

First Income-Tax Officer, Salem

Vs

Short Brothers (P.) Ltd

Civil Appeal No. 97 of 1965

(K. Subha Rao, J. C. Shah, S. M. Sikri JJ)

15.12.1965

JUDGMENT

SHAH J. –

On December 24, 1959, Messrs. Short Brothers (Private) Ltd. sold its coffee estates and other assets, and by resolution dated February 6, 1960, it was resolved that it be voluntarily wound up and liquidators be appointed to administer its affairs. Out of the proceeds realized by sale of its assets, the liquidators of the company distributed on March 30, 1960, Rs. 8,50,000 to the shareholders. By letter dated December 19, 1960, the Income-tax Officer, Salem, informed the liquidators that he proposed to treat that amount distributed as dividends in the hands of the shareholders, and to call upon the liquidators to pay the amount of tax deductible under section 18(3D) of the Income-tax Act. The liquidators submitted that the amount distributed to the shareholders was capital appreciation realised by sale of agricultural lands and buildings of the company, and was not liable to tax, and that in any event the amounts distributed represented "current profits" of the year in which it was resolved that the

The liquidators then moved the High Court of Judicature at Madras, for a writ of prohibition restraining the First Income-tax Officer from taking further action to enforce collection of the amount referred to by him in his communication dated October 18, 1962. Holding that the demand made by the Income-tax Officer was "not in conformity with the law" in that the amount of Rs. 8,50,000 which had been distributed as dividend without determining whether any portion of the amount represented capital gains, which arose out of the sale of capital assets consisting of lands from which agricultural income was derived, the High Court issued a writ restraining the Income-tax Officer from enforcing the demand for tax. The High Court reserved liberty to the Income-tax Officer to examine the question afresh, and to determine "the correct amount of dividend within the meaning of section 2(6A)(c)". With special leave, the First Income-tax Officer has appealed to this court.

It was submitted on behalf of the Income-tax Officer that the High Court, in entertaining the petition in its extraordinary jurisdiction under article 226 of the Constitution, by-passed the machinery of assessment and rectification of orders of assessment prescribed by the Indian Income-tax Act which is both adequate and efficacious. But the High Court has, under article 226 of the Constitution, jurisdiction to issue to any person or authority within the territories in relation to which it exercises jurisdiction, directions, orders, or writs in the nature, amongst others, of mandamus, prohibition and certiorari for the enforcement of any of the right conferred Court will not entertain a petition in exercise of its jurisdiction under article 226 of the Constitution when the party claiming relief has an alternative remedy which is adequate and efficacious. The question however is one of discretion of

the High Court and not of its jurisdiction, and if the High Court in exercise of their discretion thought that

The High Court was of the view that all profits accumulated in the previous years and the profits till the date on which it was resolved that the company be voluntarily wound up would be included in the expression "accumulated profits" under section 2(6A)(c) of the Indian Income-tax Act read with the Explanation. They held that even capital gains taxable under section 12B except for the period mentioned in the Explanation were, when distributed, "dividend" within the definition, but profits realised by transfer of property used for agricultural purposes and which yielded agricultural income not being capital gains taxable under the law are not "dividend", and on that account the order of the Income-tax Officer bringing to tax the entire amount distributed without determining whether any portion of that amount represented capital gains arising from the sale of capital assets consisting of lands from which agricultural income was derived was not within his authority.

Counsel for the liquidators contended in the first instance that all profits whatever may be their character arising in the year in which the company is voluntarily wound up are not liable to be taxed as they did not fall within the definition of "dividend" in section 2(6A)(c). Counsel for the department, while supporting the view of the High Court relating to the chargeability to tax of "current profits", contended that the entire amount of Rs. 8,50,000 distributed to the shareholders, whatever may be the source from which the profits were earned, was liable to be brought to tax under section 12 of the Income-tax Act as dividend distributed.

By section 12 of the Income-tax Act, tax is payable by an assessee under the head "Income from other sources" in respect of income, profits and gains of every kind which may be included in his total income if not included under any of the preceding heads in section 7 to 10 of the Act. By subsection (IA) "Income from other sources" includes dividends. Section 2(6A) defines "dividend", and at the relevant time clause(c) and the Explanation to the clause stood as follows :

"Dividend' includes -

(c) any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not;...

Explanation. - The expression 'accumulated profits' wherever it occurs in this clause, shall not include capital gains arising before the 1st day of April, 1946, or after the 31st day of March, 1948, and before the 1st of April, 1956." By the Explanation to section 2(6A) accumulated profits include capital gains not arising within the excepted period. The Explanation is undoubtedly couched in negative form, but there is no ground for accepting the argument of counsel for the department that in the substantive clauses of the definition, accumulated profits do not include capital gains. The Explanation plainly implies that within the expression "accumulated profits" are included capital gains outside the excepted periods. On the interpretation contended for by counsel for the department, the Explanation which seeks to exclude "capital gains" from the content of accumulated profits would have no meaning. By subsection (1) of section 12B tax is payable by an assessee under the head "capital gains" in respect

The contention raised by counsel for the company that the profits earned in the "current Year", i.e.,

the year in which it was resolved that the company be wound up, were not "dividend" within the meaning of section 2(6A)(c) of the Act cannot be accepted. Sub-clause (c) of section 2(6A) declares that accumulated profits, immediately before the liquidation of the company, are dividend : it does not say that accumulated profits up to the end of the previous year immediately preceding the year in which liquidation of the company commences are dividend. It is true that in giving effect to the definition, the taxing authorities have to compute profits of the company for a part of the year, but that is not a ground for reading the plain words of the statute in an artificial sense. Under section 3 of the Act read with section 4, the charge to income-tax is on the total income of the previous year, and in accordance with and subject to the provisions of the Indian Income-tax Act. But there is nothing in the Act which p

In amending the definition in section 2(6A)(c) by the Finance Acts of 1955 and 1956, Parliament has sought to clarify its meaning and to avoid the argument which was successfully raised in certain cases on the interpretation of the statute before it was amended. By the terms of the definition, distribution which is attributable to the accumulated profits of the company immediately before its liquidation is to be deemed dividend. Thereby all profits earned till immediately before liquidation, if they are distributed, will be brought to tax wholly if they consist of accumulated profits, or partially to the extent they are attributable to accumulated profits.

Amendments which have been made from time to time in the Act clearly disclose the intention of Parliament that it was not intended to allow the profits of the current year distributed by a liquidators of a company to escape liability to tax. In *Inland Revenue Commissioners v. George Burrell* it was held that on the undivided profits of past years and of the year in which the winding up of a company occurred which were distributed among the shareholders, super-tax was not payable, because in the winding up they had ceased to be profits and were assets only. It was observed in *Burrell's* case that the only thing the liquidators of a company in liquidation may do is to turn the assets into money, and divide the money among the shareholders in proportion to their shares. Surplus of trading profit made in a particular year are distributable rateably among all the shareholders as capital, and it is not right to split up the sums received by the shareholders into capital and income, by examining the accounts of the

"Dividend' includes -

(c) any distribution made to the shareholders of a company out of accumulated profits of the company on the liquidation of the company :

Provided that only the accumulated profits so distributed which arose during the six previous years of the company preceding the date of liquidation shall be so included."

By the Finance Act, 1955, the proviso to sub-clause (c) of clause (6A) was omitted. There was a further amendment made by the Finance Act, 1956, and clause (c) to the amended section read as follows :

"Dividend' includes - ...

(c) any distribution made to the shareholders of a company on its liquidation, to the extent to which the distribution is attributable to the accumulated profits of the company immediately before its liquidation, whether capitalised or not."

Under Act 7 of 1939 profits which arose within six previous years preceding the date of liquidation when distributed were to be deemed dividends. But the effect of the definition was that distribution of profits accumulated after the last day of the previous year whatever their nature could not be regarded as distribution of dividend : Sheth Haridas Achratlal v. Commissioner of Income-tax it was held in that case by the Bombay High Court that for the purpose of section 2(6A)(c) as it stood in 1949, a broken period between the last day of the previous year of a company and the commencement of winding up could not be considered "a previous year". Parliament, with a view in Sheth Haridas Achratlal's Case deleted by the Finance Act, 1955, the proviso to sub-clause (c). To make its meaning more clear Parliament by the Finance Act, 1956, recast the substantive clause (c). Viewed in the context of this legislative history, there is no doubt that "current profits", i.e., profits of a company in liquidation arising

The question which remains to be considered is whether capital appreciation in respect of the lands from which the income derived is agricultural income and which was not taxable in the hands of the company as capital gains would still on distribution be liable to be taxed as dividend under section 12 of the Income-tax Act. As we have already pointed out, capital gains under section 12B are chargeable in respect of any profits arising from transfer of "capital assets", and "capital assets" do not include lands from which the income derived is agricultural income. Profits derived by transfer of lands from which the income derived is agricultural income would not, therefore, be chargeable on a combined reading of section 12B with section 2(4A) of the Income-tax Act under the head "Capital gains". The expression "accumulated profits" does not include capital gains arising within the excepted periods : vide Explanation to section 2(6A). "Accumulated profits" are, therefore, profits which are so regarded in comme

Counsel for the department contended, relying upon Mrs. Bacha F. Guzdar v. Commissioner of Income-tax that since dividend received by a shareholder of a company out of the profits earned from agricultural income is not exempt from liability to pay tax under section 4(3)(viii), dividend distributed from profits earned out of sale of capital assets inclusive of lands from which the income derived is agricultural income is also not exempt from Income-tax. But the company does not claim exemption from liability to tax under section 4(3)(vii) : it claims exemption because the receipt is not income which is chargeable to tax under section 12 under the head "dividend". The case of Mrs. Bacha F. Guzdar has, therefore, no application to this case.

The appeal, therefore, fails and is dismissed with costs.

Appeal dismissed.

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