

Calcutta Tramways Co. Ltd.

Vs

Commissioner of Wealth-Tax.

Civil Appeals Nos. 28-30 of 1969

(H. R. Khanna, K. S. Hedge, P. Jagmohan Reddy JJ)

28.08.1972

JUDGMENT

HEGDE J. -

1. These are assessee's appeals by certificate, from the judgment of the High Court of Calcutta in a reference under section 27(1) of the Wealth-tax Act (to be hereinafter referred to as "the Act"). At the instance of the assessee (which will hereinafter be referred to as the "company"), as well as the Commissioner of Wealth- tax, West Bengal, the Income-tax Appellate Tribunal, "B" Bench, Calcutta, referred the following question to the High Court for its opinion :

" (1) Whether, on the fact and in the circumstances of the case, the amounts of pound 1,99,940, pound 1,92,907 and pound 98,017 standing in the special reserve account in the books of the assessee-company were deductible in determining the net wealth of the company for the assessment years 1957-58, 1958-59 and 1959-60, respectively ?

(2) Whether, on the facts and in the circumstances of the case, the amount of pound 1,54,434, pound 2,08,934 and pound 2,62,811 standing in the shareholders' accounts as on the respective valuation dates were deductible in determining the net wealth of the company for the assessment years 1957-58, 1958-59 and 1959-60 respectively ?

(3) Whether, on the facts and in the circumstances of the case, the amounts of pound 66,275, pound 131,180 and pound 274,587 out of the debentures of the company were allowable as debts owed by the company in the light of section 2(m) read with section 6 of the Wealth-tax Act ?"

The High Court Answered all the three questions in favour of the revenue. Hence these appeals.

The assessee is a sterling company. In the relevant assessment years, it was operating the Calcutta Tramways Co. It is a non-resident company for the purpose of Explanation 2 to section 6 of the Act. The assessment years with which we are concerned in these appeals are 1957-58, 1958-59 and 1959-60 and the relevant valuation dates are 31st December, 1956, 31st December, 1957, and 31st December, 1958, respectively. The wealth-tax Officer valued the assets of the company under section 7(2)(a) of the Act.

In 1951 the Government of West Bengal proposed to acquire the undertaking of the Calcutta Tramways Co. Ltd. In pursuance of that policy, the Government entered into an agreement with the

company on August 30, 1951. This agreement was later given statutory force. The clauses of the agreement which are relevant for our present purpose are 4,7 and 8. They read :

"4. (1) The company shall apply its revenue in the manner following that is to say -

(a) Firstly, paying all expenses of managing, maintaining and working the undertaking, including debenture interest;

(b) Secondly, paying all Indian and United Kingdom taxes payable by the company;

(c) Thirdly, setting aside in each accounting year in a Renewals and Replacements Reserve Account the sum of eight thousand pounds sterling or such greater sum as the directors of the company for the time being may in consultation with the Government consider necessary in the light of experience and in view of the expansion of the undertaking or increase in prices;

(d) Fourthly, setting aside in each accounting year in fund (hereinafter called 'the shareholders' Account') the following sum :

(i) Pound 87,457 together with, (ii) four per cent. upon any additional outside share capital raised by the company with the consent of the Government after the date of this agreement.

(e) Fifthly, accumulating any surplus in a special reserve account the balance of which (after providing for losses, if any) will eventually accrue to the benefit of the Government. (Before such transfer, however, of a loan against the credit standing in the Special Reserve Account, the Government should be consulted, the final decision on such matter nevertheless being reserved to the company.

(2) If in any accounting year the revenue arising from the undertaking are insufficient to provide for all the matters enumerated in the preceding sub-clause of this clause, such revenue shall be so applied in the priority there set out.

7. (1) Not later than twelve months before the purchase date the Government may serve upon the company notice in writing (hereinafter called ' a purchase notice') of its intention to acquire the undertaking on the purchase date.

(2) In the event of the Government serving a purchase notice the following provisions shall have effect that is to say :-

(a) The Government shall subject to the exchange regulations and other relevant laws prevailing at the time in the United Kingdom and India pay to the company in sterling in London not less than thirty days before the purchase date :-

(i) the sum of Rs. pound 3,750,000;

(ii) a sum of equal to the amount of any additional outside capital brought into the undertaking with the consent of Government under clause 6(1) of the agreement during the period between the date of this agreement and the first day of January one thousand nine hundred and seventy-one.

(b) Subject to payment being made in terms of sub-clause (a) above all the right, title and interest of the company of and in the undertaking shall on the purchase date become vested in the Government free from all mortgages, charges and liens created by the issue of debenture or debenture Stocks of the company. Provided that the Company shall be entitled to retain all statutory books of account and others documents normally kept outside India but shall afford every facility to the Government to have inspection of the same or take copies of or extracts therefrom.

(c) The Government shall also pay to the company in sterling in London, the amount of the balance (if any) of the Shareholders' Account at the purchase date within one month after a certificate by the Company's auditors of the amount thereof has been served on the Government.

(d) No further sum than is provided for in this clause shall be payable to the company in respect of the transfer of the undertaking to the Government.

(3) From and after such vesting of the undertaking in the Government all powers, rights, obligations and liabilities excepting the liabilities in respect of the share and loans capital of the company shall be exercisable by and be binding on the Government in substitution for the company and shall cease to be exercisable by or binding on the company.

Provided that no contract entered into by the company after the date of this agreement and extending for more than one year beyond the purchase date shall be binding on the Government unless it has been previously approved by the Government.

8. If the Government does not serve a purchase notice in accordance with the last preceding clause, then all the terms and conditions of this agreement shall continue in force subject to the following modifications :-

(a) (i) The Government shall pay to the company in sterling in London such sums as may from time to time be necessary to redeem the second debenture stocks of the company on their due dates;

(ii) After the second debenture stocks have been redeemed as aforesaid the company shall from time to time until the undertaking is vested in the Government pay to the Government sums equal to the interest which would have been payable on such debenture stock had the same not been redeemed.

(b) (i) The Government shall on giving two year's notice to the company be entitled to acquire the undertaking on the 1st day of January of any subsequent year and such date shall be the purchase date.

(ii) In the event of the undertaking being acquired in pursuance of a notice under this clause there shall be deducted from the sum payable under clause 7(2)(a)(i) hereof any sums which may have been paid by the Government in pursuance of paragraph (a)(i) of this clause."

In compliance with the provision in the agreement, the company maintained a special reserve. The

amounts lying to the credit of that account on the respective valuation dates were pound 1,99,407, pound 1,92,940 and pound 89,017. The company also maintained shareholders account in its books as required by clause 4(1)(d) of the agreement. Amounts credited to the said account on the relevant valuation dates stood at pound 1,54,434, pound 2,08,934 and pound 2,62,811, respectively.

The company had issued debentures which were secured by a floating charge on the general assets of the company. The assets of the company located outside India were valued at pound 4,27,786, pound 3,51,888, and pound 1,95,916 on the respective valuation dates. The company's assets in India on those dates were valued at pound 2,930,032, pound 3,010,560 and pound 3,119,149. All the debenture-holders were residents in the United Kingdom. The specialties were in the United Kingdom and the debts were payable in that country.

The company claimed the accounts in special reserve accounts, those in the shareholder reserve account as well as debenture loans as debts deductible in ascertaining the net wealth of the company. The Wealth-tax Officer rejected those contentions. In appeal the Appellate Assistant Commissioner agreed with the Wealth-tax Officer in his finding relating to the amounts in the special reserve account as well as in the shareholders' account. But, as regards the debenture loans, he distributed the same on the basis of the assets held by the company in the United Kingdom and those held by it in this country. Consequently, he gave deduction in respect of that portion of the debt which according to him should be borne by the assets in India. Both the Commissioner as well as the company appealed to the Tribunal. The Tribunal disagreed with the conclusions reached by the Appellate Assistant Commissioner that any portion of the debenture loans could be taken into consideration in ascertaining the net wealth of the assessee. It agreed with the Wealth-tax Officer and the asset of the company. It opined that the amounts Appellate Assistant Commissioner that the shareholders' reserve was the asset of the company. It opined that the amounts in the special reserve account were not includible in the special reserve account were not includible in the company's net wealth. But, as mentioned earlier, the High Court fully accept the conclusions reached by the Wealth-tax Officer.

Before considering the points arising for decision it is necessary to refer to the relevant provisions of the Act. "Net wealth" is defined in section 2(m) of the Act thus :

"net wealth" means the amount by which the aggregate value computed in accordance with the provision of this Act of all the assets, wherever located, belonging to the assessee on the valuation date, including assets required to be included in his net wealth as on that date under this Act, is in excess of the aggregate value of all the debts owed by the assessee on the valuation date other than, -

(i) debts which under section 6 are not to be taken into account.

# \* \* \* \*##

Section 3 is the charging section. It says :

"Subject to the other provisions contained in this Act, there shall be charged for every assessment year commencing on and from the first day of April, 1957, a tax (hereinafter referred to as wealth-tax) in respect of the net wealth on the corresponding valuation date of every individual, Hindu undivided family and company at the rate or rates specified in the Schedule."

Section 4 prescribes what all assets should be taken into consideration in computing the net wealth. Section 5 provides for certain exemptions. Those exemptions are not relevant for our present purpose. Then we come to section 6 which is important for our present purpose. The portion of that section which is material for our present purpose reads :

"In computing the net wealth of an individual who is not a citizen of India or of an individual or a Hindu undivided family not resident in India or resident but not ordinarily resident in India, or of a company not resident in India during the year ending on the valuation date -

(i) the value of the assets and debts located outside India; and ...

shall not be taken into account.

Explanation 1. - .....

Explanation 2. - A company shall be deemed to be resident in India during the year ending on the valuation date, if -

(a) it is a company formed and registered under the Companies Act, 1956, or is an existing company within the meaning of that Act; or

(b) during that year the control and management of its affairs is situated wholly in India."

Now that we have before us the material facts and the relevant provisions of the Act, we shall proceed to examine the question of law referred to the High Court for its opinion. Coming to question No. 1, the contention of the company was that under law, it was compelled to build up a special reserve. It could not deal with the same except in accordance with the provisions of the agreement. Hence the same cannot be considered as the asset of the company. This is the wholly untenable contention. No part of the assets of the company had been acquired by the Government. Between the Government and the company, there was only an agreement. The Government could not have acquired the company before the "purchase date" viz. January 1, 1972. Even after that date, only an option is given to the Government to acquire the company. The Government could not be compelled to acquire the company. The agreement had fixed the consideration to be paid for the acquisition of the company. Till the company was acquired, the amounts shown in the special reserve were the assets of the company. Once we come to the conclusion that they were not the assets of the Government, which conclusion that to our mind is obvious, then it follows that they are assets of company. It is not the case of the company that those assets belonged to some third party. Every item of asset must belong to someone. The question is to whom did it belong ? The obvious answer is that it belonged to the company. It is not the case of the company that the asset in question came within any of the exemptions mentioned in the Act.

Now, coming to the second question formulated for the opinion of the High Court which relates to the amounts in "shareholders' account", the contention of the company was that the amount belonged to the shareholders and, therefore, it was not an item of the assets of the company. This again is an unacceptable contention. A company is a different legal entity from its shareholders. The shareholders have no rights in the assets of the company except when dividends are declared or when the assets of the company are distributed on liquidation. Until a company in its general meeting accepts the recommendation of the director and declares dividends, no part of the profits of

the company becomes debt due to the shareholders. In *Kesoram Industries and Cotton Mills Ltd. v. Commissioner of Wealth-tax*, this court ruled that until the company in its general body meeting accepted the recommendations of its directors and declared the dividends, the report of the directors in that regard was only a recommendations and the same may be withdrawn or modified. In that case the company in its general body meeting had not declared dividends before the relevant valuation date. Hence this court held that on the valuation date nothing had happened beyond mere recommendation by the directors as to the amounts that might be distributed as dividends. Consequently, there was no debt owed by the company to the shareholders on that date. Hence the proposed dividend was not deductible in computing the net wealth of the appellant-company. The fact that a separate shareholders' reserve had to be maintained by the company because of its agreement with the Government did not change the character of the asset.

This takes us to the last question. As already mentioned the debenture loans were raised in the United Kingdom. All the debenture holders were resident in the United Kingdom. The specialties were in the United Kingdom. The debts were payable in the United Kingdom. Those debenture loans had only a floating charge on the assets of the company. No particular portion of the assets were specially charged. The meaning of a floating charge is explained in *Halsbury's Laws of England*, 3rd edition, volume 6, page 472, paragraph 914, thus :

"The terms 'floating security' and 'floating charge' mean a security or charge which is not to be put into immediate operation, but is to float so that the company is to be allowed to carry on its business. It contemplates, for instance, that book debts may be extinguished by payment, and other book debts may come in and take the place of those that have disappeared. While a specific charge is one that, without more, fastens on ascertained and definite property or property capable of being ascertained and defined, a floating charge moves with the property which it is intended to affect, until some event occurs or some act is done which causes it to settle and fasten on the subject of the charge within its reach and grasp. It is of the essence of a floating charge that it remains dormant until the undertaking charged ceases to be a going concern, or until the person in whose favour the charge is created intervenes. His right to intervene may be suspended by agreement, but if there is no such agreement he may exercise his right whenever he pleases after default."

Quite clearly the debts in question were located in the United Kingdom. Dealing with the business debts this is what is stated in *Halsbury's Laws of England*, 3rd edition, volume 15, page 58, paragraph 115 :

"Simple contract debts, including those owing under bills of exchange and promissory notes, are situate where the debtor resides. A debtor company may for this purpose be resident in any country where it has a branch office."

A specialty debt is in general an asset situate where the instrument is physically situate. In particular, a judgment debt is situate where the judgment is recorded. A debt secured by mortgage of land is in character primarily a debt, with an accessory right to resort to the land for payment, not an estate in the land measured by the amount of the debt; its locality as an asset of the mortgage is therefore to be determined prima facie under the rules relating to debts.

A share in a partnership business and the goodwill of a business are each situate

where the business is carried on."

From what has been said above, it is clear that the debenture loans in question cannot be taken into consideration is ascertaining the net wealth of the company in view of section 6 of the Act.

In the result these appeals fail and they are dismissed with costs- advocates' fee one set.

Appeals dismissed.

</html