appeal, the High Court framed the following substantial question of law: *"Whether the Tribunal was correct in holding that where*

the assessee gets shares of the amalgamated company in lieu of shares of the amalgamating company, no transfer takes place?" This formulation was wide enough to cover not only the application of Section 47 but also the broader question of taxability of such substitution of shares under the Act. The High Court did not itself assess income under Section 28, but only clarified that if the shares were stock-in-trade, the exemption of Section 47 would not apply, and the matter required reconsideration by the Tribunal so as to determine whether the shares were held as stock-in-trade or as capital assets, as without that determination the taxability or eligibility for exemption could not be ascertained.

- Third, there was no violation of natural justice in the present case, unlike in ***Shiv Raj Gupta*** where an altogether new head of income was introduced without notice to the assessee. Here, the High Court expressly recorded the preliminary objections and submissions of the appellants with respect to Section 28 and dealt with them. Thus, the parties had full opportunity to address this aspect before remand. Merely because a specific substantial question of law was not framed, it cannot be concluded that prejudice was caused to the parties, if both parties had the opportunity to address the issues in dispute.

9.5. Reference may also be made to ***Mansarovar Commercial Pvt. Ltd v. Commissioner of Income-Tax***[18], where a similar contention was raised based on ***Shiv Raj Gupta***. This Court held that issues incidental or collateral, on which the parties have been fully heard, can be considered by the High Court even if not expressly framed as substantial questions of law, especially where they arise directly from the Tribunal's findings. The following paragraphs from the said decision are pertinent in this regard:

> ***"45.13.*** *As regards the reliance placed upon the decision of this Court in Shiv Raj Gupta v. CIT [Shiv Raj Gupta v. CIT, (2021) 11 SCC 58 : AIR 2020 SC 3556], by the learned Senior Counsel appearing on behalf of the appellants on non-framing of substantial question of law in terms of Section 260-A of the Act so far as the interest liability is concerned, it is submitted that the said decision shall not be applicable to the facts of the case at hand and more particularly in case of an interest which is automatic and mandatory. It is submitted that in the said case, the dispute was with respect to capital gains which by its very nature is a separate head of income and the issue relates to the very taxability. That therefore, failure to raise a question of taxability of capital gains in a particular case may tantamount to a failure in raising a substantial question of law in terms of Section 260-A of the Act. However, the same may not apply on interest as the interest is automatic and mandatory."*
>
> ***"85. As regards the submission on behalf of the assessees that no substantial question of law was framed on levy of interest, at the outset, it is required to be noted that both the parties made submissions on levy of interest elaborately which have been dealt with and considered by the High Court in light of the Constitution Bench decision of this Court in Anjum M.H. Ghaswala [CIT v. Anjum M.H. Ghaswala, (2002) 1 SCC 633]*** *. Even otherwise, the said issue can be said to be incidental or collateral. Even otherwise, in view of the decision of this Court in Anjum M.H. Ghaswala [CIT v. Anjum M.H. Ghaswala, (2002) 1 SCC 633] holding that the levy of interest under Section 234-A is statutory interest and mandatory and automatic, thereafter the said issue cannot be said to be a question of law."*
>
> ***(Emphasis Supplied)***

[18] (2023) 454 ITR 1 (SC)

9.6. Accordingly, the High Court cannot be said to have exceeded its jurisdiction under Section 260A in making the impugned observation on Section 28 before remanding the matter. The preliminary contention of the appellants is, therefore, devoid of merit and stands rejected.

10. Now, another issue that arises for determination in these appeals is whether the High Court, while remanding the matter to the Tribunal to ascertain whether the shares of the amalgamating company were held as stock-in-trade or as capital assets, was justified in recording a finding that, if such shares were held as stock-in-trade, the allotment of shares of the amalgamated company pursuant to a court-sanctioned scheme of amalgamation would give rise to taxable business income in the hands of the appellants under Section 28 of the I.T. Act.

11. These appeals, therefore, raise a substantial question concerning the taxability of gains said to arise on amalgamation, where shares of the amalgamating company held by the assessees as stock-in-trade, stand substituted by shares of the amalgamated company. The core controversy is whether such substitution, in and of itself, constitutes a realisation giving rise to taxable business income under Section 28 and if so, the conditions under which such accrual or receipt can be said to arise in the commercial sense, or whether the incidence of taxation arises only upon the subsequent sale of the substituted shares.

12. Before proceeding further, it is apposite to refer to the statutory framework covering the issue involved in the present appeals. The relevant provisions of the I.T. Act are extracted below, for better appreciation:

Section 2(1B) – Amalgamation

> *"'amalgamation', in relation to companies, means the merger of one or more companies with another company or the merger of two or more companies to form one company (the company or companies which so merge being referred to as the amalgamating company or companies and the company with which they merge or which is formed as a result of the merger, as the amalgamated company) in such a manner that—*
> *(i) all the property of the amalgamating company or companies immediately before the amalgamation becomes the property of the amalgamated company by virtue of the amalgamation;*
> *(ii) all the liabilities of the amalgamating company or companies immediately before the amalgamation become the liabilities of the amalgamated company by virtue of the amalgamation;*
> *(iii) shareholders holding not less than [three-fourths] in value of the shares in the amalgamating company or companies (other than shares already held therein immediately before the amalgamation by, or by a nominee for, the amalgamated company or its subsidiary) become shareholders of the amalgamated company by virtue of the amalgamation,*
> *otherwise than as a result of the acquisition of the property of one company by another company pursuant to the purchase of such property by the other company or as a result of the distribution of such property to the other company after the winding up of the first-mentioned company."*

Section 2(14) – Capital asset

> ***"capital asset" means –***
> ***(a)*** *property of* ***any kind*** *held by an assessee, whether or not connected with his business or profession,*
> ***(b)*** *...*
> ***(c)*** *...*
> *but does not include—*
> *(i) any* ***stock-in-trade*** *[other than the securities referred to in sub-clause (b)], consumable stores or raw materials held for the purposes of his business or profession.*
> *(j) ..."*

Section 2(47) – Transfer

"transfer", in relation to a capital asset, includes,

(i) the sale, exchange or relinquishment of the asset; or

(ii) *the extinguishment of any rights therein; or*

(iii) *the compulsory acquisition thereof under any law*

..."

Section 28 — Profits and gains of business or profession

"The following income shall be chargeable to income-tax under the head "Profits and gains of business or profession",—

(i) *the profits and gains of any business or profession which was carried on by the assessee at any time during the previous year;*

...

(iv) *the value of any benefit or perquisite arising from business or the exercise of a profession, whether—*

(a) convertible into money or not; or

(b) in cash or in kind or partly in cash and partly in kind;]

...

(vi-a) *the fair market value of inventory on the date on which it is converted into, or treated as, a capital asset determined in the prescribed manner;*

...."

Section 45(1) — Capital gains

"Any profits or gains arising from the ***transfer of a capital asset*** *effected in the previous year shall, save as otherwise provided in sections 54, 54B, 54D, 54E, 54EA, 54EB, 54F, 54G and 54H, be chargeable to income-tax under the head "Capital gains", and shall be deemed to be the income of the previous year in which the* ***transfer took place****."*

Section 47 – Transactions not regarded as transfer

"Nothing contained in section 45 shall apply to the following transfers:

....

(vii) any transfer by a shareholder, in a scheme of amalgamation, of a capital asset being a share or shares held by him in the amalgamating company, if—

(a) the transfer is made in consideration of the allotment to him of any share or shares in the amalgamated company except where the shareholder itself is the amalgamated company, and

(b) the amalgamated company is an Indian company;

...."

12.1. The above provisions make it clear that the scope of taxability on amalgamation depends on the nature of the shares held. Section 2(14) excludes stock-in-trade from the definition of a capital asset, while Section 2(47) defines "transfer" only in relation to capital assets. Section 28 casts a wide net, taxing the "profits and gains of business or profession", including benefits or perquisites arising from business, whether convertible into money or not, or in cash or kind. Section 45 imposes capital gains tax only on the transfer of a capital asset, subject to exceptions under Section 47, including the transfer of shares in a scheme of amalgamation. Section 47(vii) specifically exempts from capital gains tax any transfer by a shareholder of a capital asset being shares of the amalgamating company, in consideration of the allotment of shares in the amalgamated company, provided the amalgamated company is an Indian company. There is a difference between a charging provision and an exemption provision. A provision that enables the levy of tax on a particular transaction is a charging provision. Only a transaction that is covered by a charging provision is taxable. Only if the transaction is taxable can there be an exemption. Therefore, the transfer of shares arising out of an order of amalgamation, even if it is treated as a capital asset, is generally taxable but would be exempt from taxation only if both the requirements under Section 47 (vii) are satisfied.

13. On behalf of the appellants, it was contended that no taxable event arises at the stage of amalgamation. According to them, income can be said to arise only upon the actual realisation or sale of the substituted shares, and not at the point of their allotment in the amalgamated company. The scheme of the Act, it was submitted, proceeds on the foundational premise that only real income is taxable unless Parliament, by express words, enacts a contrary legal fiction. Illustratively, Section 28(via) expressly deems the fair market value of inventory converted into a capital asset to be taxable, even without the receipt of money. This demonstrates that where the legislature intends to tax notional accretions, it does so explicitly. In the absence of any analogous deeming provision in respect of amalgamations, Section 28 cannot be judicially expanded to cover hypothetical or unrealised gains.

14. Conversely, on behalf of the Revenue, it was submitted that Section 28 does not predicate the existence of a "transfer", "sale" or "exchange". What the provision taxes are the "profits and gains of business or profession", which may be realised either in cash or in kind. Where stock-in-trade ceases to exist and is substituted by another commodity or asset of ascertainable value, profit accrues. According to the Revenue, the language of Section 28 is wide enough to encompass all benefits or advantages arising from business activity, irrespective of the form of realisation. Therefore, once the shares held as stock-in-trade in the amalgamating company ceases to exist and are replaced by shares of the

amalgamated company of higher value, a business profit arises which is liable to be taxed under Section 28.

Scope of Section 28

15. Before considering the rival submissions, it is necessary to delineate the scope of Section 28. The provision contemplates the chargeability of the "profits and gains of any business or profession" carried on by the assessees during the relevant previous year. What is material, therefore, is that there must be income arising from or in the course of business to be treated as profits or gains. Such profit must be ascertainable with reasonable definiteness at the relevant point of time, and the assessees must have either received it, or acquired a vested right to receive and commercially realise it, even if the receipt is in kind. It is not necessary for the benefit to be capable of being converted into money. Significantly, Section 28 does not prescribe any precondition as to the precise mode through which the profit must arise. The moment any income arises out of business or profession, the provision becomes applicable. It does not incorporate the definition of "transfer" under Section 2(47), unlike Section 45. It is sufficient if there is "income", and the "transfer", whether it is actual, material, or immaterial, is not relevant. The two provisions thus operate in distinct and independent fields. As already mentioned, the language of Section 28 – "the profits and gains of any business or profession" is deliberately wide, i.e., the charge itself is cast in wide terms. It is well settled that charging

provisions, while construed strictly, are not to be read in an unduly narrow manner when the language of the provision itself is wide.

15.1. In ***Mazagaon Dock Ltd v. Commissioner of Income Tax and Excess Profits Tax***[19]**,** this Court held that the language of Section 42(2) of the 1922 Act, though strict in nature, could not be artificially restricted. Expressions such as "business' and "profits derived" were held to be of wide import in fiscal statutes and must be construed broadly to give effect to the legislative intent. The Court rejected the narrow interpretation urged by the assessee and clarified that wide words used in charging provisions cannot be cut down merely to avoid unusual or harsh consequences. Similarly, in ***Ujagar Prints Etc. v. Union of India and others Etc.***[20], the Court reiterated that wide statutory language must receive its full amplitude and cannot be artificially confined. Further, in ***Commissioner of Customs (Import), Mumbai v. Dilip Kumar and Company and others***[21], this Court clarified that "strict interpretation" does not connote a literal or pedantic reading. Instead, legislative intent must be combined with the words of the statute to arrive at a meaning that is neither too narrow nor too broad.

15.2. Thus, business profits may accrue or be realised in diverse circumstances, even in the absence of a conventional sale, transfer, or exchange in the strict legal sense. To confine the operation of Section 28 to such modes would unduly

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[19] AIR 1958 SC 861
[20] (1989) 3 SCC 488
[21] (2018) 9 SCC 1 (5-Judge Bench)

restrict a provision that Parliament has intentionally couched in broad terms. Illustratively, waiver of a trading liability has been treated as taxable business income under Section 28, as held in ***Commissioner of Income Tax v. T.V. Sundaram Iyengar & Sons Ltd.***[22] Again, in ***Commissioner of Income Tax v. Meghalaya Steels Ltd***[23], this Court noted that under Section 28, income from cash assistance, by whatever name called, received or receivable by any person against exports under any scheme of the Government of India, would be income chargeable to income tax under the head "Profits and gains of business or profession". It was held that if cash assistance received or receivable against exports schemes is included as income under the head "Profits and gains of business or profession" subsidies which go to the reimbursement of cost in the production of goods of a particular business would also have to be included under the same head, and not under the head "Income from other sources". Likewise, in ***Commissioner of Income Tax, Delhi v. Woodward Governor India P. Ltd***[24], this Court held that foreign exchange fluctuations on trading items directly affect the profit and loss account, thereby forming part of the computation of business profits. Although that case concerned the deduction of fluctuation losses, its reasoning underscores that real income under Section 28 may accrue without any conventional "transfer".

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[22] (1996) 222 ITR 344 (SC)
[23] (2016) 383 ITR 217 (SC)
[24] (2009) 312 ITR 254 (SC)

15.3. It therefore emerges that Section 28 is a comprehensive charging provision designed to bring within the tax net all real profits and gains arising in the course of business, whether convertible into money or received in money or in kind, and irrespective of whether such accrual or receipt of income is accompanied by a legal transfer in the strict sense.

Amalgamation – Concept and Legal character

16. Amalgamation, in corporate law, signifies the statutory blending of two or more undertakings into one. It is distinct from winding up: while the transferor company ceases to exist as a separate corporate entity, its business, assets, and liabilities are absorbed into and continue within the transferee. As held in ***Saraswati Industrial Syndicate Ltd v. Commissioner of Income Tax***[25], the transferor company ceases to exist, and the transferee emerges with a blended corporate personality, inheriting all rights and liabilities. Stroud's *Judicial Dictionary of Words and Phrases* (9th Edn.) describes amalgamation as the "welding or blending of two or more concerns into one". Black's Law Dictionary (11th Edn.) similarly defines it as the "act of combining or uniting; consolidation; amalgamation of two small companies to form a new corporation". In ***Walker's Settlement, In re***[26]**,** amalgamation was explained as the state of two companies being so joined as to form a third, or of one company

[25] 1990 Supp SCC 675
[26] 1935 Ch 567 (CA)

being absorbed into another [See: ***Religare Finvest Ltd. v. State (NCT of Delhi***[27]***]***.

16.1. Notably, the Companies Act, 2013 contains no express definition of amalgamation. Instead, Sections 230 – 232 prescribe the procedure and spell out the legal effect, namely, the extinguishment of the transferor's corporate identity and the vesting of its assets, rights, and obligations in the transferee. Thus, amalgamation – ordinarily effected through a scheme of compromise or arrangement sanctioned by the Court or Tribunal – is founded on agreement between shareholders and creditors, but its legal effect is statutory: upon sanction, all assets, rights, and liabilities of the transferor vest in the transferee by operation of law. In other words, amalgamation is more than a mere contractual transfer; it is a statutory process of substitution.

16.2. In ***Commissioner of Income Tax v. Mahagun Realtors (P) Ltd***[28], this Court explained that amalgamation is unlike liquidation. Though the corporate shell of the transferor disappears, its business continues within the transferee, and courts therefore identify the successor-in-interest upon whom rights and obligations devolve. The relevant paragraphs are extracted below for proper understanding:

> ***"19.*** *Amalgamation, thus, is unlike the winding up of a corporate entity. In the case of amalgamation, the outer shell of the corporate entity is undoubtedly destroyed; it ceases to exist. Yet, in every other sense of the term, the corporate venture continues — enfolded within the new or the existing transferee entity. In other words, the business and the adventure lives on but within a new corporate*

[27] (2024) 1 SCC 797
[28] (2022) 19 SCC 1

residence i.e. the transferee company. It is, therefore, essential to look beyond the mere concept of destruction of corporate entity which brings to an end or terminates any assessment proceedings. There are analogies in civil law and procedure where upon amalgamation, the cause of action or the complaint does not per se cease — depending of course, upon the structure and objective of enactment. Broadly, the quest of legal systems and courts has been to locate if a successor or representative exists in relation to the particular cause or action, upon whom the assets might have devolved or upon whom the liability in the event it is adjudicated, would fall."

***"21.** In Saraswati Syndicate [Saraswati Industrial Syndicate Ltd. v. CIT, 1990 Supp SCC 675], the facts were that after amalgamation, the transferee company claimed exemption from tax, of a sum which had been allowed as a trading liability, on accrual basis, in the hands of the transferee company which had ceased to exist. The Revenue disallowed that claim; that view was upheld. This Court stated that : (SCC pp. 679-81, paras 5-6)*

> *"5. ... In amalgamation two or more companies are fused into one by merger or by taking over by another. Reconstruction or "amalgamation" has no precise legal meaning. The amalgamation is a blending of two or more existing undertakings into one undertaking, the shareholders of each blending company become substantially the shareholders in the company which is to carry on the blended undertakings. There may be amalgamation either by the transfer of two or more undertakings to a new company, or by the transfer of one or more undertakings to an existing company. Strictly "amalgamation" does not cover the mere acquisition by a company of the share capital of other company which remains in existence and continues its undertaking but the context in which the term is used may show that it is intended to include such an acquisition. See: Halsbury's Laws of England, 4th Edn., Vol. 7, para 1539. Two companies may join to form a new company, but there may be absorption or blending of one by the other, both amount to amalgamation. When two companies are merged and are so joined, as to form a third company or one is absorbed into one or blended with another, the amalgamating company loses its entity.*
>
> *6. In General Radio & Appliances Co. Ltd. v. M.A. Khader [General Radio & Appliances Co. Ltd. v. M.A. Khader, (1986) 2 SCC 656], the effect of amalgamation of two companies was considered. M/s General Radio and Appliances Co. Ltd. was tenant of a premises under an agreement providing that the tenant shall not sublet the premises or any portion thereof to anyone without the consent of the landlord. M/s General Radio and Appliances Co. Ltd. was amalgamated with M/s National Ekco Radio and Engineering Co. Ltd. under a scheme of amalgamation and order of the High Court under Sections 391 and 394*

of Companies Act, 1956. Under the amalgamation scheme, the transferee company, namely, M/s National Ekco Radio and Engineering company had acquired all the interest, rights including leasehold and tenancy rights of the transferor company and the same vested in the transferee company. Pursuant to the amalgamation scheme the transferee company continued to occupy the premises which had been let out to the transferor company. The landlord initiated proceedings for the eviction on the ground of unauthorised subletting of the premises by the transferor company. The transferee company set up a defence that by amalgamation of the two companies under the order of the Bombay High Court all interest, rights including leasehold and tenancy rights held by the transferor company blended with the transferee company, therefore the transferee company was legal tenant and there was no question of any subletting. The Rent Controller and the High Court both decreed the landlord's suit. This Court in appeal held that under the order of amalgamation made on the basis of the High Court's order, the transferor company ceased to be in existence in the eye of the law and it effaced itself for all practical purposes. This decision lays down that after the amalgamation of the two companies the transferor company ceased to have any entity and the amalgamated company acquired a new status and it was not possible to treat the two companies as partners or jointly liable in respect of their liabilities and assets. In the instant case the Tribunal rightly held that the appellant company was a separate entity and a different assessee, therefore, the allowance made to Indian Sugar company, which was a different assessee, could not be held to be the income of the amalgamated company for purposes of Section 41(1) of the Act. The High Court was in error in holding that even after amalgamation of two companies, the transferor company did not become non-existent instead it continued its entity in a blended form with the appellant company. The High Court's view that on amalgamation there is no complete destruction of corporate personality of the transferor company instead there is a blending of the corporate personality of one with another corporate body and it continues as such with the other is not sustainable in law. The true effect and character of the amalgamation largely depends on the terms of the scheme of merger. But there cannot be any doubt that when two companies amalgamate and merge into one the transferor company loses its entity as it ceases to have its business. However, their respective rights or liabilities are determined under the scheme of amalgamation but the corporate entity of the transferor company ceases to exist with effect from the date the amalgamation is made effective."

***"30.** In Bhagwan Dass Chopra v. United Bank of India [Bhagwan Dass Chopra v. United Bank of India, 1987 Supp SCC 536] it was held that in every*

> *case of transfer, devolution, merger or scheme of amalgamation, in which rights and liabilities of one company are transferred or devolved upon another company, the successor-in-interest becomes entitled to the liabilities and assets of the transferor company subject to the terms and conditions of contract of transfer or merger, as it were. Later, in Singer India Ltd. v. Chander Mohan Chadha [(2004) 7 SCC 1] this Court held as follows: (SCC p. 10, para 8)*
>
> > *"8. ... there can be no doubt that when two companies amalgamate and merge into one, the transferor company loses its identity as it ceases to have its business. However, their respective rights and liabilities are determined under the scheme of amalgamation, but the corporate identity of the transferor company ceases to exist with effect from the date the amalgamation is made effective."*

16.3. At this juncture, it must be noted that the High Court relied on ***Hindustan Lever***, which, though not in the context of taxation, observed that amalgamation bears all the "trappings of a sale". We shall, however, proceed to analyse Section 28 in the context of amalgamation since the test under Section 28 is somewhat different: it does not hinge on whether there is a sale, transfer, or exchange in the strict legal sense, as already discussed. At the same time, it cannot be overlooked that this Court in ***Grace Collis***, overruling ***Vania Silk Mills***, held that amalgamation, for the purposes of capital gains under Section 45, does involve a "transfer" of shares. Even if that ratio was rendered in the context of capital gains, once this Court has recognized that amalgamation entails a transfer, that conclusion cannot be ignored while considering the ambit of Section 28.

16.4. The real question, therefore, is whether an amalgamation – though, in company law, it operates as a statutory substitution of rights – nonetheless gives

rise to taxable business profits under Section 28 of the I.T. Act. That enquiry is not concluded merely by characterising the event as a "transfer". It requires a deeper examination of whether the substitution of shares results in real commercial profits, having accrued or arisen in the course of business, so as to be chargeable as business income under Section 28.

Whether there is receipt or accrual of income upon amalgamation

17. In the context of amalgamation, what transpires is essentially a statutory substitution of one form of holding for another. The shareholder's interest in the transferor company is replaced by a corresponding interest in the transferee company. For the purposes of Section 28, the first test is whether such substitution constitutes either a receipt or an accrual of income.

17.1. It is settled law that income yielding business profits may be realised not only in money but also in kind. Thus, where an assessee receives shares of the amalgamated company in place of its shares held as trading stock, there is, in form, a receipt of consideration in kind. Though such amalgamations receive the sanction of the Court/Tribunal to be effectuated, they are preceded by decisions taken in meetings of shareholders. In such meetings, valuation reports are placed before the shareholders, and for the amalgamation to be approved, 90% of the shareholders must vote in favour of the amalgamation. The report contains details of the share exchange ratio. Though the value of each share is

determined at that stage, it is not tradable, as no right is vested at that point. Ordinarily, such receipt arises only upon the actual allotment of shares, since until that point no asset is placed in the hands of the assessee. It cannot, however, be ruled out that in certain cases, the terms of the sanctioned scheme may themselves create, from an earlier date, a vested and imminent enforceable right to allotment; in such situations, one may speak of "accrual". The general position, nevertheless, is that what the law recognises in amalgamation is the receipt of shares in substitution of trading assets.

Commercial realisability

18. Coming to the next test, it must be underscored that mere receipt of shares does not suffice to attract Section 28; commercial realisability is also required when income is received in kind. Moreover, in ***Kanchanganga Sea Foods Ltd v. Commissioner of Income Tax***[29], it was observed that the recipient of income must have control over the income received, emphasising that mere receipt in kind is not enough.

18.1. It must also be clarified at this stage that amalgamation, in strict legal terms, does not amount to an "exchange." In ***Rasiklal Maneklal***, this Court held that the allotment of shares in the amalgamated company under a court-sanctioned scheme is not the result of a bilateral bargain between two parties, i.e., there is no mutual or reciprocal transfer of ownership. Since the

[29] (2010) 11 SCC 144

amalgamating company itself ceases to exist, the element of mutual transfer that characterises an exchange is absent. Therefore, amalgamation, as held in other decisions, is to be understood as a statutory substitution of holdings, and not as an "exchange" in the legal sense.

18.2. Thus, the jurisprudence discloses three related strands: first, cases such as ***Orient Trading***, relying on English decision (***Royal Insurance Co. Ltd. v. Stephen***), which will be discussed later, emphasise that receipt of an asset of definite money's worth in substitution for another may amount to commercial realisation attracting Section 28; second, the decision in ***Rasiklal Maneklal***, which clarifies that allotment on amalgamation is not an "exchange", along with other decisions holding it to be a statutory substitution; and third, the ruling in ***Grace Collis***, which makes it clear that, notwithstanding its statutory character, amalgamation does involve a "transfer" within the meaning of the Income-tax Act.

18.3. Reconciling these strands, the true test under Section 28, as already noted, is not the legal label of "exchange" or "transfer", but whether the assessee, in consequence of the amalgamation and thereby of its business, has obtained a profit that is real and presently realisable. The well-known real-income principle, as emphasised in ***E.D. Sassoon*** *and* ***Shoorji Vallabhdas***, must be applied. Therefore, the enquiry for the Court is whether, as a result of the amalgamation, the assessee has in fact realised a profit in the commercial sense. This assessment may turn on whether:

(A) The old stock-in-trade has ceased to exist in the assessee's books;

(B) The shares received in the amalgamated company possess a definite and ascertainable value; and

(C) The assessee, immediately upon allotment, is in a position to dispose of such shares and realise money.

18.4. If these conditions are satisfied, the substitution bears the character of a commercial realisation and the profit may be taxed under Section 28. Where, however, the allotment of shares is merely a statutory substitution mandated by the scheme of amalgamation, without yielding an immediately realisable benefit, no income can be said to accrue or be received at that stage, and taxability arises only upon the eventual sale of the shares. For instance:

(A) If a shareholder of Company A receives shares of Company B pursuant to a court-sanctioned amalgamation, but such shares are subject to a statutory lock-in period during which they cannot be sold in the market, the allotment cannot be equated with a commercial realisation. It represents only a replacement of one form of holding by another, without any immediate gain capable of monetisation.

(B) Similarly, where the amalgamated company is closely held and its shares are not quoted on any recognized stock exchange, the mere allotment of such shares does not generate a realisable profit, since no open market exists to ascribe a fair disposal value.

18.5. These illustrations, which are not exhaustive, underline that unless the assessee is, by virtue of the substitution, placed in possession of an asset which is freely tradable and of an ascertainable market value, the principle of real income bars taxation at the stage of amalgamation. Thus, the substitution of shares upon amalgamation does not, by itself, give rise to taxable income under Section 28. What must be established is that the transaction has the attributes of a commercial realisation resulting in a real and presently disposable advantage. Where this test is satisfied, taxability may arise at the stage of substitution. Otherwise, the accrual or receipt of income is deferred until actual sale.

18.6. In other words, as noted earlier, the governing test under Section 28 is not the presence of a sale, exchange, or extinguishment of rights in the technical sense, but whether the assessee has, in consequence of business operations, come into possession of a real and presently realisable commercial benefit. This may take the form of money directly received, or assets in kind capable of being immediately disposed of for money's worth. The shares, therefore, must be readily available for trading to be treated as stock-in-trade.

19. We may now refer to the judgment in ***Orient Trading.*** Although it dealt with an exchange, the observations therein as to the nature of "realisation" are of general application. The Court, relying on English decision (***Royal Insurance Co. Ltd. v. Stephen***), explained that a realisation takes place when the old investment ceases to figure in the affairs of the company and its worth –

whether by way of profit or loss – can be determined with finality in monetary terms. At that point, the old investment is regarded as closed and a new investment is treated as having commenced. The emphasis is that realisation is not merely a matter of accounting entries, but arises where the former asset is replaced by a new and distinct asset of ascertainable value, thereby crystallising the economic outcome of the earlier holding. Lord Trayner, in ***Californian Copper Syndicate Ltd v. Inland Revenue***[30] observed that "no doubt here the price took the form of fully paid shares in another company, but, if there can be no realised profit except when that is paid in cash, the shares were realisable and could have been turned into cash". On this reasoning, even the exercise of an option, such as the choice to accept shares of the amalgamated company in lieu of the old holding, may amount to a realisation of the old asset, subject to the other conditions being satisfied, as discussed. The relevant portions of the judgment in ***Orient Trading***, are as under:

> ***"8.*** *The decision of Rowlatt, J. in Royal Insurance Co. Ltd. v. Stephen [(1928) 14 TC 22 : 44 TLR 630] was approved in the said case. In the case of Royal Insurance Co. Ltd. v. Stephen [(1928) 14 TC 22 : 44 TLR 630] the appellant-company had, under the Railways Act, 1921, to accept new stocks in the amalgamated companies in exchange for the stock held in the companies which were absorbed and which resulted in loss to the appellant-company. The claim of the appellant-company for deduction of such loss was upheld by Rowlatt, J. who held: (TC pp. 28-29)*
> ***"At the bottom of this principle of waiting for a realisation, I think there is this idea; while an investment is going up or down for income tax purposes the company cannot take any notice of fluctuations, but it has to take notice of them when all that state of affairs comes to an end, when that investment is wound up I will say — 'wound up' is an unfortunate expression perhaps and I will say when an investment ceases to figure in the company's affairs, when it***

[30] 5 TC 159

is known exactly what the holding of that investment has meant, plus or minus to the company, and then the company starts so far as that portion of its resources is concerned with a new investment. Then one knows where one is and it is no longer a question of paper, it is a question of fact and that is a realisation. I think that is the point of view from which it ought to be looked at, and looking at it from that point of view the company is right. It has done with the investments in the companies. They have disappeared. It is known exactly in money. It is known now exactly what their holding of them has meant to the company. They will never more go up or down. What will go up or down now are the different shares in the new companies, altogether different investments really, and therefore I think that the old investment is closed and realised and a new investment is started."

9. Similarly in Californian Copper Syndicate Ltd. v. Inland Revenue (Harris, Surveyor of Taxes) [5 TC 159], decided by the Court of Exchequer in Scotland, Lord Trayner has said: (TC p. 167)

"But it was said that the profit — if it was profit — was not realised profit and, therefore, not taxable. I think the profit was realised. A profit is realised when the seller gets the price he had bargained for. ***No doubt here the price took the form of fully paid shares in another company, but, if there can be no realised profit, except when that is paid in cash, the shares were realisable and could have been turned into cash, if the appellants had been pleased to do so****. I cannot think that income tax is due or not according to the manner in which the person making the profit pleases to deal with it."*

11. *The subsequent decision of the House of Lords in British South Africa Co. v. Varty (Inspector of Taxes) [1966 AC 381 : (1965) 2 All ER 395 : (1965) 3 WLR 47] does not lend assistance to the submission of Shri Puri. In that case the appellant-company in 1953 had lent 200,000 pounds to a gold mining company and in return had received, inter alia, an option to subscribe for 100,000 shares in the mining company at 1 pound per share, the value of the shares then being 19 Sh. 6 d a share. In 1954 when the value of the shares had gone up to 43 Sh. 6 d a share the appellant exercised the option and obtained shares worth 217,500 pounds for which they paid 100,000 pounds. The company was assessed for income tax on a profit of 11,75,000 pounds. On behalf of the company it was urged that upon the exercise of the option there was a realisation because the option which was a "trading asset" or an item of "stock-in-trade" was exchanged for or was replaced by a different item of stock-in-trade which had a value in money's worth. The said contention was rejected by the House of Lords (Lord Guest, dissenting). It was held that the appellant-company never, in fact, realised their option in the sense of passing it on for a consideration to someone else and that there was neither a sale of the option or its exchange for something else and that when the company exercised their option or used or availed themselves of their rights they did not make the end of the trading transaction*

and that there was merely the end of the beginning of a trading transaction. It was emphasised that there was no element of exchange as there was in Royal Insurance Co. Ltd. v. Stephen [(1928) 14 TC 22 : 44 TLR 630] and in Westminster Bank Ltd. v. Osler (Inspector of Taxes) [(1933) 1 ITR 65 : 1932 All ER Rep 917, HL]. (See Lord Morris of Borth-Y-Gest at pp. 394-395.) Lord Guest, in his dissenting judgment, however felt that the option was a trading asset of the appellant-company and, applying the principles laid down in Royal Insurance Co. Ltd. v. Stephen [(1928) 14 TC 22 : 44 TLR 630] and Westminster Bank Ltd. v. Osler (Inspector of Taxes) [(1933) 1 ITR 65 : 1932 All ER Rep 917, HL], held that the exercise of option amounted to a realisation of the option which resulted in a trading profit of 11,75,000 pounds. This would show that the principles laid down in Royal Insurance Co. Ltd. v. Stephen [(1928) 14 TC 22 : 44 TLR 630] and Westminster Bank Ltd. v. Osler (Inspector of Taxes) [(1933) 1 ITR 65 : 1932 All ER Rep 917, HL] have been affirmed by all the Law Lords and the difference amongst them was only as regards the applicability of the said principles to the facts of that case.

***13.** Having regard to the principles laid down in the decisions aforementioned, it must be held that the High Court has rightly taken the view that as a result of their having taken the shares in the second company in exchange of the shares of the first company the assessee had made realisation of the value of the shares of the first company and the difference between the price of the shares of the first company and the second company on the date of such exchange, i.e., Rs 4,06,000, has to be treated as a profit of the assessee and has been rightly assessed as income of the assessee. We, therefore, do not find any merit in the appeal and the same is accordingly dismissed, but in the circumstances with no order as to costs."*

20. The Privy Council in ***Raja Raghunandan Prasad Singh v. Commissioner of Income Tax***[31], recognised that income may be received in kind as well as in cash, and that the equivalent of cash may constitute income, but stressed that what is received must be "money's worth". It was clearly observed that there must be an actually realised or realisable profit or loss. The following passages are pertinent in this regard:

[31] (1933) 1 ITR 113 : 1933 SCC OnLine PC 8

"Their Lordships fully recognise that income may be received in kind as well as in cash and that the receipt of an equivalent of cash may be a receipt of income. In the case of Californian Copper Syndicate v. Harris [(1905) 6 F. 894 : 5 Tax. Cas. 159.], a company which dealt in mining properties sold certain property for fully-paid shares in another company and was held to be liable to income-tax on the profit made on the transaction although no cash passed, but this was on the ground that the shares taken in exchange were realisable and were thus money's worth and the equivalent of cash. *In the case of Royal Insurance Company, Ltd. v. Stephen [(1928) 44 T.L.R. 630 : 14 Tax. Cas. 22.], an insurance company, which admitted that any profit which it made on the realisation of investments was liable to tax, effected an exchange of securities in pursuance of a railway amalgamation scheme. The new stocks received in place of the surrendered stocks had at the date of the exchange a definite market value which was less than the original cost to the company of the surrendered stocks. A claim was made by the company in computing its profits to deduct the difference loss sustained by it. For the Crown it was contended that there has been no realisation of investments, but merely an exchange of one set of investments for another. The company's claim was upheld by Rowlatt, J. on the ground that it had in substance realised its former holdings and received for them money's worth of, a definite amount. The loss was thus a realised loss susceptible of exact estimation in money. The transaction was on "a money basis." Reference may also be made to the recent case in the House of Lords of Westminster Bank, Ltd. v. Osler (15th November, 1932) [(1933) A.C. 139.], where the bank surrendered certain holdings of National War Bonds in exchange for other Government securities and the Crown claimed tax oil the excess value of the substituted over the original securities. The question was whether these transactions were the equivalent of a realisation of the original holdings, and it was held that they were. "The exchange effected in the present case," said Lord Buckmaster, "was in fact the exact equivalent of what would have I taken place had instructions been given to sell the original stock and invest the proceeds in the new security." The bank had thus in effect realised its profit, for it had deceived it in money's worth of a I definitely ascertained amount.* ***From these cases it is plain that the essence of the matter is that there must be an actually realised or realisable profit or loss.***

Applying this principle to the assessees' transaction in 1904, their Lordships are of opinion that there was in the circumstances no realisation of the principal and interest of the original mortgage of 1894 and that when the assessees received, the new mortgage for Rs. 7,33,135, which included the principal and interest of the original mortgage, they did not thereby receive payment or the equivalent of payment of the principal and interest of the original mortgage. No doubt the grantors of the new mortgage were not identical with the grantor of the original mortgage and the property mortgaged was greater in extent, but the substitution effected cannot in any real sense, be described as the equivalent of a

> *realisation of the original mortgage, principal and interest. What happened was that the assessees received a new and substituted security for an existing debt. To give security for a debt is not to pay a debt. If the assessees had received payment in kind of the amount outstanding on the original mortgage, in the shape, say, of realisable shares or bonds, the case would have been different, but they merely received further and better security for their debt. It is, in their Lordships' view, quite immaterial that the assessees discharged the original mortgage and all liability under it, for that was merely an incident in the transaction whereby the new security was substituted for the old. Their Lordships accordingly hold that the assessees did not by virtue of the transaction of 1904 receive payment of the arrears of interest amounting to Rs.2,33,135 then outstanding on the mortgage of 1894; that the assessees were not liable to be taxed on this sum as being income received when the new mortgage was granted; and that this sum of arrears of interest (though after 1904 secured by the new mortgage) continued to retain its character and remain due to the assessees down to the time of the judicial sales of November, 1924, and January, 1925. In so holding their Lordships find themselves in agreement in result with the Commissioner and the High Court."*

21. In ***Raja Mohan Raja Bahadur v. Commissioner of Income Tax***[32], this Court held that where commercial assets are received in satisfaction of an obligation, income embedded in such assets is deemed to be received when title passes, irrespective of actual sale. The Court again took note of the observations made in the ***Californian Copper Syndicate*** case. The following paragraphs from the decision are apposite:

> ***"4.*** *Under Section 4 of the Income Tax Act, 1922, the total income of any previous year of a resident assessee includes all income, profits and gains from whatever sources derived which are received or are deemed to be received in the taxable territories in such year by or on behalf of such person, or accrue or arise or are deemed to accrue or arise to him in the taxable territories during such year, or accrue or arise to him without the taxable territories during such year, or having accrued or arisen to him without the taxable territories before the beginning of such year and after the 1st day of April, 1933, are brought into or received in the taxable territories by him during such year. The Act does not contain much guidance as to cases in which tax is to be levied on income*

[32] (1967) 66 ITR 378

received, and cases in which tax is to be levied on income accrued or arisen. Section 13 however requires that income, profits and gains for the purposes of Sections 10 and 12 shall be computed in accordance with the method of accounting regularly employed by the assessee. ***If accounts are maintained according to the mercantile system, whenever the right to receive money in the course of a trading transaction accrues or arises, even though income is not realised, income embedded in the receipt is deemed to arise or accrue. Where the accounts are maintained on cash basis receipt of money or money's worth and not the accrual of the right to receive is the determining factor. Therefore, if commercial assets are received by a trade maintaining accounts on cash basis in satisfaction of an obligation, income which is embedded in the value of the assets is deemed to be received : the receipt of income is not deferred till the asset is realized in terms of cash or money. It makes no difference whether the receipt of assets is in pursuance of an agreement or that the trader is compelled by law to accept the assets from the debtor. Once title of the trader to an asset received is complete, whether by a consensual arrangement or by operation of law, he receives the income embedded in the value of the asset****. In Californian Copper Syndicate (Limited and Reduced) v. Harris (Surveyor of Taxes) [5 TC 159] Lord Trayner in dealing with a case of assessment to income tax of a Company formed for the purpose, inter alia, of acquiring and reselling mining property resold the whole of its assets to a second Company and received payment in fully paid shares of the purchasing Company, observed:

> *"A profit is realised when the seller gets the price he has bargained for. No doubt here the price took the form of fully paid shares in another company, but, if there can be no realised profit, except when that is paid in cash, the shares were realisable and could have been turned into cash, if the appellants had been pleased to do so. I cannot think that Income tax is due or not according to the manner in which the person making the profit pleases to deal with it."*

Counsel for the appellant contended that the bonds were intended to renew the promise to pay the amount due by the debtor through his agent, and by the renewal of the promise even if the original liability was extinguished and a fresh liability was substituted, no income was received by the appellant.

5. *We are unable to agree with that contention. The Government of the State undertook to pay the amount of the bonds in satisfaction of the liability of the debtor. The liability of the original debtor was extinguished and a fresh obligation was undertaken by the State Government in substitution of the original liability. The Government had the right to recover the amount due under the bonds from the landholder, but on that account the Government did not become the agent of the landholder for payment of his debts. Even if the Government was unable to recover the money from the landholder, the liability undertaken by the Government under the bond remained unimpaired. The bond*

was a security for payment of the debt which completely replaced the original liability of the debtor."

22. This Court in ***Commissioner of Income Tax v. Ashokbhai Chimanbhai***[33], reiterated that profits do not accrue from day to day but are ascertained by a comparison of assets at two points in time. Further, the test of accrual is whether the person entitled thereto has a right to claim the profits. The following paragraphs are relevant in this regard:

> ***"6.*** *Under the Income Tax Act, income is taxable when it accrues, arises or is received, or when it is by fixation deemed to accrue, arise or is deemed to be received. Receipt is not the only test of chargeability to tax; if income accrues or arises it may become liable to tax. For the purpose of this case it is unnecessary to dilate upon the distinction between income "accruing" and "arising". But there is no doubt that the two words are used to contradistinguish the word "receive". Income is said to be received when it reaches the assessee : when the right to receive the income becomes vested in the assessee, it is said to accrue or arise. Fletcher Moulton, L.J., in In re The Spanish Prospecting Co. Ltd. [(1911) 1 Ch 92] observed at p. 98:*
>
> > *"The word 'profit' has * * * a well-defined legal meaning and this meaning coincides with the fundamental conception of profits in general parlance; although in mercantile phraseology the word may at times bear meanings indicated by the special context which deviate in some respects from this fundamental signification. 'Profit' implies a comparison between the state of a business at two specific dates usually separated by an interval of a year. The fundamental meaning is the amount of gain made by the business during the year. This can only be ascertained by a comparison of the assets at the two dates."*
>
> *In the gross receipts of a business day after day or from transaction to transaction lie embedded or dormant profit or loss: on such dormant profit or loss undoubtedly taxable profits, if any, of the business will be computed. But dormant profits cannot be equated with profits charged to tax under Sections 3 & 4 of the Income Tax Act. The concept of accrual of profits of a business involves the determination by the method of accounting at the end of the accounting year or any shorter period determined by law. If profits accrue to the assessee directly from the business the question whether they accrue de die, in*

[33] (1965) 56 ITR 42

diem or at the close of the year of account has at best an academic significance, but when upon ascertainment of profits the right of a person to a share therein is determined, the question assumes practical importance, for it is only on the right to receive profits or income, profits accrue to that person. If there is no right, no profits will be deemed to have accrued. This principle was applied by this Court in E.D. Sassoon & Co. Ltd. v. CIT [26 ITR 27]. The material facts bearing on that principle were these: E.D. Sassoon & Co. Ltd, — called "Sassoons" — were the managing agents of a Company which may be called 'the United Mills' and were entitled to receive a percentage of annual net profits of the Company as their remuneration. On December 1, 1943 Sassoons assigned to Messrs Agarwal & Co. their office as managing agents and all their rights and benefits under the managing agency agreement. Accounts of the managing agency commission payable to the managing agents for the calendar year 1943 were made up in 1944 and commission for the whole year was paid to Messrs Agarwal & Co. thereafter. In the course of assessment proceeding of Sassoons it was debated whether in respect of commission earned by the managing agency, tax was payable on the entirety of the commission by Messrs Agarwal & Co. or by Sassoons or it was liable to be apportioned between Messrs Agarwal & Co. and Sassoons. This Court held (Jagannadhadas, J. dissenting) that Messrs Agarwal & Co. alone were liable to pay tax on the whole of the remuneration received under the contract of service between the United Mills, because the managing agency was entire and indivisible, and the remuneration or commission fell due to the managing agents, only on completion of a definite period of service and at stated periods it being a condition of recovery of wages or salary that the service or duty should be completely performed. Remuneration as managing agents constituted according to the Court "a debt" only at the end of each such period of service and no remuneration or commission was payable to the managing agents for broken periods. After referring to the observations of Fletcher Moulton, L.J. in the Spanish Prospecting Co. Ltd. case [(1911) 1 Ch 92] (already set out), Bhagwati, J., observed that "it would be absurd to suggest that the profits of the company could accrue from day to day or even from month to month". The working of the company from day to day could certainly not indicate any profit or loss, even the working of the company from month to month could not be taken as a reliable guide for this purpose. If the profit or loss has to be ascertained by a comparison of the assets at two stated points, the most businesslike way would be to do so at stated intervals of one year and that would be a reasonable period to be adopted for the purpose. In the case of large business concerns the working of the company during a particular month may show profits and the working in another month may show loss. The business during the earlier part of the year may show profit or loss and in the later part of the year may show loss or profit which would go to counterbalance the profit or loss as the case may be in the earlier part of the year. It would therefore be reasonable to determine the profit or loss as the case may be at the end of every year so that on such calculation of net profits the managing agents may be paid

their remuneration or commission at the percentage stipulated in the managing agency agreement and the shareholders also be paid dividends out of the net profits of the Company.

7. *Counsel for the Commissioner submitted that the judgment in E.D. Sassoon Co. Ltd. case [26 ITR 27] proceeded upon the special character of a managing agency agreement and did not purport to lay down a general rule that accrual of income depends on quantification, or that right to payment of an ascertainable amount does not arise till accounts are made. Counsel also submitted that in sale transactions of a trading venture profits accrue to the trader from transaction to transaction and are embedded in each transaction carried on by the trader, and the charge imposed by Section 4(1)(a) is not deferred till settlement of accounts. On that premise, counsel said, that profits dormant or embedded in the transactions carried on by Messrs Amrit Chemicals accrued from transaction to transaction till November 12, 1955 and properly belonged to the assessee and were liable to be taxed in the hands of the assessee notwithstanding any subsequent disposition of those profits by the assessee. In support of his contention counsel relied upon Turner Morrison & Co. Ltd. v. CIT [23 ITR 152] — a case decided by this Court. In that case an Indian Company received commission on sales effected in India of goods received from a foreign company. The Indian Company handled the cargo arriving at Calcutta and made disbursements in connection therewith, collected and after deducting expenses including their commission remitted the balance to the foreign principal. It was held by this Court that the income, profits and gains derived from sale of goods by the Indian Company in British India were assessable to tax under Section 4(1)(a) as income, profits and gains received in the taxable territories by the Company on behalf of the foreign principal. The Court in that case observed at p. 160:*

> *"There can therefore, be no question that when the gross sale proceeds were received by the Agents in India they necessarily received whatever income, profits and gains were lying dormant or hidden or otherwise embedded in them. Of course, if on the taking of accounts it be found that there was no profit during the year then the question of receipt of income, profits and gains would not arise but if there were income, profits and gains, then the proportionate part thereof attributable to the sale proceeds received by the Agents in India were income, profits and gains received by them at the moment the gross sale proceeds were received by them in India and that being the position the provisions of Section 4(1)(a) were immediately attracted and the income profits and gains so received became chargeable to tax under Section 3 of the Act."*

8. *These observations were, it may be noticed, made in rejecting the contention raised by counsel for the taxpayer that in the gross sale proceeds received by him in India, there was no income at all. Counsel for the Indian Company said*

> *that the gross sale proceeds were merely credit items in the account and that several amounts were to be debited in the same account and if there remained any credit balance, such balance alone could be regarded as stamped with the formal impress of income capable of being dealt with as such : income could therefore be said to have been received only at that stage. The Court did propound that when gross sale proceeds are received in which is embedded income, that income will enter the ultimate computation of the total profits assessable to tax. But that is not to say that the profits accrue or arise to a trader from day to day or from transaction to transaction. The observation that to the income, profits and gains embedded in the gross receipts Section 4(1) was immediately attracted also does not warrant the inference that the Court intended to lay down that profits accrue to a taxpayer before the right thereto has come into existence.* ***"Profits" as pointed out in E.D. Sassoon Co. Ltd. case [26 ITR 27] do not accrue from day to day or even from month to month and have to be ascertained by a comparison of assets at two stated points. The Court also pointed out in that case that the test for ascertaining whether profits have accrued or arisen is whether the person who is entitled thereto has a right to claim the profits."***

23. Accordingly, where under a scheme of amalgamation the shareholder merely receives, in substitution, shares of the amalgamated company in lieu of the shares held in the amalgamating company, there is no real or completed profit capable of being taxed under Section 28, unless it is shown that the shares are held as stock-in-trade and are readily available for realisation. In the absence thereof, what takes place is only a statutory vesting and substitution of one form of holding for another. Unless and until the substituted shares are commercially realisable – whether saleable, tradeable, or by whatever other mode of disposition so described – so as to yield real income, no taxable event can be said to arise.

Definite valuation

24. The next test, which is well settled, is that profit must be capable of definite valuation, so that the real gain or loss stands crystallized. Judicial decisions have consistently underscored that "profits", in the commercial sense, are ascertainable only when the old position is closed and the new position is determined in terms of money's worth – whether by sale, transfer, exchange, or statutory substitution. This principle is an application of the doctrine of real income and applies with equal force to stock-in-trade as it does to other forms of commercial receipts. Therefore, the test is not satisfied merely by the receipt of realisable shares in substitution of earlier holdings; such shares must also be capable of quantification.

24.1. In ***Commissioner of Income Tax v. Woodward Governor India (P) Ltd***.[34], this Court reaffirmed the settled principles of commercial accounting, particularly that profits can be ascertained only by a comparison of assets at two defined points in time, and that unrealised gains embedded in stock-in-trade are not brought to charge unless and until they are crystallised in terms of money's worth. The following paragraphs are apposite:

> ***"28.*** *One more aspect needs to be highlighted. Under Section 28(i), one needs to decide the profits and gains of any business which is carried on by the assessee during the previous year. Therefore, one has to take into account stock-in-trade for determination of profits. The 1961 Act makes no provision with regard to valuation of stock. But the ordinary principle of commercial accounting requires that in the P&L account the value of the stock-in-trade at the beginning and at the end of the year should be entered at cost or market price, whichever is the*

[34] (2009) 13 SCC 1

lower. This is how business profits arising during the year need to be computed. This is one more reason for reading Section 37(1) with Section 145.

29. *For valuing the closing stock at the end of a particular year, the value prevailing on the last date is relevant. This is because profits/loss is embedded in the closing stock. While anticipated loss is taken into account, anticipated profit in the shape of appreciated value of the closing stock is not brought into account, as no prudent trader would care to show increased profits before actual realisation. This is the theory underlying the rule that closing stock is to be valued at cost or market price, whichever is the lower. As profits for income tax purposes are to be computed in accordance with ordinary principles of commercial accounting, unless, such principles stand superseded or modified by legislative enactments, unrealised profits in the shape of appreciated value of goods remaining unsold at the end of the accounting year and carried over to the following year's account in a continuing business are not brought to the charge as a matter of practice, though, as stated above, loss due to fall in the price below cost is allowed even though such loss has not been realised actually.*

30. *At this stage, we need to emphasise once again that the above system of commercial accounting can be superseded or modified by legislative enactment. This is where Section 145(2) comes into play. Under that section, the Central Government is empowered to notify from time to time the accounting standards to be followed by any class of assessees or in respect of any class of income. Accordingly, under Section 209 of the Companies Act, mercantile system of accounting is made mandatory for companies. In other words, accounting standard which is continuously adopted by an assessee can be superseded or modified by legislative intervention. However, but for such intervention or in cases falling under Section 145(3), the method of accounting undertaken by the assessee continuously is supreme.*

…….

33. *It is well established, that, on general principles of commercial accounting, in the P&L account, the values of the stock-in-trade at the beginning and at the end of the accounting year should be entered at cost or market value, whichever is lower—the market value being ascertained as on the last date of the accounting year and not as on any intermediate date between the commencement and the closing of the year, failing which it would not be possible to ascertain the true and correct state of affairs. No gain or profit can arise until a balance is struck between the cost of acquisition and the proceeds of sale.* ***The word "profit" implies a comparison between the state of business at two specific dates, usually separated by an interval of twelve months. Stock-in-trade is an asset. It is a trading asset. Therefore, the concept of profits and gains made by business during the year can only materialise when a***

comparison of the assets of the business at two different dates is taken into account."

24.2. Accordingly, in the context of amalgamation, the issue does not turn on the accrual of income in the abstract sense, but on whether the assessee has received a commercially realisable consideration in kind. Upon sanction of the scheme, there is only a statutory substitution of rights; no asset then exists in the hands of the assessee that is capable of commercial realisation. The charge under Section 28 crystallises only upon allotment of the new shares, when the assessee actually receives realisable instruments capable of valuation in money's worth. At that point, the old stock-in-trade ceases to exist and stands replaced by new shares having a definite market value. Since these shares are received in the course of business and in substitution of trading assets, their receipt represents a commercial profit or gain arising from business activity. What attracts Section 28 is, therefore, the receipt of shares coupled with their present realisability and their nexus with business. These three conditions—actual receipt, present realisability, and ascertainability of value—together determine the timing of taxability in cases of amalgamation. Consequently, the profit arising on receipt of the amalgamated company's shares may be taxed under Section 28 where the shares allotted are tradable and possess a definite market value, thereby conferring a presently realisable commercial advantage. This conclusion flows from the real income principle and not from any judicially created fiction. Equally, it must be emphasised that where such

attributes are absent, the Court cannot, by analogy, extend Section 28 to tax hypothetical accretions in the absence of an express statutory mandate.

24.3. It is further clarified that the principles enunciated herein lay down a fact-sensitive test. The enquiry whether, consequent upon an amalgamation, the allotment of new shares has resulted in a real and presently realisable commercial benefit must be determined on the facts of each case. The burden lies on the Revenue to establish the same. It is thereafter for the Tribunal, as the final fact-finding authority, to apply these principles to the evidence on record.

Timing of Taxability

25. Having established that the charge under Section 28 may be attracted if the shares are saleable, tradable, *etc.,* and of definite market value, thereby conferring a presently realisable commercial advantage, it becomes necessary to clarify the general principle. In the context of amalgamation, three points in time require to be distinguished. First, the appointed date specified in the scheme, which determines corporate succession and continuity between the transferor and transferee companies. Secondly, the sanction of the scheme by the Court, which gives statutory force to the amalgamation. At these stages, however, there is only a substitution of rights by legal fiction, without any asset in the hands of the shareholder capable of commercial exploitation. Thirdly, the allotment of new shares in the amalgamated company, which alone crystallises the benefit in the shareholder's hands, for it is only then that the old stock-in-

trade ceases to exist and is replaced by new shares of definite market value capable of immediate realisation. Even if the scheme contemplates the issue of shares in a certain ratio from the appointed date, until allotment there is no identifiable scrip or tradable asset in existence in the hands of the assessee. Thus, the charge under Section 28 is not attracted on the mere sanction of the scheme or on the appointed date, but only upon the receipt of the new shares, when the statutory substitution translates into a concrete, realisable commercial advantage.

26. Without prejudice to the broader question of chargeability under Section 28, it was contended on behalf of the appellants that even if the fair market value of the shares allotted in the amalgamated company exceeded the book value of the shares held in the amalgamating company, such excess would be merely hypothetical and illusory until the shares were sold, given that market value is inherently fluctuating. As discussed, the test under Section 28 is not postponed until an actual sale, but is satisfied once the assessee comes into possession of an asset of determinable and presently realisable value in substitution of its trading stock. The fact that such value may fluctuate subsequently does not render the benefit unreal; valuation for tax purposes is always carried out at a particular point in time, notwithstanding subsequent volatility. What matters is that, on the date of allotment, the assessee must have

received realisable instruments capable of being valued in money's worth, and such receipt constitutes a real, and not a notional, commercial gain.

Distinction between Capital and Business assets

27. Notably, Section 47 of the I.T. Act expressly carves out an exemption in respect of certain transfers in the context of amalgamation, but that exemption is confined to capital assets. The rationale is plain. Where a shareholder holds shares as an investment, the underlying object is to remain invested in the corporate venture, and a mere amalgamation ordinarily does not alter that position. While the possibility of tax avoidance in the investment field cannot be ruled out altogether, the legislative judgment reflects that the risk is relatively low. The exemption under Section 47 is thus founded on the recognition that amalgamation, in the capital field, is essentially a corporate restructuring and not a true realisation of profit. It is also common in business parlance for entities to hold shares either as investments or as stock-in-trade.

27.1. By contrast, Section 28, which governs profits of business, contains no such carve-out, nor could it be otherwise. The nature of stock-in-trade is wholly different from that of an investment. Stock-in-trade represents circulating capital: it is held not for preservation or appreciation, but for conversion into

money in the ordinary course of business. In ***Commissioner of Income Tax v. Express Newspapers Ltd***.[35] it was observed as follows:

> *"... The profits and gains of business and capital gains are two distinct concepts in the Income Tax Act: the former arises from the activity which is called business and the latter accrues because capital assets are disposed of at a value higher than what they cost the Assessee. They are placed under different heads; they are derived from different sources; and the income is computed under different methods....."*

27.2. In this context, the substitution of one trading asset by another, such as the receipt of shares in an amalgamated company in lieu of shares held as stock-in-trade in the amalgamating company, cannot be equated with a mere continuation of an investment. It represents a commercial realisation in kind, for the new shares are distinct assets with a definite and presently realisable market value.

27.3. If amalgamations involving trading stock were insulated from tax by judicial interpretation, it would open a ready avenue for tax evasion. Enterprises could create shell entities, warehouse trading stock or unrealised profits therein, and then amalgamate so as to convert them into new shares without ever subjecting the commercial gain to tax. Equally, losses could be engineered and shifted across entities to depress taxable income. Unlike genuine investors who merely restructure their holdings, traders deal with stock-in-trade as part of their profit-making apparatus; to exempt them from charge at the point of substitution would undermine the integrity of the tax base.

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[35] MANU/SC/0126/1964 : 1964 INSC 152

27.4. Accordingly, while the Act makes an express exception for amalgamation of capital assets, no such exception is contemplated in the case of business assets. Section 28 is deliberately cast in wide terms to bring to tax real and presently realisable profits arising in the course of business, and in the context of stock-in-trade, the allotment of shares upon amalgamation constitutes precisely such a taxable realisation.

Application to the present case

28. In the present case, the Tribunal, relying on ***Rasiklal Maneklal***, held that no "transfer" occurs in a scheme of amalgamation. The High Court, however, found this view unsustainable, observing that under the 1961 Act, as clarified in ***Grace Collis***, the extinguishment of rights in the shares of the amalgamating company constitutes a "transfer" within the meaning of Section 2(47). Since such transfer is exempt under Section 47(vii) only in respect of capital assets, the High Court proceeded to examine whether shares held as stock-in-trade would nonetheless give rise to taxable business income under section 28.

28.1. The High Court reasoned that once the shares of the amalgamating company ceased to exist and were substituted by shares of the amalgamated company, there was a cession of the old trading stock and its replacement by a new commodity of ascertainable market value. On this footing, it held that a realisation of business profit had occurred, taxable under Section 28. Relying

upon ***Orient Trading*** and ***Hindustan Lever***, the Court observed that shares received on amalgamation are fundamentally new assets, and the process results in realisation of value irrespective of shareholder status. The taxable event, therefore, depends on the substance of the transaction and not merely accounting entries. On this reasoning, the Tribunal's findings were set aside, the question of law was answered in favour of the Revenue, and the matter was remitted to the Tribunal.

29. As already noticed, the correctness of this reasoning constitutes the core issue in the present appeals. In view of the foregoing discussions, we reiterate that Section 28 of the I.T. Act is of wide import and encompasses all profits and gains arising in the course of business, even when such profit is realised in kind. The statutory substitution of shares of the amalgamating company by shares of the amalgamated company is not a mere neutral replacement; where the new shares are freely marketable and possess a definite commercial value, the event constitutes a commercial realisation giving rise to taxable business income. The principle laid down in ***Orient Trading*** and similar authorities makes it clear that such profit need not await actual sale if the benefit received is real and presently realisable.

30. We thus hold that where the shares of an amalgamating company, held as stock-in-trade, are substituted by shares of the amalgamated company pursuant to a scheme of amalgamation, and such shares are realisable in money and

capable of definite valuation, the substitution gives rise to taxable business income within the meaning of Section 28 of the I.T. Act. The charge under Section 28 is, however, attracted only upon the allotment of new shares. At earlier stages namely, the appointed date or the date of court sanction, no such benefit accrues or is received.

31. Accordingly, the main issue is answered in favour of the Revenue, in principle holding that the receipt of shares of the amalgamated company in substitution of stock-in-trade can give rise to taxable business profits under Section 28. However, the actual application of this principle to the facts of the present case, including whether the shares received are freely realisable or otherwise subject to restrictions, or whether the shares are held only as investment, is a matter requiring factual determination. In these circumstances, the proper course is to remit the matter to the Tribunal for fresh adjudication in accordance with law.

32. Before parting, we may observe that business, by its very nature, admits of profits arising in diverse forms, whether in money or in kind, yet the common denominator is that the benefit must be concrete, capable of commercial realisation, and not a mere paper re-arrangement. Amalgamation, as a statutory substitution, ensures continuity of enterprise but also extinguishes one form of holding and replaces it with another. As we have held, where such substitution confers on the assessee realisable assets of definite market value, a commercial

realisation takes place, and Section 28 is attracted. At the same time, courts must remain alive to the distinction between genuine commercial gain and hypothetical accretion. The touchstone is, therefore, the doctrine of real income, applied with due regard to the facts of each case, ensuring that the tax charge operates neither oppressively nor evasively, but in harmony with the legislative design, to tax true profits of business, however manifested, while eschewing illusory gains.

33. In fine, the judgment of the High Court is affirmed, and all these appeals stand disposed of in the aforesaid terms. There is no order as to costs.

34. Pending application(s), if any, shall stand disposed of.

……J.
[J.B. PARDIWALA]

……J.
[R. MAHADEVAN]

NEW DELHI;
JANUARY 09, 2026.