ANDHRA PRADESH HIGH COURT

Mir Imdad Ali Khan

Vs.

Commissioner of Wealth Tax

Case Referred No. 30 of 1961

(Jaganmohan Reddy and Anantanarayana Ayyar, JJ.)

15.11.1962

JUDGMENT

Jaganmohan Reddy, J.

1. The Income-tax Appellate Tribunal has referred the following two questions under Section 27 of the Wealth Tax Act 1957 (No. 27 of 1957) namely, (1) whether the value of the shares owned by the assessee in the limited company was property includible in his wealth as on the valuation dates under Section 4(1) of the Act? (2) whether the compensation sanctioned by the Government on the abolition of the assessee's Jagir, though not paid but due to the assessee as on the valuation dates, was property includible in the net wealth of the assessee under Section 4(1) of Act? These questions arose out of the wealth tax assessment of the assessee for the year 1957-58 for which the valuation date was 30-9-1956 and for the assessment year 1958-59 for which the valuation date was 30-9-1957. It appears from the statement of the case that the assessee owns house properties and shares in limited companies and is entitled to commutation amounts under the Hyderabad (Abolition of Jagirs) Regulation 1358F (No. LXIX of 1358F.) and the Hyderabad Jagirs (Commutation) Regulation 1359F (No. XXV of 1359F.). in respect of the inclusion of the shares of the limited companies and the commutation amount in the assessment for wealth tax for the two relevant years, the contention of the assessee was that since the shares of the company held by him represent the wealth of the limited company, the limited company was liable to pay tax on the same and the wealth as represented by the shares could not once again be included in his net wealth. This contention was negatived throughout by the income-tax officer, the Appellate Assistant Commissioner and the Tribunal, the last of which holding that the wealth of the limited companies was not coterminous with, or the same as, the wealth of a share-holder as represented by the value of the shares and that as there was no denial that the assessee was the owner of the shares it was properly included in his net wealth. At the time of hearing of the appeal, the assessee also sought permission of the tribunal to raise two additional grounds of appeal, one of which concerned the abatement of tax in respect of shares in assessee's net wealth as provided by rule 2 of the schedule to the Wealth Tax Act. But the tribunal refused to allow him to raise this contention as it was not raised before the Appellate Assistant Commissioner and as such it did not arise out of his orders. In our view, since the question, as framed, relates to the inclusion or non-inclusion of the value of the shares owned by the assesses in the limited

companies in the net wealth of the assessee, dependant on whether the principle of double taxation is applicable or not, it will be permissible in determining this question to refer to the relevant provisions including rule 2 of the Schedule as indicating to what extent the legislature has recognized the principle of double taxation or its avoidance. In the circumstances we would be justified in amending the question to bring about that sense. Accordingly question 1 is amended by the addition of the words "and subject to what provisions, if any" at the end of the question.

2. The taxing Section 3 enjoins that a 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 shall be charged for every financial year commencing on and from the first day of April, 1957. Section 4 sets out what shall be included in computing the net wealth of an individual and in that definition the value of assets which on the valuation date are held by his wife by a minor child or by a person or association of persons to whom such assets have been transferred by the individual otherwise than for adequate consideration for the benefit of the individual or his wife or minor child, or by a person or association of persons to whom such assets have been transferred by the individual otherwise than under an irrevocable transfer and the value of his interest in the firm or association or other assets specified therein are to be included. Section 5 enumerates the assets that are exempted from inclusion in the net wealth of the assessee so that all assets which belong to the assessee or the persons enumerated in Section 4, and which are not exempt under Section 5 would constitute the net wealth of the assessee. An asset has been defined in Section 2(e) as including property of every description, movable or immovable, but does not include agricultural land and growing corps etc. or any building owned or occupied by a cultivator or receiver of rent or revenue out of agricultural land; or animals or a right to any annuity in any case where the terms and conditions relating thereto preclude the commutation of any portion thereof into a lump sum grant; or any interest in property where the interest is available to an assessee for a period not exceeding six years. "Net wealth" has been defined under Section 2(m) as meaning the amount by which the aggregate value computed in accordance with the provisions of the 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 the Act is, in excess of the aggregate value of all the debts owed by the assessee on the valuation date other than debts which under Section 6 are not to be taken into account and debts which are secured on, or which have been incurred in relation to, any asset in respect of which Wealth Tax is not payable under the Act and the amount of the tax, penalty or interest payable in consequence of any order passed under or in pursuance of the Act or any law relating to taxation of income or profits or the Estate Duty Act, the Expenditure Tax Act or the Gift Act etc., which is outstanding on the valuation date and is claimed by the assessee in appeal, revision or other proceeding as not being payable by him or which, although not claimed by the assessee as not being payable by him, is nevertheless outstanding for a period of more than twelve months on the valuation date. Reading these several provisions together, it is undeniable that shares in a limited company held by an assessee are assets owned by him and not by the company. The very notion of a share is that the individual owns or has a right in the asset of the company to the extent of the value of the share and in the event of liquidation he is entitled to the distribution of its assets which are available for distribution in accordance with the share or shares held by him. To put it differently and more comprehensively a share is a right to receive the proportion of the proms of the company and its assets on a winding up and an other benefits of membership together with an obligation to contribute to its liabilities, all of which are subject to and controlled

by the memorandum and articles of association of the company. On this basis, the wealth of the company is owned by the share-holders in accordance with their respective shares. On this principle it would appear that where the net wealth of the company is taxed in the hands of the company and that wealth is again taken into account in imposing a tax in the hands of the individuals who own shares in that company, there would be a case of double taxation. But, the Legislature was aware of the effect of this in so far as the shares held by assessees in limited companies are concerned and thus provided for the relief in rule 2 of the schedule subject to certain limitation to avoid this effect in respect of double taxation on shares once in the hands of the share-holders and a second time in the hands of the company inasmuch as the subscription of the members to the shares are reflected in the assets of the company. This relief in effect helps only where the tax attributable to shares exceeds 1-1/2% of their market value. In our view, therefore, the applicability of rule 2 of the schedule in considering whether the value of the shares is to be included in the net wealth of the assessee is germane to the determination of the question No. 1 as amended by us and consequently we must hold that the shares owned by the assessee in the limited companies are properly includible in its net wealth subject to the relief if applicable to him under rule 2 of the schedule to the Wealth-tax Act.

3. The answer to the second question would depend upon the nature of the commutation and the extent of the interest which the assessee has in that commutation amount under the Jagirs Abolition Regulation and the Jagirs Commutation Regulation. It has to be noticed that under the definition of "assets" and "net wealth" every kind of property i.e., moveable or immovable the valuation of which is computable under the provisions of the Act wherever situated and on the valuation date which is in excess of the aggregate value of all the assets other than those specified in Section 2(m) would constitute the net wealth which is assessable under Section 3. The question is whether commutation amounts are "assets" within the meaning of Section 2(e) of the Act; if so, whether the total commutation amount payable to the assessee should be taken into account or only those instalments of the commutation amounts which are periodically paid under the provisions of the Jagir Abolition Regulation and the Jagirs Commutation Regulation. Learned Advocate for the petitioner seeks firstly to obtain total exemption under Clause 18 of sub-section (2) of Section 5 and secondly, to include in the net wealth only that amount which is paid by or on the date of valuation. It is apparent from a reference to Section 3 of the Jagirs Commutation Regulation that the commutation sum for every jagir is calculated on the basis of multiplication of a basic annual revenue which is calculated in accordance with Section 4. In brief what sections 3 and 4 provide is that the gross basic sum is to be computed on the average annual gross revenue of the jagir for the ten years opening with the year 1347 F. and ending with the year 1356F. Thereafter in the case of a Jamiat Jagir the gross basic sum shall be reduced by 20 per cent and the sum resulting from this reduction shall be the net basic sum; (from this reduction shall be the net basic sum); from the gross basic sum, in the case of a jagir other than a Jamiat jagir 60 per cent shall be dedudcted and in the case of a Jamiat jagir the deduction of 60 per cent shall be from the net basic sum, the sum resulting from this deduction in either case was termed the basic annual revenue. Once the basic annual revenue is computed, Section 3 enjoins that the commutation sum for every jagir shall be the sum resulting from the multiplication of the basic annual revenue of the jagir calculated in accordance with Section 4 by the figure specified in the appropriate entry in the second column of the table given therein subject however to the provisions that where the amount thus arrived at is less than the alternative sum given in column 3, the alternative sum applicable will be the commutation amount. This elaborate provision of working out commutation would indicate that the annual income or revenue of the Jagir was

being capitalized for a period of years which in any case is not less than ten years, depending on the basic annual revenue.

4. It may also be stated that under the Jagirs Abolition Regulation also, elaborate provision had been made as to the manner in which the gross revenue and net income and the balance had to be calculated - vide Section 7 and after payment of the balance under Section 10 now the amount of net income should be distributed under Section 11 and the deductions permissible under Section 12 from that amount. Section 14 states that the amounts payable to Jagirdars and Hissedars under the Jagirs Abolition Regulation shall be deemed to be interim maintenance allowances payaable until such time as the terms for the commutation of jagirs are determined, so that the amount which is paid as interim maintenance was treated as income of the jagirdar till such date as the commutation amount was fixed. That this is so is clear from Section 7(2) of the Jagirs Commutation Regulation which is in the following terms :-

> "The payment to a Jagirdar or Hissedar of his appropriate share in the commutation sum of the Jagir shall constitute the final commutation as from the 1st April, 1950, of his rights in the Jagir and if any payment by way of an interim maintenance allowance under the said Regulation is made in respect of a period the whole or part of which is subsequent to the said date, the amount of such payment or, as the case may be, the appropriate proportion of such amount shall be recovered from the recipient thereof by deduction from the first payment made to him on account of his share in the commutation sum for the Jagir."

Sub-section (1) of Section 7 states that the appropriate share of the commutation sum shall be payable to every person entitled to participate in the distribution thereof in such form and manner and at such time or times and in such number of installments as may be prescribed : provided that if at the time prescribed for the payment of any such share or installment the person entitled to receive payment of the sum is in dispute, the amount of the share of installment shall be deposited with the prescribed authority in the prescribed manner and subject to the prescribed conditions. The provisions of Section 7 of the Jagirs commutation Regulation therefore, clearly envisage the distribution of the commutation amount in accordance with the rules which may be prescribed under the Regulation. In other words, it does not preclude the total commutation being paid at once or in installments. But, from these provisions it is clear that if any sums are paid towards interim maintenance allowances in respect of a period, the whole of part of which is subsequent to the 1st April 1950, the date from which the commutation amount is due, that amount is deductible from the commutation amount. The commutation amount represents the net value of compensation payable to the holder of the Jagirdar in liquidation of his rights in the Jagir by capitalizing the amount based on the basic annual revenue of the jagir. There is little doubt that the commutation amount payable to the assesses is his asset within the meaning of Section 2(e) of the Wealth Tax Act.

5. But it is contended however by reference to Section 2(e) (iv) that is a right to an "annuity". This contention, in our view, is not well founded. Under clause (iv) of Section 2(e) a right to any annuity in any case where the terms and conditions relating thereto preclude the commutation of any portion thereof into a lump sum grant was excluded from the "assets" for the reason that such

an annuity is not a capital asset but income chargeable under the Income-tax Act. The distinction between an annuity properly so-called and payment by annual installment or an annual payment has always given rise to controversies. The famous dictum of Baron Watson in *Foley v. Fletcher*[1], to which reference is invariably in dealing with this aspect of the matter may be usefully noticed :

> "An annuity means where an income is purchased with a sum of money, and the capital has gone and has ceased to exist, the principal having been converted into an annuity."

The fine distinction between the two ideas namely; an annuity properly so called and an annual capital payment is always difficult and has been such as to elude any definition by which one or the other could be determined with any certainty. The true nature and character of each transaction has to be looked into. A simple way of putting it, though we hesitate to simplify a matter which is beset with difficulty, is that if it is the purchase of an income the annual payment is exigible to income-tax, but if it is a payment of a capital by annual installment or in other words if the annual sum receivable represents a payment or return of the capital, the amount thus paid would form part of the capital asset. Romer, L. J. in *Inland Revenue Commrs. v. Wesleyan and General Assurance Society*[2], has given this lucid example to illustrate the principle involved :

> "a man having some property may either sell it in consideration of a payment by the purchaser to him of an annuity of Rs. 500 for the next twenty years, or he can sell his property to the purchaser for 10,000, the 10,000 to be paid by equal installments of 500 over the next twenty years. If he adopts the former of the two methods, then the sum of 500 received by him each year is exigible to income-tax.....If he adopts the second method, then the sums of 500 received by him each year are. . . . .not liable to income-tax; The vendor has the power of choosing which of the two methods he will adopt. The question which method has been adopted, must be a question of the proper construction to be placed upon the documents by which the transaction is carried out." Keeping these principles in mind and the nature of the commutation amount to which

[1](1858) 3 H and N 769 at p. 785, 117 R.R. 967

[2](1948) 1 All England Reporter 555 (sic)

> we have referred, we have no difficulty in coming to the conclusion that the commutation amount payable to the Jagirdar under the Jagirs Abolition Regulation and the jagirs commutation Regulation is a capitalized amount of the value of the jagir taken over by the Government and the capital amount under Section 7(1) of the Commutation Regulation, is distributable monthly, quarterly or annually, as the case may be. We asked Mr. jalil Ahmed as to what difference there is in the case before us i.e the distribution of the commutation amount annually or quarterly and the case of the payment by a debtor, to whom a sum of money has been lent and who undertakes to pay the amount in installments. He frankly admitted that if the commutation amount is to be equated in that way there is no difference.

6. Shri Jalil Ahmed has put forward another contention that, having regard to the nature of the jagir and its grant which was made for gallantry or for merit, the commutation amount must be deemed to have been impressed with that character and since the Central Government have approved of it, it is exempt under Section 5(1) (xviii) of the Wealth-tax Act. Section 5(1) (xviii) is in the following words :-

> "5(1) Wealth-tax shall not be payable by an assessee in respect of the following assets, and such assets shall not be included in the net wealth of the assessee.....(xviii) the property received by an assessee from Government in pursuance of any gallantry or merit award instituted or approved by the Central Government;"

7. This exemption, in our view, has no application to the commutation amount, firstly, because the amount or commutation is not received by an assessee from the Government in pursuance of any gallantry or merit award which is either instituted or approved by the Central Government. The commutation amount is not granted for either gallantry or merit nor is it an award instituted or approved by the Central Government. As we have pointed out, commutation amount is the value of the jagir which is being taken over by the Government in much the same way as compensation payable to a person whose asset is taken over. If it was a voluntary surrender on terms to be determined between the parties, the commutation amount would represent the amount of consideration fixed for the surrender of that asset and if it was a compulsory acquisition, the value fixed in accordance with the law authorizing such acquisition; secondly, the exemption has been obviously granted to stimulate encouragement to armed and police forces and is not even remotely referable to commutations of jagirs whatever the reasons for their grant may have been.

8. Before concluding we may at this stage cite a decision of the Bench of this Court in *Raja Rameswar Rao v. Commissioner of Income Tax*[3], which, though under the Income-tax Act, would lend support to our conclusion. That was a case where certain interim payments made on four different occasions namely, 25-1-1950, 10-4-50, 3-7-50 and 3-8-50 amounting to an aggregate of Rs. 1,47,857-4-0 was sought to be made exigible to income-tax and was resisted. After reaching the stage of the tribunal, the tribunal held that only those amounts paid as interim allowances as such would be

[3] AIR 1960 And Pra 42

exigible to income-tax while those that are referable to the commutation paid after 1-4-50 were held to be a capital receipt and in that view the tribunal had asked the Income-tax Officer to find out as to what period the four payments related to. Two questions were referred namely, (1) whether the interim maintenance allowances received by the assessee under the Hyderabad (Abolition of Jagirs) Regulation 1358 Fasli are income and, therefore, liable to tax? and (2) whether the receipt of maintenance allowances is exempt under Section 4(3) (vii) of the Indian Income-tax Act? On the first question, the Bench held that the interim maintenance allowances received by the assessee, which do not form part of the commutation amount, are income and liable to tax and (2) that the aforesaid interim allowances are not exempt under Section 4(3) (vii) of the Indian Income-tax Act and (3) that payments subsequent to 1-4-50 towards the commutation amount and in partial discharge therefore would not be liable to taxation for the obvious reason that if any of such payments had been made towards commutation payable to the petitioner and since it is to go in partial discharge of the commutation amount, it would be a

capital receipt and as such not liable to be taxed.

9. In the result, our answer to Question No. 1 is the value of the shares owned by the assessee in the limited companies will be properly includible in his net wealth subject to the application of rule 2 of the schedule to the Wealth-tax Act and our answer to the second question is in the affirmative. Let the reference be answered accordingly with costs. Advocate's fee Rs. 100/-.
Answered accordingly.