

(2002) 10 KL CK 0003

In the High Court Of Kerala

Case No : Report No. 58 in CP. No. 19 of 1992, Report No. 40 and 51 in CP. No. 2 and 29 of 1995 11 October 2002

In re KTC Tyres (India) Ltd.

Date of Decision : 11-10-2002

Acts Referred:

COMPANIES ACT, 1956 — Section 476, 520, 529, 529A, 530
Income Tax Act, 1961 — Section 143, 178

Citation : (2003) 1 ILR (Ker) 321 : (2002) 125 TAXMAN 899

Hon'ble Judges : K.S. Radhakrishnan, J; K.A. Mohamed Shafi, J

Bench : Full Bench

Advocate : K. Moni, P.K. Ravindranatha Menon, for the Appellant;

Judgement

K.S. Radhakrishnan, J.

These reports have been placed before us on a reference made by the learned single Judge in view of the importance other questions raised. The matter arises in connection with the liquidation proceedings of KTC Tyres (India) Limited, Hendez Electronics Limited and Venad Pharmaceuticals and Chemicals Limited. For the convenient sake we may refer to Report No. 58 in connection with KTC Tyres (India) Limited. Statement and reply statement has been filed by the contesting parties in that case. In the report Official Liquidator prayed for the following reliefs.

(i) take this report on record;

(ii) direct that no Income Tax is payable from the sale proceeds as capital gains tax, advance tax instalments and additional tax, if any, on the sale of the charged assets of the company in liquidation until the dues of the secured creditors and workmen creditors are paid in full;

(iii) declare that no advance tax is payable in respect of this company in liquidation for the assessment year 1997-98 and subsequent assessment years until the claims of the secured creditors and workmen creditors are paid in full; and

(iv) pass such other orders as deemed fit and proper in the premises of the case.

These are the requests made in other reports as well.

2. We may refer to the facts in report No. 58 which is as follows : The Company KTC Tyres (India) Limited was ordered to be wound-up by the company court as per order dated 22-1-1993. During the pendency of liquidation Official Liquidator had disposed of all the movable and immovable assets by public auction and obtained total sum of Rs. 1,78,37,000 in May 1996. Full consideration was received by the Official Liquidator. Entire assets of the company in liquidation have been charged to Canara Bank, Calicut and Industrial Development Bank of India, IDBI Tower, Cuffe Parade, Mumbai. During the course of the winding-up proceedings, Official Liquidator had settled the list of creditors and the total amount admitted to the secured creditors and workmen creditors would come to Rs. 12,57,12,181. Out of the admitted amount, the Official Liquidator had paid first dividend of 16 paise in a rupee to the secured creditors and workmen creditors amounting to Rs. 1,99,22,706 vide order dated 17-2-1998 in M.C.A. No. 31 of 1998 in C.P. No. 19 of 1992.

3. The Company in liquidation had filed return of income regularly upto the assessment year 1999-2000. The Company had not earned any income till the assessment year 1996-97. On the sale of the immovable properties of the Company, a sum of Rs. 1,78,37,000 was received by the Official Liquidator. The stand of the Official Liquidator is that payment of Income Tax, capital gain tax, advance tax and additional tax is to be considered only after satisfying the dues of the secured creditors and workmen.

4. A statement has been preferred on behalf of the Income Tax Department. In the return submitted by the Official Liquidator for the assessment year 1997-98 on 25-11-1997 a note was appended which is extracted below :

"Note:- In the instant case, the dues of the secured creditors and workmen are yet to be settled. Hence, in the light of the order dated 25-9-1990 on Report No. 120 in C.P. No. 7 of 1979 and 4 of 1980 in the matter of Giovanola Binny Limited (In liquidation) order dated 8-4-1991 on Report No. 34 in C.P. No. 28 of 1988 in the matter of Premier Steel (P) Ltd. (In liquidation) and order dated 18-10-1995 on Report No. 56 in CP 6/90 in the matter of Southern Organics (P) Ltd. (In liquidation), etc., passed by the Hon"ble High Court of Kerala, the payment of tax is to be considered only after the dues of the secured creditors and workmen are paid in full. Therefore, in this case the payment of Income Tax for the assessment year 1997-98 does not arise."

Counsel for the Official Liquidator, Sri K. Moni submitted that as per sections 529A and 530 of the Companies Act special rights are conferred on the workmen and the rights of the workmen are pari passu with that of the secured creditors of the company in liquidation. Counsel submitted workmen of the company in liquidation being made secured creditors of the company and assets of the company in liquidation they would get position along with secured creditors. In

order to establish this contention counsel placed reliance on the decision of this court in *In Re: Giovanola Binny Ltd. (In Liquidation)*;, , *Syndicate Bank and another Vs. The Official Liquidator and others*, .

5. Senior Standing Counsel for the Income Tax Department, Sri P.K. Ravindranatha Menon, on the other hand contended that department will have preference over the workmen on the assets of the company in liquidation. Counsel made reference to the decision of this court in *ITO v. Official Liquidator, Swaraj Motors (P) Ltd. (1978) 48 Comp Cas 11 (Bom)*. Learned Company Judge found favour with the contention raised on behalf of the department and held as follows :

"To me, it appears that capital gains is part of the incidence of the sale effected by the Official Liquidator of the property belonging to the company just like a liability for stamp duty, registration charges or the like, it is not a debt due by the company as on the date of commencement of winding-up or the order for winding-up.

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But section 529A only puts the claims of the workmen *pari passu* with the secured creditors. It can only be as regards the assets that are available for distribution which naturally must be after providing for the expenses in connection with the winding-up. So the decision of the Division Bench that capital gains tax must be taken as part of the winding-up expenses still holds good."

We will at the outset examine whether the decision of the Division Bench in *Income Tax Officer, B-Ward Vs. Official Liquidator, Swaraj Motors (P.) Ltd. (In liquidation)*, read with the decision of the Apex Court in *Imperial Chit Funds (P) Ltd. Vs. Income Tax Officer, Ernakulam*, would conclude the issue raised in this case, as opined by the learned Company Judge. If that be so, we could dispose of the Reports accordingly following the principle laid down in those cases. The question posed before the Division Bench in *Swaraj Motor (P) Ltd.'s case (supra)* is whether Income Tax Department has got any preference or they could be treated just like any other creditor. Liquidator took up the stand that Income Tax Department must prove the claim and get dividend *pari passu* just like any other simple creditor of the company. Division Bench took the view that before assets are distributed among the creditors amount due to Income Tax Department is payable as provided in sections 520 and 476 of the Companies Act. The court held that the liquidator would pay tax demanded for distributing the dividend. We may now examine whether the point raised by the Official Liquidator, is covered by the decision of the Apex Court in *Imperial Chit Funds (P) Ltd.'s case (supra)*. What was raised before the Apex Court was whether order passed u/s 178 of the Income Tax Act would have preference over rights of unsecured creditors. The Apex Court held that Income Tax Department is to be treated as secured creditor and would get priority in the matter of payment. *Imperial Chit Funds (P) Ltd.'s case (supra)*, is an authority for the proposition that between unsecured creditors

the claim of tax due u/s 178 of the Income Tax Act would have preference over all other claims of unsecured creditors.

6. We are of the view, Apex Court in Imperial Chit Funds (P) Ltd.'s case (supra) as well as the decision of the Division Bench in Swaraj Motors (P) Ltd.'s case (supra) had no occasion to deal with the scope of section 529A of the Companies Act, as amended. Section 529A is extracted below for easy reference.

"529A. Overriding preferential payments.(1) Notwithstanding anything contained in any other provision of this Act or any other law for the time being in force, in the winding-up of a company

(a) workmen's dues; and

(b) debts due to secured creditors to the extent such debts rank under clause (c) of the proviso to sub-section (1) of section 529 pari passu with such dues;

shall be paid in priority to all other debts,

(2) The debts payable under clause (a) and clause (b) of sub-section (1) shall be paid in full, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions."

We have to examine the claim of the Income Tax Department vis-a-vis section 529A of the Companies Act. Section 529A was inserted in the Companies Act by Act 35 of 1985. Sections 529A and 530 confer special rights and benefits on the workmen of the undertaking. Workmen get rights pari passu with those of the secured creditors on the assets of the company in liquidation. Purpose of the section is to ensure that workmen should not be deprived of their rights in the event of liquidation of the company. Section 529A has employed a non obstante clause which says that "notwithstanding anything contained in any other provision of the Companies Act or any other law for the time being in force". The non obstante clause whittles down the priority of even the crown debts. It is the general concern for the interest of the workmen that is saved by the Apex Court in the decision in Workmen of Rohtas Industries Ltd. v. Rohtas Industries Ltd. (1987) 62 Comp Cas 872 (SC). The Apex Court held that subsistence and living of the workers is of paramount importance and has to rank with highest priority. Their wages and emoluments upto the date of closure of the company will rank in priority over the secured creditors.

In Giovanola Binny Ltd.'s case (supra) this court has held that tax on capital gains cannot be claimed in preference to dues of bank and claims of workmen.

7. Counsel for the Income Tax Department submitted that the tax demanded is capital gain tax on the amount incurred for the winding-up of the company as per section 520 of the Act and section 476 and that tax is payable as "cost, charges and expenses incurred in the winding-up." In this connection we may refer to section 520 also. Section 520 of the Companies Act reads as follows :

"520. Costs of voluntary winding-upAll costs, charges and expenses properly

incurred in the winding-up, including the remuneration of the liquidator, shall, subject to the rights of secured creditors, if any, be payable out of the assets of the company in priority to all other claims." (Emphasis, here italicised in print, supplied)

Claim of secured creditors has not been overridden by section 520 which is subject to rights of secured creditors. The right of secured creditors are safeguarded by section 529A by employing a non obstante clause. Therefore, the argument advanced by the standing counsel on behalf of the Income Tax Department on the basis of sections 520 and 476 cannot be sustained. The above view is fortified by the decision of the Bombay High Court in Polyolefins Industries Ltd. Vs. Kosmek Plastics Manufacturing Co. Ltd., as well as Syndicate Bank's case (supra) with which we concur. Finally, counsel for the Income Tax Department contended that the amount due to the department by way of capital gain tax is not a debt within the expression "debt" used in section 529A. Section 529A has used the expression "workmen's dues". Further, the expression "debt" is used to mean any pecuniary liability. In Commissioner Of Wealth-Tax, Assam Vs. Ahmed Tea Co. (Pvt.) Ltd., the court held any liability to pay Income Tax and the assessee has set apart certain amount thought to be necessary for discharging the tax liability, the same has been ascertained it cannot be said that the amount is not a debt. Therefore, the tax liability may also come within the expression "debt" u/s 529A. The Apex Court in Imperial Chit Fund's case (supra), or the Division Bench in Swaraj Motors case (supra) had no occasion to examine the scope of section 529A which was introduced by the legislature by employing a non obstante clause which overrides other provisions under the Companies Act as well as under other legislations.

In view of the above circumstances we accept the reports of the Official Liquidator and hold that no Income Tax is payable on the sale proceeds as capital gain tax, advance tax instalments and additional tax, if any u/s 143(1A) on the sale of the charged assets of the company (in liquidation) until the dues of the secured creditors and workmen creditors are paid in full. It is so ordered and all the reports are disposed of accordingly.