SUPREME COURT OF INDIA

Commissioner of Income Tax, Cochin

Vs.

Mrs. Grace Collis

C.A.No.4437-4445 of 1997

(Y.K.Sabharwal, S.N.Hegde and S.P.Bharucha JJ.)

23.02.2001

JUDGMENT

S.P.Bharucha, J

1. These are the appeals by the Revenue against the decision of a Division Bench of the High Court of Kerala on a reference application at the instance of the assessees under Section 256(1) of the *Income Tax Act, 1961*. The High Court was called upon to answer the following three questions : 1. Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that on the amalgamation of Ambassador Steamships Pvt. Ltd. with Collis Line Pvt. Ltd., there was a transfer by the assessee of their shares in Ambassador Steamships Pvt. Ltd. ?

2. In case the answer to question No. 1 above is in the affirmative, whether the Tribunal was right in holding that the transfer was made in consideration of the allotment for to the assessees of shares in Collis Line Pvt. Ltd.?

3. Whether on the facts and in the circumstances of the case, the Tribunal was right in holding that Section 49(2) of the I.T. Act, 1961 applied to the sale of the shares of the assessees in Collis Line Pvt. Ltd., which were obtained by the assessees on the amalgamation of Ambassador Steamship Pvt. Ltd. with Collis Line Pvt. Ltd.?

4. The High Court answered the first question in the negative and in favour of the assessees, namely, that there was no transfer. In view of this answer, it held that the second question did not arise. It answered the third question in the negative and in favour of the assessees. Even so, it held that the taxing authorities could consider taxing the assessees on the basis of the transaction whereunder the share of Rs.100/- was sold for Rs.107.50. The assessees were shareholders of Ambassador Steamship Pvt. Ltd.. The High Court of Kerala sanctioned a Scheme of Arrangement under Section 391(2) and 394 of the Companies Act whereby Ambassador Steamship Pvt. Ltd. (the amalgamating company) was amalgamated with Collis Line Pvt. Ltd.(the amalgamated company). The Scheme contemplated the transfer by way of amalgamation of all assets and liabilities of the amalgamating company to the amalgamated company in consideration of the amalgamated company issuing to the members of the

amalgamating company 14 equity shares of Rs.100/- each, credited as fully paid up, in the amalgamated company for each share held in the amalgamating company. Upon amalgamation, the amalgamating company would cease to function and the amalgamated company would take over all its business, assets and liabilities and carry on its business. The sanctioned Scheme stated: As the residue of the consideration for the said transfer, the Transferee Company shall issue to the members of the Transferor Company 14 equity shares of Rs.100/- each in the Transferee Company credited as fully paid up in respect of each share held by him or her in the Transferor Company

5. The assessees sold the 45318 shares of the amalgamated company of the face value of Rs.100/- each which they had acquired under the Scheme to one B.K. Chatterji and his associates on 29th February, 1976 for the aggregate sum of Rs.48,72,523/-. This meant that they had sold each share for Rs.107.50.

6. For the Assessment Year 1976-77, the previous year whereof ended on 31st March, 1976, the Income Tax Officer levied capital gains tax upon the assessees in respect of the sale to Chatterji and others. The Income Tax Officer applied the provisions of Section 49(2) read with Section 47(vii) for the purposes of computing the capital gain. Thereunder the cost of the shares of the amalgamating company is the cost of the shares of the amalgamated company that the assessee surrendered in exchange under a scheme of arrangement. The assessees had not furnished to the Income Tax Officer information as to the cost at which they had acquired the shares of the amalgamating company. Accordingly, the Income Tax Officer noted that under the Scheme the assessees had received 14 shares of the face value of Rs.100/- each in the amalgamated company for one share of the face value of Rs.100/- in the amalgamating company. He multiplied the number of shares of the amalgamated company that the assessees had sold by their face value of Rs.100/- and divided the result by 14 to arrive at their cost. The price at which the assessees had sold the shares less their cost as aforesaid was the capital gain that the Income Tax Officer subjected to tax. The Income Tax Officer rejected the contention of the assessees that Sections 49(2) and 47(vii) were not attracted as the assessees had not become the owners of the shares of the amalgamated company in consideration of the transfer of their shares in the amalgamating company.

7. The order of the Income Tax Officer was confirmed by the C.I.T.(Appeals). The matter went up before the Tribunal and the Tribunal upheld the appellate order. From out of the order of the Tribunal, the questions aforestated were referred to the High Court and answered as set out above.

8. For the purposes of appreciating the controversy in this appeal, it is necessary to set out the relevant provisions of the Act as they obtained at the relevant time.

9. Section 2(47) defines transfer, in relation to a capital asset, to include the sale, exchange or relinquishment of the asset or the extinguishment of any rights therein or the compulsory acquisition thereof under any law. Section 45 states that any profits or gains arising from the transfer of a capital asset effected in the previous year shall 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 states which transactions are not to be regarded as transfers. Nothing contained in Section 45 applies, by reason thereof, to: (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, and
>
> (b) the amalgamated company is an Indian company."

10. Section 49 sets out how cost is to be computed with reference to various modes of acquisition. It says, in sub-section(2): Where the capital asset being a share or shares in an amalgamated company which is an Indian company became the property of the assessee in consideration of a transfer referred to in clause (vii) of Section 47, the cost of acquisition of the asset shall be deemed to be the cost of acquisition to him of the share or shares in the amalgamating company.

11. In *Commissioner of Income-tax, Bombay v. Rasiklal Maneklal (HUF)*[1], this Court was concerned with a case of acquisition of shares consequent upon a scheme of amalgamation virtually identical to the Scheme before us. At that time capital gains were chargeable to tax by reason of Section 12B of the Income Tax Act, 1922, which stated thus : 12B. Capital gains.- (1) The tax shall be payable by an assessee under the head Capital gains in respect of any profit 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 in which the sale, exchange, relinquishment or transfer took place.

12. The question this Court was called upon to consider read thus: Whether, on the facts and in the circumstances of the case, the sum of Rs.49,350 could be assessed in the hands of the assessee as capital gains as having accrued to the assessee by exchange or relinquishment as provided for under section 12B of the Act ? This Court held that no exchange was involved in the transaction. An exchange involved the transfer of property by one person to another and, reciprocally, the transfer of property by that other to the first person. There had to be a mutual transfer of ownership of one thing for the ownership of another. In the case before the Court the assessee could not be said to have transferrd any property to anyone. When he was allotted shares of the amalgamated company, he was entitled to such allotment because of his holding 90 shares of the amalgamating company. The holding of 90 shares in the amalgamating company was merely a qualifying condition entitling the assessee to the allotment of 45 shares in the amalgamated company. The dissolution of the amalgamating company deprived the holding of the 90 shares of that company of all value.

13. Learned counsel for the assessees submitted that no capital gains tax could be levied upon the assessees in respect of the sale by them of their shares in the amalgamated company because there was no provision in the Act with regard to the manner of determination of the cost of these shares. This was for the reason that Section 49(2) prescribed the mode of

determining the cost where the shares in an amalgamated company had become the property of the assessee in consideration of a transfer, as referred to in Section 47(vii); that is to say, a transfer by a shareholder in a scheme of amalgamation of shares held by him in the amalgamating company if the transfer was made in consideration of the allotment to him of shares in the amalgamated company. The decision in Rasiklal had held that there was no transfer of any property to any one by the assessee in circumstances identical to those before us.

14. This, however, is not the end of the matter for Section 2(47) defines transfer to include the extinguishment of any rights in a capital asset.

15. In this regard, our attention was drawn by learned counsel for the assessees to the decision of a Bench of two learned Judges of this Court in *Vania Silk Mills Pvt. Ltd. v. C.I.T.*[2]. This was a case in which the appellant company carried on the business of manufacture and sale of art-silk cloth. It purchased during the year 1957 machinery and gave it on hire to Jasmine Mills at an annual rent. Jasmine Mills, as bailee of the machinery, insured it against fire along with its own machinery. The insurance policy contained a reinstatement clause requiring the insurer to pay the cost of the machinery as on the date of the fire in case of destruction or loss. A fire did break out in the premises of Jasmine Mills causing extensive damage, inter alia, to the machinery which became useless as a result. On settlement of the insurance claim, Jasmine Mills received an amount from the insurance company. From out of it it paid Rs. 6,32,533 to the appellant on the account of the destruction of the machinery. The Income-tax Officer brought to tax the sum of Rs. 3,50,792, being the difference between the insurance amount received by the appellant for the machinery and the original cost thereof, as a capital gain. The Appellate Tribunal held that the insurance amount was not received by the appellant on the transfer of a capital asset but on account of the damage to its machinery and that Section 45 of the Act was not attracted. On a reference, the High Court reversed the decision of the Tribunal. This Court held in appeal therefrom that when an asset was destroyed, there was no question of transferring it to others. The destruction or loss brought about the destruction of the right of the owner of the asset in it, but it was not on account of a transfer but on account of the disappearance of the asset. The extinguishment of the right in an asset on account of the extinguishment of the asset was not a transfer of the right but its destruction. The destruction of the right on account of the destruction of the asset could not be equated with the extinguishment of the right on accounts of its transfer. Section 45 of the Act was, therefore, not attracted. The fact that while paying for the total loss or damage to the property the insurance company took over such property or whatever was left of it did not change the nature of the insurance claim, which was an indemnity or compensation for the loss. The payment of the insurance claim was not in consideration of the property taken over by the insurance company, for one was not consideration for the other. This Court then, having so very rightly held that Section 45 was not attracted, went on to consider the definition of transfer and it said: It is true that the definition of transfer in section 2(47) of the Act is an inclusive definition and therefore, extends to events and transactions which may not otherwise be transfer according to its ordinary, popular and natural sense. It is this aspect of the definition which has weighed with the High Court and, therefore, the High Court has argued that, if the words extinguishment of

any rights therein are substituted for the word transfer in section 45, the claim or compensation received from the insurance company would attract the said section. The High Court has, however, missed the fact that the definition also mentions such transactions as sale, exchange, etc., to which the word transfer would properly apply in its popular and natural import. Since those associated words and expressions imply the existence of the asset and of the transferee, according to the rule of noscitur a sociis, the expression extinguishment of any right therein would take colour from the said associated words and expressions and will have to be restricted to the sense analogous to them. If the Legislature intended to extend the definition to any extinguishment of right, it would not have included the obvious instances of transfer, viz., sale, exchange, etc. Hence, the expression extinguishment of any rights therein will have to be confined to the extinguishment of rights on account of transfer and cannot be extended to mean any extinguishment of right independent of or otherwise than on account of transfer.

16. Learned counsel for the assessees relied upon this decision to contend, again, that there had been no transfer by the assessees of their shares in the amalgamating company and that, therefore, the case would still not fall within the meaning of the expression extinguishment of any rights therein in Section 2(47). By reason of the decision, the expression extinguishment of any rights therein had to be confined to the extinguishment of rights on account of a transfer and could not be extended to refer to the extinguishment of rights independent of or otherwise than on account of transfer.

17. Learned counsel for the Revenue submitted that having held that the payment in settlement of the insurance claim was not in consideration of the transfer to the insurer of the damaged machinery and that, therefore, there was no transfer within the meaning of Section 45, it was unnecessary for this Court in Vanias case to go on to consider the definition in Section 2(47) and the meaning to be attached to the expression extinguishment of any rights therein. In his submission, the decision in Vanias case was to this extent obiter dicta. The definition in Section 2(47) of transfer included sale and exchange. In each of those cases there was an extinguishment of the right of the seller or exchanger in the capital asset. To restrict the extinguishment of rights to extinguishment on account of transfer was, in learned counsels submission, to render the expression extinguishment of any rights therein otiose and to nullify the effect of their use in the definition.

18. We have given careful thought to the definition of transfer in Section 2(47) and to the decision of this Court in Vanias case. In our view, the definition clearly contemplates the extinguishment of rights in a capital asset distinct and independent of such extinguishment consequent upon the transfer thereof. We do not approve, respectfully, of the limitation of the expression extinguishment of any rights therein to such extinguishment on account of transfers or to the view that the expression extinguishment of any rights therein cannot be extended to mean the extinguishment of rights independent of or otherwise than on account of transfer. To so read the expression is to render it ineffective and its use meaningless. As we read it, therefore, the expression does include the extinguishment of rights in a capital asset independent of and otherwise than on account of transfer.

19. This being so, the rights of the assessees in the capital asset, being their shares in the amalgamating company, stood extinguished upon the amalgamation of the amalgamating company with the amalgamated company. There was, therefore, a transfer of the shares in the amalgamating company within the meaning of Section 2(47). It was, therefore, a transaction to which Section 47(vii) applied and, consequently, the cost to the assessees of the acquisition of the shares of the amalgamated company had to be determined in accordance with the provision of Section 49(2), that is to say, the cost was deemed to be the cost of the acquisition by the assessees of their shares in the amalgamating company.

20. Upon this reading of the law, our answers to the questions are: (1) In the affirmative and in favour of the assessee. (2) Does not arise. (3) In the affirmative and in favour of the Revenue.

21. We have already set out how the Income Tax Officer computed the capital gain and see no reason to take another view, having regard to the fact that the assessees could have disclosed, without prejudice to their contentions, the cost at which they had acquired their shares in the amalgamated company. We are at a loss to understand the reasoning of the High Court in giving to the Revenue the liberty to consider taxing the assessees on the basis that it was a transaction by itself whereunder a share of Rs.100.00 each was sold as a share of Rs.107.50. We are obliged to learned counsel for their assistance. The appeals are allowed. The judgment and order under appeal is set aside. The questions are answered as already indicated. There shall be no order as to costs.

[1]*177 I.T.R. 198*
[2]*191 I.T.R. 647*