

DELHI HIGH COURT

Income-Tax Officer

Vs.

Official Liquidator, National Conduits (Delhi)

Company Appeal No. 7 of 1974.

(Rajinder Sachar And O.N. Vohra, JJ.)

1.10.1980

JUDGMENT

Rajinder Sachar, J.

1. Can the provisions of Section 222 of the I.T. Act, 1961, for recovery of the tax be resorted to by the ITO without seeking leave of the company judge under Section 446 of the Companies Act, 1956, in the case of a company after a winding-up order has been made is the question arising in this appeal against the judgment of the learned single judge, who has held that obtaining leave under Section 446(1) of the Companies Act was a condition precedent for seeking to recover tax by the ITO.

2. M/s. National Conduits P. Ltd. is a company registered under the Companies Act. In respect of its employee, one S. S. Arora, the company made deduction on account of income-tax from his salary, the total amount of which came to about Rs. 44,000 for the years 1961-62 to 1965-66. The company, however, did not deposit the said amount with the I.T. authorities. As a result on October 6, 1966, the ITO demanded from the company the payment of this amount, but to no effect. On January 16, 1969, an application was moved for winding up the company. An order of winding up was passed on May 7, 1969. On February 24, 1971, the ITO requested the official liquidator for payment of Rs. 44,000 due on account of deductions made from the salary of Arora. The official liquidator by his letter of March 1, 1971, asked the ITO to obtain leave of the High Court under Section 446 of the Companies Act, before any payment could be made by him. It was apparently this which made the ITO on July 25, 1972, to move an application under Section 446 of the Companies Act, seeking leave to take proceedings under the provisions of the I.T. Act for the recovery of the

aforesaid amount. It was at this stage that the issue was joined as to whether leave should be granted. The learned judge has refused to grant leave and hence the appeal by the ITO.

3. Section 446(1) of the Companies Act provides that when a winding-up order has been made and an official liquidator appointed no suit or other legal proceedings shall be commenced or shall be proceeded with except by leave of the court and subject to such terms as the court may enforce. Section 530(1) provides that in a winding up there shall be paid in priority to all other debts certain mentioned claims like wages, taxes, etc. Before the learned single judge it was not disputed or at least it was not established that any of the amounts claimed by the ITO were covered under the preferential payments within any of the clauses of Section 530(1) of the Act. As a matter of fact the learned judge has specifically safeguarded the interest of the appellant by permitting it to move any time a separate application if it is able to show that any portion of a sum of Rs. 44,000 is entitled to priority under Section 530(1). As the debt was not found to be preferential payment, the order refusing leave is not open to objection because there is no reason why this debt should not take its place along with other debts due from the company, especially when the right of the appellant to move later on if the circumstances show that any part of the debt covered by Section 530(1)(a) has been protected by the learned single judge.

4. Mr. Verma, however, invokes Section 537, which though by Sub-section (1) provides that any attachment execution against a company which is being, wound up, without leave of court, will be void, yet by Sub-section (2) excepts the applicability in proceedings for recovery of any tax payable to Government. The argument is that notwithstanding Section 446 of the Companies Act there is an independent indefeasible power with the ITO to recover the arrears of tax, under Section 537(2) of the Act; we cannot agree. New Section 446(1) is specific that after a winding-up order has been made no legal proceedings can be commenced or proceeded with except by leave of the court. What was, however, urged was that as Section 537(2) excepts proceedings for the recovery of any tax or dues payable to the Government, it means that the proceedings for recovery of such dues are immune from the restriction of Section 446(1) of the Act. The argument is unacceptable. That Section 171 of the Companies Act, 1913, corresponding to Section 446 of the Companies Act, 1956, requires leave to be obtained from the court by the ITO for seeking to recover the tax as

arrears of land revenue by virtue of power under the I.T. Act, was decided as far back as over 30 years and is reported in Governor-General in *Council v. Shiromani Sugar Mills Ltd.*¹ wherein it was observed:

"Accordingly, we agree with the learned judges of the Allahabad High Court in holding that the words 'other legal proceeding' in Section 171 of the Indian Companies Act, 1913, comprise any proceeding by the revenue authorities under Section 46(2) of the Indian Income-tax Act and that accordingly before forwarding the requisite certificate under Section 46(2) to the Collector, which would put the machinery for the collection of the arrears of income-tax as arrears of land revenue into motion, the appellant should have applied in the liquidation under Section 171 of the Companies Act for leave of the winding-up court."

5. It may be noted that Section 46(2) of the Indian I.T. Act, 1922, corresponded to Section 222 of the present I.T. Act. The attempt to avoid the applicability of Section 446 of the Companies Act by the counsel for the revenue by importing Section 537(2) to his aid is of no avail in view of the Federal Court decision wherein, though reference was made to s, 232(1) and (2) of the Indian Companies Act, 1913 (corresponding to Section 537 of the Companies Act, 1956), it was nevertheless held that leave of the court has to be obtained. Reference in this connection may be made to *S. V. Kondaskar v. V.M. Deshpande, ITO*² which, while recognizing that the power under Section 148 of the I.T. Act, 1961, could be exercised without resort to Section 171 of the Indian Companies Act, 1913 (corresponding to Section 446 of the Companies Act, 1956), because the words "legal proceeding" in Section 446 did not cover the proceedings under Section 148, went on to observe :

"The fact that after the amount of tax payable by an assessed has been determined or quantified its realization from a company in liquidation is governed by the Act because the income-tax payable also being a debt has to rank *par passu* with other debts due from the company does not mean that the assessment proceedings for computing the amount of tax must be held to be such other legal proceedings as can only be started or continued with the leave of the liquidation court under Section 446 of the Act."

6. Thus, the Supreme Court has clearly held that notwithstanding the assessment the recovery of the tax can only be proceeded with after leave of the

court has been obtained. We are, therefore, in agreement with the view taken by the learned single judge that leave under Section 446 of the Companies Act was necessary and also with his further finding that in the absence of any claim for priority for this amount the ITO was not entitled to the grant of leave.

7. The learned judge has observed that there seemed to be an inconsistency between the provisions of Section 537 and Section 446 of the Companies Act, for, if the proceedings are stayed under Section 446(1) it will not be possible for proceedings for Realizing tax arrears to end in execution or sale to which Section 537(1) or (2) could apply. But the controversy had been resolved by the Federal Court by holding that Government was not entitled to preferential payment for tax arrears except as it is permitted by Section 530(1)(a) of the Companies Act. In our opinion, there is no inconsistency as they deal with different stages. Section 444(1) contemplates a situation where a winding-up order has been passed and then certain consequences will follow with regard to proceedings on the date of the winding-up order. The winding-up of a company by the court is deemed to commence at the time of the presentation of a petition for the winding-up (s. 441(2)). There is thus obviously a time gap between the commencement of the winding-up and the passing of the winding up order. Section 537 is covering a period in between this interval, because it clearly says that where any company is being wound up by court any attachment, distress or execution put in force, without leave of the court, after the commencement of the winding-up, or any sale held, without leave of court after such commencement shall be void. Section 537(1), therefore, only makes all such transactions void between the date of presentation of petition for the winding-up and the date of winding-up order. The reason why nothing more need to be said under Section 537(1) is that by virtue of Section 446 of the Companies Act the moment the winding-up order is passed no legal proceedings shall be commenced or if pending on the date of the winding-up order shall be proceeded with against the company except by leave of the court. That, however, left out the transactions earlier to the passing of the winding-up order. This is covered by Section 537(1) of the Companies Act. Thus, right from the date of presentation of a petition for winding up, the courts' protective arm is thrown on all transactions so that private individuals may not take undue advantage of the situation and thus leave only the husk of the company at the time when the order of winding-up comes to be passed. But no public interest is involved when taxes are being realized during this period and that is why Sub-

section (2) of Section 537 excepts the proceedings for the recovery of any tax by impost or any dues payable to the Government, from the provisions of Section 537(1). Thus, even if any proceedings have been started for the recovery of such tax even after the date of presentation of the petition for winding up they would not be deemed to be void automatically. It appears to us that Section 537(2) of the Companies Act has really no relevance to the question whether the ITO can resort to Section 222 without obtaining the leave of the court under Section 446(1) of the Act. Section 537(1) affects certain proceedings prior to the date of the winding-up order. Section 446, however, is a special provision dealing with a: company which is being wound up from the date of winding-up order. The power of recovery proceedings under Section 222 of I.T. Act are general provisions applicable to all companies whether being wound up or not, Section 446(1), however, deals with a company which is being wound up and is thus a special provision and will prevail over the general provision of recovery of tax under the I.T, Act. That I.T. Act is a general provision applicable to all assessed and cannot override the provisions of a special law like the Companies Act was recognized in *Union of India v. India Fisheries (P.) Ltd.*³ wherein it was held that the department cannot by exercising the right under Section 49E of the I.T. Act get priority over the other unsecured creditors as laid down under Sections 228 and 229 of the Indian Companies Act, 1913. Similar consequences must follow in the present case. To accept the argument of Mr. Verma would mean that though the I.T. Dept. is an unsecured creditor for the amount in dispute and would have to stand along with other unsecured creditors for the realization of this amount it could still exercise its powers under Section 222 of the I.T. Act. This would be contrary to the Companies Act. It must, therefore, be held that without obtaining leave under Section 446(1) of the Companies Act, the ITO cannot resort to Section 222 of the I.T. Act for recovery of tax due from the company. It must obey the mandate of the Companies Act and proceed within its requirements.

8. We may also note that Mr. Verma tried to invoke Section 178 of the I.T. Act. The first objection to permitting this contention being raised is that this point was never raised before the learned single judge who, therefore, had no occasion to deal with it. Not only that, even in the grounds of appeal no such ground has been raised on the basis of this provision. That apart, even on merits, in our view, the argument is also of no assistance to Mr. Verma. Section 178 empowers the ITO on receipt of information from the liquidator about his

having been appointed as a liquidator of a company to inform the liquidator of the tax liability and also to direct him to keep sufficient funds to provide for any tax which is likely to be payable by the company and the liquidator shall not, without leave of the Commissioner, part with any of the assets, equal to the amount notified. This provision in no way interferes with or abrogates the provision of priority of the debts laid down in Section 530(1)(a) of the Companies Act [See *Baroda Board & Paper Mills Ltd. v. Income Tax Officer* ⁴ where it was held that the non obstante clause of Section 178(1)(b) of the I.T. Act does not interfere, in any manner with the order of priorities laid down in Section 530(1)(a) of the Act.

9. A similar view has been taken by the Mysore High Court in *Income Tax Officer v. Official Liquidator, Mysore High Court* ⁵ We, however, also must notice that a contrary view has been taken by the Andhra Pradesh High Court and by the Kerala High Court (See *Income Tax Officer v. Official Liquidator* ⁶ and *Steel Sons Pvt. Ltd. v. Registrar of Companies* ⁷ (It may, however, be noted that when the Companies Act, 1956, was enacted, it was urged before the Company Law Committee that the power for review of the I.T. Act should not be limited to a particular period. This plea was rejected by the Committee. The conflicting views taken by the courts have an area of plausibility. We may, however, note that the high-powered expert committee appointed by the Govt. of India took note of this conflict and has recommended (in para. 15.30) that Section 530 of the Companies Act should be amended by way of clarification that notwithstanding anything contained in Section 178 of the I.T. Act, 1961, the priority for payment of taxes will be limited to taxes having become due and payable within 12 months next before the relevant date. Though, therefore, there may be a view that by the enactment of Section 178(6), the tax due, which is in the present case even prior to 12 months, can claim priority, it will still not help the appellants. The reason is as mentioned above that this point not having been raised before the single judge cannot be allowed to be raised in the appeal. That apart, even if this view was to be accepted that priority for tax of any period is to be given under Section 530 of the Companies Act, 1956, it does not take away the requirement of obtaining leave under Section 446 of the Act. No doubt, in granting or refusing leave, it may be one of the considerations, whether the debt has priority under Section 530 of the Companies Act but the main question which calls for decision in the present case, whether the tax can be recovered without obtaining leave under Section 446 of the Companies Act,

has not been answered by the Kerala and Andhra Pradesh High Courts. The requirement of obtaining leave under Section 446 of the Act still has to be decided in the light of the decision given in the Federal Court decision in Shiromani Sugar Mills' case [1946] 14 ITR 248 ; 16 Comp Case 71. Section 178 of the I.T. Act, 1961, is only a mode of keeping intact certain assets of the company to be able to adjust them for the purpose of the tax liability which the ITO may determine in future. The question of how to recover that tax will necessarily have to be decided by the special provisions of the Companies Act and, in the case of a company which is being wound up, the requirements of obtaining leave laid down in Section 446 of the Act would have to be observed. The question of any conflict between Section 446, and Section 530 of the Companies Act does not at all arise.

10. As a result, we find no merit in the appeal which is dismissed, but without costs.

Cases Referred.

1. [1946] 14 ITR 248, 258 ; 16 Comp Case 71, 80 (FC),
2. [1972] 83 ITR 685, 698 ; 42 Comp Case 168, 181 (SC),
- 3.(1965) 57 ITR 331 : 35 CC 669,
4. [1976] 102 ITR 153; 46 Comp Case 25 (Guj)],
- 5.[1967] 63 ITR 810; 37 Comp Case 114.
6. [1975] 101 ITR 470; [1976] 46 Comp Case 46
7. C.P. No. 14/1969).