

(1967) 12 CAL CK 0013
In the Calcutta High Court

Case No : Income Tax Reference No. 74 of 1964

Commissioner of Income Tax, W.B. II

APPELLANT

Vs

Chrestian Mining Co. Ltd.

RESPONDENT

Date of Decision : 21-12-1967

Acts Referred:

Income Tax Act, 1922 — Section 10(2)

Citation : AIR 1968 Cal 359

Hon'ble Judges : P.B. Mukharji, J;A.C. Sen, J

Bench : Division Bench

Advocate : B.L. Pal and Dipak Sen, for the Appellant;

Judgement

P.B. Mukharji, J.—This Income Tax Reference raises the following question for an answer:

"Whether on the facts and in the circumstances of the case the sum of Rs. 5 lacs was a capital receipt or a revenue receipt in the hands of the assessee?"

2. The facts are simple and short. The assessee was the lessee of mica mining rights over a certain area of Mahal Mahassi. It had also a lease of 16 annas surface rights in the said Mahal. There were two leases. One was in respect of the mining rights, the other was in respect of surface rights. They were both obtained on the 25th April, 1942. On 12th December, 1942, the mining rights in the said Mahal were requisitioned by the Government of India. Thereafter, on the 4th December 1943, the Government acquired 4722 acres thereof. The requisition in respect of the mining rights over area other than the said area of 4722 acres was withdrawn on the 30th October, 1945. 3 parties were interested in the claims for compensation for the acquisition. They were (1) Bhoticas, (2) the assessee and (3) Mr. E. C. Knuckey. The Bhoticas were the proprietors of the entire Mahal and were the owners of 8 annas share in the mining rights therein. Mr. Knuckey was the Muk-aridar of the 16 annas of the said property and was the owner of 8 annas in the mining rights in the said property. The assessee was the

lessee. The assessee was M/s. Christian Mining Company Ltd. now in liquidation and represented by the Official Liquidator.

3. During the pendency of the compensation proceedings Chrestian Mica Industries Ltd. acquired the shares of the Bhoticas and of Mr. Knuckey. An award was made by the arbitrator appointed for the purpose. There was an appeal to the High Court at Patna from the award of the arbitrators. This appeal was ultimately compromised. One term of the compromise was that mica mining lease was to be granted to the appellant namely the assessee and Chrestian Mica Industries Ltd. in respect of the acquired portion for a period of 20 years. On the 28th May, 1953, the assessee agreed to the grant of lease solely in favour of Chres-tian Mica Industries Ltd. and executed an agreement to that effect, for a consideration of Rs. 3,85,000 in addition to the sum receivable by the assessee as its share under the award of arbitrator and a further sum equivalent to 50 per cent of the net profits earned by the lessee Chrestian Mica Industries Ltd. from an area of mica mining operation to be carried on by them in the acquired portion. This was by way of royalty.

3A. The assessee company thereafter went into voluntary liquidation in the month of May, 1955. On the 29th June, 1955, the assessee company along with this liquidator assigned its right to receive the said royalty and also all other benefits available to it under the lease agreement dated the 28th May, 1953 to M/s. Associated Industries Limited for a consideration of Rs. 5 lakhs. The cheque for Rs. 5 lakhs being the consideration for the assignment was received by the liquidator. It is this sum of Rs. 5 lakhs which is in issue in this case. The question here is whether that was a capital receipt or a revenue receipt.

4. We can briefly now notice the different contentions in this respect. The contention before the Income Tax Officer on behalf of the assessee was that the company having gone into liquidation it could not do any business. Therefore, the receipt could not be a business receipt. The Income Tax Officer overruled that contention. He was influenced by the fact that this was not a case of liquidation by the Court but a case of voluntary liquidation. On the merits the Income Tax Officer came to the conclusion that the assessee was receiving the consideration in bits of lump sum from time to time and therefore the amount of Rs. 5 lakhs was the income from business liable to Income Tax.

5. The Income Tax Officer considered mainly the agreement dated the 29th June, 1955, between the assessee company, the Bharat Secretaries Ltd., the then liquidators and the Association Mining Industries Ltd., of 4, Lyons Range, Calcutta as well as the agreement dated 28th May, 1953, between the assessee company and Chrestian Mica Industries Ltd. of the same address, 4, Lyons Range, Calcutta. According to the Income Tax Officer the agreement dated the 28th May 1953, shows that the Chrestian Mica Industries Limited was liable to pay to the assessee company for consideration of 50 per cent of the net profits earned by the Chrestian Mica Industries Limited from any or all Mica Mining operation carried on by it in the specified area by way of royalty during the currency of

lease mentioned therein and in renewal thereof. He also finds that in the agreement of the 28th May, 1953, a sum of Rs. 3.85,000 was to be given as compensation to the assessee company apart from the benefit of the aforesaid 50 per cent of the net profits by way of royalty. Then by the agreement dated the 29th June, 1955, he finds that even this benefit of royalty was purported to be transferred for consideration of Rs. 5 lakhs. From the I. T. O.'s reading of the documents and the history of the case it appeared to him that this was a business transaction carried on in the normal course of making profits.

6. The assessee appealed to the Appellate Assistant Commissioner who reversed the judgment and order of the Income Tax Officer. He came to the conclusion that the amount received by the assessee was not for termination of any agency agreement but for the assignment of his rights under an agreement and was a capital receipt and not liable to be included in the taxable income of the assessee.

7. Thereafter the Department appealed to the Tribunal. The Tribunal confirmed the finding of the Appellate Assistant Commissioner. The Tribunal held that the assessee had sold away the right to receive the royalty at 50 per cent of the net profit from Chrestian Mica Industries Limited for the consideration of Rs. 5 lakhs and it was received by the assessee on account of such assignment of its rights. The Tribunal held that it was not a case of lump sum realisation of 50 per cent of the net profits available from the Chrestian Mica Industries Ltd. on a consideration for sale of right to receive the income. Therefore, the Tribunal came to the conclusion that it was a case of repayment of capital and not liable to tax. The reference before us is now on this point:

"Whether, on the facts and in the circumstances of the case the sum of Rupees 5,00,000 was a capital receipt or a revenue receipt in the hands of the assessee?"

8. Mr. Pal mainly relied on the decision of Nilkantha Narayan Singh Vs. Commr. of Income Tax, B and O, . That case in our opinion has no application to the facts before us. There the assessee executed three documents, each termed as Indenture of Lease in favour of a company conveying its right to collect royalties and rents from the three leases in lieu of an outright payment called selami of Rs. 1,00,000, Rupees 40,000 and Rs. 60,000 respectively and annual rent of Rs. 10, Rs. 5 and Rs. 5 respectively. The terms of the leases were 11, 10 and 15 years respectively. It was a special stipulation there that after the expiry of the period the right of the assessee would be revived in each case and he would be entitled to collect from the original lessees the amount of royalties and rents as before. Naturally in these circumstances the Income Tax authorities assessed the assessee Income Tax on a sum of 2 lakhs received from the company on the ground that it was assessable income and the sum of Rs. 84,000 representing the value of encashed high denomination notes on the ground that it represented the income from undisclosed sources. It was held by the Division Bench of the Patna High Court there that the sum of Rs. 2 lakhs paid by the company to the assessee was in the circumstances taxable income. Obviously there the whole of the leases was not dealt with or disposed of but a residue retained which was to

revert to the assessee. It was not a case of outright sale and therefore cannot be regarded as capital receipt under any circumstances.

9. The facts before us are entirely different.

10. In answering the question raised on this reference it is desirable to keep in view certain major principles well established in this connection. Some of these principles are stated in the Judgement of Lord Atkin In the Privy Council in Rhodesia Metals, Ltd. v. Commissioner of Taxes 1940 AC 774 where the question was almost the same as here. It was contended in that case that there was a sale of the whole undertaking by the Liquidator in the performance of his duties in winding up the company. It was a lump sale and therefore one particular ground could not be picked out of the Stems included in the lump sale treating the sale of the mining claim as the separate sale. In the ordinary way the sale by the liquidator of the whole undertaking of the company is a capital transaction unless there are special circumstances attached to the transaction. It was accepted by both sides there that in order that any receipt should be a taxable receipt it must be one arising in the course of carrying on a trade or business. The whole question therefore in that case was, as it is here, was the liquidator carrying on the company's business there in entering into this agreement. If he was not, then no part of the receipt could be the gross income. If he was then it might become income. Lord Atkin at p. 787 of the report said "prima facie, the sale by a liquidator of the whole undertaking of a company would result in a capital asset."

11. The general principle, therefore, was clearly laid down by the Privy Council in that decision. Applying that general principle to the particular facts of the case, the Privy Council came to the conclusion there that the company in that case received the sale price from a source within the territory, namely, the mining claims which had acquired and developed there for the particular purpose of obtaining the particular receipt. Therefore, the ratio of the decision was that as it was for the only purpose of obtaining the particular receipt it was a profit and accordingly assessable to Income Tax. But it cannot be said at all in the facts of the present case before us that this agreement was for obtaining the particular receipt for the purposes of profit.

12. The Liquidator of a Company normally realises the assets of the company after its liquidation. In doing so or in merely letting out the plant, machinery or other assets of the company when the normal business activities had come to a close, the liquidator cannot ordinarily be said to carry on business, apart from any special circumstances appearing in any particular case. The Liquidator may carry on the company's business in so far as it is necessary for the winding up or may realise the assets of the company in such a way as to involve the carrying on of trade. In this connection see for instance, the decisions in Narain Swadeshi Weaving Mills Vs. The Commissioner of Excess Profits Tax, and Baker v. Cook (1939) 7 ITR 284 :21 Tax Cas 337. It has been also held in case of a firm or other business concern that the trading activities may be continued even after

the dissolution in order to facilitate the winding up, as for instance, in *O. RM. OM. RM. PL. MUTHUKARUPPAN CHETTIAR and OTHERS Vs. COMMISSIONER OF Income Tax, MADRAS.*, and the decision of the House of Lords in *J & R O'Kane and Co. v. Inland Revenue Commissioner*, (1928) 12 Tax Cas 303.

13. For the purposes of illustrating further the point how a liquidator could or could not be said to carry on business after Liquidation, the decision in *Wilson Box v. Brice*, (1936) 20 Tax Cas 736 may be cited. There in July 1933 the appellant company acquired certain foreign patent rights. Subsequently the shareholders of the company agreed to sell all the shares to two individuals for Pounds 50,000, payable in instalments. The purchasers paid sums amounting to pounds 13,500, but then refused to complete. An action for specific performance was ultimately settled in November, 1934, on terms that (1) the agreement for the sale of shares was cancelled, (2) the appellant company was put into liquidation, and (3) the liquidator sold to the said purchasers part of the foreign patent rights for pounds 20,000, the amount of pounds 13,500, already paid being treated as part of the purchase price.

14. On appeal against an assessment for the year 1934-35 for the sum of pounds 20,000, made upon the appellant company in the name of the liquidator, it was contended (a) that the company did not carry on any trade of dealing in patent rights, and (b) alternatively, that the sum of pounds 6,500 only fell to be treated as a trading receipt of the company. The Special Commissioners held that the trade of the Company included dealing in patent rights and that the proceeds of the sale of the rights in question comprising both the sums of pounds 6,500 and pounds 13,500, were trading receipts received by the liquidator in the course of trading. The court held that there was no evidence upon which the Commissioners could find that the sale of the patent rights constituted the carrying on of a trade by the liquidator or by the Company.

Lawrence, J. whose judgment was later on confirmed by the Court of Appeal at p. 742 observed:

"The only question is: How were the assets liquidated? Did that form of liquidation involve the carrying on of a trade by the liquidator or by the company? No authority was cited to me which indicates that, if a company is formed for the purpose of exploiting a certain asset and chooses to go into voluntary liquidation for the purpose of the realisation of that asset, and realises that asset by the mere liquidation of the company's assets, that attracts tax any more than the mere liquidation of any other company's assets."

15. The decision of Lawrence J. was confirmed by the Court of appeal and the following observations of Greene, L. J. at pp. 750-51 are relevant:

"The facts that the liquidation took place, and that the liquidator acted in a particular way because those interested in the shares of the Company had agreed that the liquidation should take place and that the assets should be sold, appear to me to be no evidence whatever to justify the finding of the

Commissioners. Most companies have in their memorandum a power to sell their assets, and it is a very common thing indeed for companies when they are reconstructed to sell their assets in whole or in part, to have an arrangement or an agreement between the shareholders beforehand, deciding what is to be done, agreeing that certain resolutions shall be passed putting the company into liquidation and agreeing that the assets of the company in the liquidation shall be disposed of by the liquidator in a particular way. To accept the proposition which has been put before us would really come to this, that whenever a company acted in that way, the act of the liquidator in selling the assets would be an act of the company trading, instead of an act of realisation.....In my opinion they were nothing more or less than receipts by the liquidator on realisation by him in the ordinary course of his duty as liquidator to realise and get in the assets of the Company."

16. Incidentally, it may be mentioned that this is a case of voluntary liquidation which is also the case before us. At the other extreme we shall notice another authority which will show that in an appropriate case the liquidator can be held to carry on a trade or business That is the case decision of (1939) Tax Cas 337 There by two agreements dated 9th July, 1928, the Appellant Company acquired the assets of two other companies, of which one made and distributed cinema films and the other distributed such films, and thereafter carried on business in succession to those companies. In 1931, the appellant company went into liquidation and the liquidator sold to two newly formed companies its plant, stock, etc., but retained the benefit of contracts made or to be made for exhibiting films on hand at the date of the liquidation. After the liquidation the liquidator produced no new films and by himself entered into no new contracts for the distribution of films. But the new companies carried out the existing contracts, paying 90 per cent of the proceeds to the liquidator, and one of them also made new contracts to exploit certain films which remained the property of the Liquidator, paying over to him in this instance 80 per cent of the proceeds.

17. On appeal against an assessment under Schedule D made upon him for the year 1932-33 the Liquidator contended that no trade had been carried on by him. The Special Commissioners held that the arrangements made constituted the new companies agents for the liquidator, and that in both cases the liquidator was himself trading through the new companies and was accordingly properly assessed. The Court confirmed the findings of the Special Commissioners. The point of distinction is clearly put by Finlay, J., at pp. 352-53 of that report as follows:

"Of course, if the whole thing had been sold, lock, stock and barred, then in that event no business would have been carried on by the Liquidator, but also in that event the whole of the profits would have been assessable in the hands of the operating company, and it seems to me that what was done here makes the whole difference. It seems absolutely certain that a trade here was being carried on in respect of these current films. Whose trade was it? I think that there was

ample evidence that it was the trade of the Liquidator. He had reserved his rights with regard to these films; he was to take the profits in respect of them, after allowing a sum for the trouble of the companies, and the substance of the thing was, therefore, that the two companies were on his behalf carrying on the trade in respect of these current films, carrying it on on behalf of the liquidator, who, therefore, is liable for the profits."

18. Nothing like this appears on the facts of the present case before us. Here the Liquidator reserves no right. He carried on no business. He sold outright this mining lease with the mining rights. In fact this Rs. 5 lakhs represent, in our view, on the facts of this case the capitalised value of this mining lease with mining rights.

19. Mr. Pal for the Department tried to attract us by the seductive doctrine of annuity laid down by the Privy Council in AIR 1935 143 (Privy Council) . That case really has no application either in law or on facts to the present case before us. There the assessee who owned a nine annas share in an estate with the object of discharging his debts and of obtaining for himself an adequate income for his life, conveyed the greater portion of his estate to his son-in-law's mother who owned the remaining seven annas in the estate. The consideration for such transfer was (i) the payment of the assessee's debts amounting to Rs. 10,26,937; (ii) a cash payment of Rs. 4,73,063, and (iii) an annual payment of Rs. 2,40,000 to the assessee for his life. There the Patna High Court held that the amount of Rs. 2,40,000 thus received by the assessee annually was income and not a receipt of a capital sum in instalments and was therefore assessable to Income Tax and super-tax. The Privy Council confirmed the decision of the Patna High Court and dismissed the appeal. Annuity means periodical benefit or income. The present sale of the mining lease or mining rights in the case before us is an outright assignment with no reservation of any benefit to the Liquidator and it produced no income in the shape or in the manner of an annuity or any periodical return. The doctrine of annuity, therefore, has no application to the problem raised in the question before us in this reference.

20. It will not be inappropriate to conclude our discussion on this subject by a reference to the Companies Act. But before we do so we shall set put the relevant clause of assignment in this case to show why we hold this as an outright transfer without any reservation for the Liquidator. The relevant clause reads as follows:

".....the Assignor Company does hereby assign and transfer and the liquidator both hereby confirm unto the assignee Company All that the benefit and advantage provided and mentioned in the said recited agreement of the twenty-eighth day of May One thousand nine hundred and fifty three and all other benefits rights and advantages " which are held under the compromise and have arisen or may arise under the said agreement together with full power and authority to ask, demand, sue for, recover, receive and realise from the said Chrestian Mica Industries Limited.....to hold the said benefits, rights and

advantages upto the Assignee Company for ever free from encumbrances"

This was a complete and outright transfer. Therefore, the money or consideration received in lieu thereof must be held in the facts and circumstances of the case to be a capital receipt.

21. Turning now to the relevant Sections of the Companies Act the types of winding up under the Indian Companies Act are three -- (1) winding up by the Court, (2) voluntary winding up and (3) winding up subject to the supervision of the court. In the facts of this case it is a case of voluntary winding up.

22. Section 512(1) of the Companies Act sets out, inter alia, the powers and the duties of a liquidator in voluntary winding up. Sub-clause (a) thereof provides that in the case of a members' voluntary winding up with the sanction of a special resolution of the company, and in the case of a creditors' winding up, with the sanction of the Court, or, the committee of inspection or, if there is no such committee, by a meeting of the creditors, the liquidator may exercise any of the powers given by Clauses (a) to (d) of Sub-section (1) of Section 457 to a Liquidator in winding up by the Court. It is also provided by Sub-clause (b) of that Section that without the sanction referred to in the previous Sub-clause (a) the Liquidator in a voluntary winding up may exercise any of the powers given by this Act to the Liquidator in a winding up by the Court. Now in order to look at the powers of the Liquidator in a winding up by the Court Section 457 is material. Section 457(1)(b) of the Companies Act provides that the Liquidator in a winding up by the Court shall have power with the sanction of the Court to carry on the business of the company so far as may be necessary for the beneficial winding up of the company. The law, therefore, is clear that the Liquidator can carry on the business of the company but its limitation is strict and such carrying on of the business of the company by the Liquidator can only be "so far as may be necessary for the beneficial winding up of the company."

23. Therefore, In appropriate cases even under the Indian Companies Act it is possible for the Liquidator to carry on business of the company in so far as it is necessary for the beneficial winding up of the company and in that event business receipt will be a trading receipt or a revenue receipt and not a capital receipt. But then sub- Clause (c) of Section 457(1) of the Companies Act also describes the other power of the liquidator with the sanction of the Court to sell the immovable and movable property and actionable claims of the company by public auction or private contract, with power to transfer the whole thereof to any person or body corporate, or to sell the same in parcels. That would, therefore, include the Liquidator's power to sell the assets of the company or to transfer.

24. We have come to the conclusion on the facts of this case that what the Liquidator has done in obtaining the receipt for Rs. 5,00,000 is that he has sold or and/or transferred and/or assigned the mining lease and the rights completely and for ever and free from all encumbrances in order to realise and get in the

assets of the company in liquidation.

25. For the reasons stated above we answer the question by saying that the sum of Rs. 5,00,000/- in the facts of this case was a capital receipt and not a revenue receipt in the hands of the assessee.

26. There will be no order as to costs because no one appeared for the Liquidator before us.

A.C. Sen, J.

27. I agree.