Commissioner of Income Tax, Madras

Vs

M/s. Madurai Mill Co. Limited

Civil Appeal No. 1394 (NT) of 1970

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

09.03.1973

JUDGMENT

KHANNA, J. –

1. This appeal on certificate has been filed by the Commissioner of Income Tax against the judgment of the Madras High Court whereby that court answered the following question referred to it under Section 66(1) of the Indian Income Tax Act, 1922 (hereinafter referred to as the Act) in the negative in favour of the assessee-respondent :

> "Whether on the facts and circumstances of the case, the Tribunal was right in holding that the sum of Rs. 95,944/- is liable to tax under Section 12-B(2) ?"

2. The matter relates to the assessment year 1961-62. The assessee is a public limited company carrying on the business of manufacture and sale of yarn. The assessee held shares in the following companies as under :

> "(1) Indian Mills Supply Company (Private) Limited, 2,760 shares of the face-value of Rs. 100/-
>
> "(2) Harveys (Private) Limited, 1,000 shares of the face-value of Rs. 100/-
>
> "(3) Pandyan Weaving Mills (Private) Limited, 1,800 shares of the face-value of Rs. 100/-

The above three companies went into voluntary liquidation in December, 1959. In the course of the liquidation proceedings, the liquidators made distribution in the relevant year of account and the assessee company got cash or assets in lieu of cash of the account of Rs. 4,57,858, Rs. 1,41,739 and Rs. 1,83,175 in respect of Indian Mills Company (Private) Limited, Harveys (Private) Limited and Pandyan Weaving Mills (Private) Limited, respectively. The revenue took the view that by reason of the distribution of assets of the three private companies under liquidation by the liquidators, there had been a capital gain of Rs. 96,735.85 in respect of Indian Mills Supply Company (Private) Limited and Rs. 41,168.88 in respect of Harveys (Private) Limited making a total of Rs. 1,37,904.73. Out of that, loss amounting to Rs. 41,960.56 in respect of Pandyan Weaving Mills (Private) Limited was deducted, leaving a balance of Rs. 95,944.00. The assessee-company at first showed the sum of Rs. 95,944.00 as capital gains but subsequently it filed a statement showing a loss of Rs. 59,104 on the basis that the cost of shares distributed by the liquidators should be taken at the figure at which they had been acquired by the companies which distributed the shares. The

Income Tax Officer assessed the assessee-company to capital gain at the sum of Rs. 95,944. Aggrieved by the order of the Income Tax Officer the assessee filed appeal before the Appellate Assistant Commissioner and on being unsuccessful there, filed further appeal before the Income Tax Appellate Tribunal. The main contention which was raised on behalf of the assessee was that the transaction in question involved no sale, exchange, relinquishment or transfer and as such, the amount in question was not capital gain under Section 12-B of the Act. The Appellate Assistant Commissioner was of the view that the surplus arose out of the exchange of shares held by the assessee-company in the three companies and therefore the surplus ought to be brought to tax. The Tribunal held that there was an exchange or transfer of shares and assets in question. The transaction, according to the Tribunal, could also be viewed as a relinquishment. The assessee was consequently held liable to pay tax on the sum of Rs. 95,944 under Section 12-B of the Act. The question reproduced above was thereafter, on the application of assessee, referred to the High Court.

3. The High Court while answering the question in the negative held that when a liquidator distributes the assets of a company which has gone into voluntary liquidation, he is performing a legal function and there is no element of sale, transfer, exchange or relinquishment involved in such distribution. The judgment of the High Court is reported in (1969) 74 ITR 623.

4. Before dealing further, we may mention that capital gains were charged for the first time by the Income Tax and Excess Profits Tax (Amendment) Act, 1947 (Act 22 of 1947) which inserted Section 12-B in the Act. It taxed capital gains arising after March 31, 1946. The tax on capital gains was virtually abolished by the Indian Finance Act, 1949 which confined the operation of that section to capital gains arising before April 1, 1948. Capital gains tax was, however, revived with effect from April 1, 1957 by the Finance (No. 3) Act of 1956. Sub-section (1) of Section 12-B along with its first proviso was as under :

> "The tax shall be payable by an assessee under the head 'capital gains' in respect of any profits or gains arising from the sale, exchange, relinquishment or transfer, of a capital asset effected after the 31st day of March, 1956, and such profits and gains shall be deemed to be income of the previous year to which the sale, exchange, relinquishment or transfer took place :
>
> Provided that any distribution of capital assets on the total or partial partition of a Hindu undivided family or under a deed of gift, bequest or will, shall not for the purposes of this section be treated as a sale, exchange, relinquishment or transfer of the capital assets...."

Sub-section (2) of Section 12-B prescribed a statutory formula for purposes of computation of capital gains. Sub-section (3) of Section 12-B was as under :

> "Where any capital asset became the property of the assessee by succession, inheritance or devolution or on any distribution of capital assets on the total or partial partition of a Hindu undivided family or on the dissolution of a firm or other association of persons or on the liquidation of a company or under a deed of gift, or transfer on irrevocable trust, its actual cost allowable to him for the purposes of this section shall be its actual costs to the previous owner thereof, and the provisions of sub-section (2) shall apply accordingly; and where the actual cost to the previous owner cannot be ascertained, the fair market value at the date on which the capital asset became the property of the previous owner shall be deemed to be the actual cost

thereof....."

5. Perusal of sub-section (1) of Section 12-B reproduced above shows that the liability to pay tax on account of capital gains can arise only if the assessee makes profits or gains arising from the sale, exchange, relinquishment or transfer of a capital asset effected after March 31, 1956. The question with which we are concerned is whether the distribution of assets of the companies which had gone into voluntary liquidation by the liquidators to the assessee-company resulted in a transaction which amounted to sale, exchange, relinquishment or transfer.

6. Mr. Manchanda on behalf of the appellant has argued in this Court that the transaction in question amounted to sale or transfer. We, however, find ourselves unable to accede to this contention. The act of each of the liquidators in distributing the assets of the company which had gone into voluntary liquidation did not result in the creation of new rights. It merely entailed recognition of legal rights which were in existence prior to the distribution. According to observations on page 512 of Buckley's Commentaries on the Companies Act, thirteenth edition, a liquidator is only a trustee in the sense that the property of the company ceases upon the winding up to belong beneficially to the company and passes into his custody, to be applied by him as directed by the statue. It is further observed on page 513 :

> "The question whether a liquidator in a voluntary winding up is a trustee within the meaning of the Trustee Act, 1925, and as such entitled to the benefit of Sections 30 and 61 of that Act, was discussed, but not decided, In re Windsor Steam Coal Co. Semble, ((1929) 1 Ch 151) a liquidator is in the position of a trustee for the members when distributing surplus assets in specie in a winding up, so that 'no beneficial interest passes in the property conveyed or transferred' within the Finance (1909-1910) Act, 1910, Section 74(6), and ad valorem stamp duty under that section is not payable on conveyances or transfers of the property to the members."

7. When a shareholder receives money representing his share on distribution of the net assets of the company in liquidation, he receives that money in satisfaction of the right which belonged to him by virtue of his holding the shares and not by operation of any transaction which amounts to sale, exchange, relinquishment or transfer. In the circumstances, we find it difficult to hold that the assessee-company is liable to pay tax on capital gains as contemplated by Section 12-B of the Act, in respect of the amount of Rs. 95,944.

8. In the case of Commissioner of Income Tax, U.P. v. Bankey Lal Vaidya ((1971) 79 ITR 594 : (1971) 1 SCC 355) (to which one of us was a party) the respondent who was a karta of a Hindu undivided family, entered into a partnership with D to carry on the business of manufacturing and selling pharmaceutical products and literature relating thereto. On the dissolution of the partnership, its assets, which included goodwill, machinery, furniture, medicines, library and copyright in respect of certain publications, were valued at Rs. 2,50,000. Since most of the assets were incapable of Physical division, it was agreed that the assets be taken over by D and the respondent be paid his share of the value of the assets in money and accordingly the respondent was paid Rs. 1,25,000. Question arose whether the sum of Rs. 65,000 being part of the amount received by the respondent could be brought to tax as capital gains under Section 12-B of the Act. It was held by Shah, J., speaking for the Court, that the arrangement between the partners of the firm amounted to a distribution of the assets of the firm on dissolution and that there was no sale, exchange or transfer of the respondent's share in the capital assets to D. The sum of Rs. 65,000, it was accordingly held, could not be taxed as capital gains. The receipt of money by the respondent was, in the opinion of

the Court, nothing but a receipt of his share in the distributed assets of the company.

9. Reliance in that case was placed, as has been done also in the present case, on behalf of the revenue upon the case of James Anderson v. Commissioner of Income Tax. ((1960) 39 ITR 123 : (1960) 3 SCR 167 : AIR 1960 SC 751 : 1960 SCJ 665). The said case was distinguished and was found to be of not much avail to the revenue. In that case the assessee who held a power of attorney from the executor of a deceased person, sold certain shares and securities belonging to the deceased for the purpose of distributing the assets amongst the legatees. The excess realised by sale was treated by the department as capital gains. The contention of the assessee was that since the sale of the shares and securities fell within the purview of the third proviso to Section 12(d)(1), it could not be treated as a sale of capital assets but this contention was rejected by this Court. James Anderson's case (supra), in our opinion, is not of much assistance to the revenue as in that case there was no distribution of capital assets between the legatees. On the contrary, the assessee has had in pursuance of the authority given to him by the executor of the deceased sold the shares and securities and the said sale had resulted in capital gain. In the present case there has been no sale or receipt of price but only a distribution of the assets of the companies which had gone into voluntary liquidation. Such a transaction does not amount to sale, exchange, relinquishment or transfer of the assets. The revenue, in the circumstances, cannot derive much assistance from that case.

10. In the case of Commissioner of Income Tax v. Dewas Cine Corporation, ((1968) 68 ITR 240 : (1968) 2 SCR 173 : AIR 1968 SC 676 : (1968) 1 SCJ 691) this Court while dealing with Section 10(2)(vii) of the Act, observed that the expression "sale" in its ordinary meaning is a transfer of property for a price, and adjustment of the rights of the partners in a dissolved firm by allotment of its assets is not a transfer nor it is for a price. In that case the assets were distributed among the partners and it was contended that the assets must in law be deemed to be sold to the individual partners in consideration of their respective shares, and the difference between the written-down value and the price realised should be included in the total income of the partnership under the second proviso to Section 10(2)(vii). This Court in this context observed that a partner may in an action for dissolution insist that the assets of the partnership be realised by sale of its assets, but property allotted to a partner in satisfaction of his claim to his share, could not be deemed in law to be sold to him.

11. In Commissioner of Income Tax v. Associated Industrial Development Co. Pvt. Ltd. ((1969) 73 ITR 50), a division Bench of the Calcutta High Court held that the amount received by a shareholder on the liquidation of a company was not assessable to capital gains as there was no sale, exchange, relinquishment transfer of the capital assets. Similar view has also been taken by the Gujarat High Court in Commissioner of Income Tax v. R. M. Amin. ((1971) 82 ITR 194).

12. We are, therefore, of the view that distribution of the assets of the companies in liquidation does not amount to a transaction of sale, exchange, relinquishment or transfer so as to attract Section 12-B of the Act.

13. Mr. Manchanda on behalf of the appellant has invited our attention to the third proviso to sub-section (1) of Section 12-B as originally enacted by the Income Tax and Excess Profits Tax (Amendment) Act wherein it was stated, inter alia, that any distribution of capital assets on the dissolution of a firm or other association of persons or on the liquidation of a company shall not for the purpose of Section 12-B be treated as sale, exchange or transfer of capital assets. It is urged that the omission of such distribution of capital assets in the first proviso to sub-section (1) of Section 12-B, as revived by the Finance (No. 3) Act of 1956, would show that the Legislature wanted the

distribution of capital assets on dissolution of a firm or other association of persons or the liquidation of a company to be treated as sale, exchange or transfer. This contention, in our opinion, is not well-founded. It appears to us that the cases of the distribution of capital assets on dissolution of a firm or other association of persons or liquidation of a company were mentioned in the third proviso under the earlier Act, as a matter of a clarification to allay fears even though the language of sub-section (1) of Section 12-B was not intended to apply to such cases. Provisos, as mentioned on page 221 of Craies on Statute Laws, Sixth Edition, are often inserted to allay fears. A proviso is inserted to guard against the particular case of which a particular persons is apprehensive, although the enactment was never intended to apply to his case or to any other similar case at all.

14. We have already stated earlier that the distribution of assets by a liquidator on the voluntary winding up of a company cannot constitute sale, transfer or exchange for the purpose of sub-section (1) of Section 12-B of the Act. If the language of sub-section (1) of Section 12-B of the Act is clear and does not warrant the inference that distribution of assets on liquidation of a company constitutes sale, transfer or exchange the said transaction of distribution of assets would not, in our opinion, change its character and acquire the attributes of sale, transfer or exchange because of the omission of a clarification in the first proviso to sub-section (1) of Section 12-B of the Act, even though such a clarification was there in the third proviso of the section inserted by the earlier Act (Act 22 of 1947). It is well settled that consideration stemming from legislative history must not be allowed to override the plain words of a statute (See Maxwell on the Interpretation of Statutes, Twelfth Edition, Page 65). A proviso cannot be construed as enlarging the scope of an enactment when it can be fairly and properly construed without attributing to it that effect. Further, if the language of the enacting part of the statute is plain and unambiguous and does not contain the provisions which are said to occur in it, one cannot derive these provisions by implication from a proviso (see page 217 of Craies on Statute Law, Sixth Edition).

15. In the light of what has been discussed above, the difference between the language of the first proviso to Section 12-B(1), as inserted by Finance (No. 3) Act of 1956 and the third proviso to Section 12-B(1), as inserted by Act 22 of 1947, cannot be of much material help to the revenue.

16. Reference has also been made by Mr. Manchanda to Section 46 of the Income Tax Act, 1961 which contains a provision for charging with capital gains the money or assets received by a shareholder on the liquidation of a company. The liability under that section arises from its express provisions. It cannot, however, be said that such a liability would also arise even in the absence of such provisions under the Act of 1922.

17. The appeal consequently fails and is dismissed with costs.

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