(1998) 08 BOM CK 0047

In the Bombay High Court

Case No : Company Petition No. 910 of 1987

In Re: Starit India Ltd. (In Liquidation)

Date of Decision : 28-08-1998

Acts Referred:
Companies Act, 1956 — Section 529A, 530, 530(1)
Income Tax Act, 1961 — Section 178, 178(1), 178(2), 178(3)

Citation : (1999) 98 CompCas 818 : (2000) 242 ITR 275

Hon'ble Judges : F.I. Rebello, J

Bench : Single Bench

Advocate : J.P. Devadhar, S.A. Tawade, for workers, S.K. Shah, instructed by Sridhar and Co. for contributories, for the Appellant;

Judgement

F.I. Rebello, J.—The short but interesting question that arises in this matter is whether capital gains tax payable u/s 45 of the Income Tax Act, 1961, has precedence over the claims of other secured creditors covered by Section 530 read with Section 529A of the Companies Act, 1956.

2. The company is under liquidation. The workers of the company in liquidation had filed claims for payment of their dues as secured creditors. By order dated August 31, 1996, the court allowed the application and also directed payment of interest. The said order has not been challenged. The present dispute is regarding payment of interest pursuant to the order of this court dated August 31, 1996. On behalf of the Department of Income Tax, Government of India, the same has been opposed on the ground that the department has a preferential right in respect of the properties sold by the liquidator and that the capital gains tax has preference over dues of other secured creditors. The department has claimed two amounts one in an amount of Rs. 10 lakhs and the other of about Rs. 90 lakhs as capital gains tax pursuant to the sale of a property. The amount of Rs. 10 lakhs is not in issue here. The official liquidator as per para. 7 has averred that the present fund position of the company is around Rs. 43,68,230.25. If the demand of the department is to be satisfied then no amount would be available to be paid to other secured creditors including the workers.

3. It is, further contended on behalf of the department that the order of this court is dated August 31, 1996, and the learned judge while passing the order has not taken into consideration the judgment of the apex court dated March 19, 1996, in the case of Imperial Chit Funds (P) Ltd. Vs. Income Tax Officer, Ernakulam, . If the said judgment is considered it is contended then it must be held that u/s 178 of the Income Tax Act, tax dues of the department are a preferential claim over all secured creditors.

4. For that purpose it would be essential to consider Section 178 of the Income Tax Act, 1961. Section 178 reads as under :

"178. Company in liquidation.-(1) Every person-

(a) who is the liquidator of any company which is being wound up, whether under the orders of a court or otherwise ; or

(b) who has been appointed the receiver of any assets of a company (hereinafter referred to as ''the liquidator'') shall, within thirty days after he has become such liquidator, give notice of his appointment as such to the Assessing Officer who is entitled to assess the income of the company.

(2) The Assessing Officer shall, after making such inquiries or calling for such information as he may deem fit, notify to the liquidator within three months from the date on which he receives notice of the appointment of the liquidator the amount which, in the opinion of the Assessing Officer, would be sufficient to provide for any tax which is then, or is likely thereafter to become, payable by the company.

(3) The liquidator-

(a) shall not without the leave of the Chief Commissioner or Commissioner, part with any of the assets of the company or the properties in his hands until he has been notified by the Assessing Officer under Sub-section (2) ; and

(b) on being so notified, shall set aside an amount equal to the amount notified and, until he so sets aside such amount, shall not part with any of the assets of the company or the properties in his hands :

Provided that nothing contained in this sub section shall debar the liquidator from parting with such assets or properties for the purpose of the payment of the tax payable by the company or for making any payment to secured creditors whose debts are entitled under law to priority of payment over debts due to Government on the date of liquidation or for meeting such costs and expenses of the winding up of the company as are in the opinion of the Chief Commissioner or Commissioner reasonable.

(4) If the liquidator fails to give notice in accordance with sub Section (1) or fails to set aside the amount as required by Sub-section (3) or parts with any of the assets of the company or the properties in his hands in contravention of the provisions of that sub-section, he shall be personally liable for the payment of

the tax which the company would be liable to pay :

Provided that if the amount of any tax payable by the company is notified, under Sub-section (2), the personal liability of the liquidator under this sub-section shall be to the extent of such amount.

(5) Where there are more liquidators than one, the obligations and liabilities attached to the liquidator under this section shall attach to all the liquidators jointly and severally.

(6) The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other law for the time being in force."

5. Previous to the judgment in Imperial Chit Funds (P.) Ltd. (In Liquidation) v. ITO [1996] 86 Comp Cas 555 there was a conflict of views amongst the High Courts as to the interpretation of Section 178(1) and (2) of the Income Tax Act and Section 530 of the Companies Act. The question which the apex court was called upon to answer was whether the dues of secured creditors u/s 529A of the Companies Act had prior claim over the claim of the department u/s 178(1) and (2) of the Income Tax Act. The apex court held, considering the purpose for which the section was introduced in the year 1961, that the object sought to be achieved by the provisions in Chapter XV was "to fasten liability to pay the tax". The apex court while so holding upheld the views taken by the High Courts of Kerala and Andhra Pradesh. The apex court held that the claim u/s 178(1) and (2) has preference over the claims of the other secured creditors u/s 529A of the Companies Act.

6. It is based on this judgment that the Department has contended that they have a preferential claim over all other secured creditors in respect of properties sold by the liquidator.

7. Let us examine therefore whether the ratio of judgment in Imperial Chit Funds (P.) Ltd. (In Liquidation) v. ITO [1996] 86 Comp Cas 555 will apply to the case in question.

8. Sub-section (1) of Section 178 of the Income Tax Act provides that every person who is appointed as a liquidator of any company which has been wound up whether under the orders of the court or otherwise or appointed as a receiver of any assets of the company shall within thirty days after he becomes such liquidator, give notice of his appointment to the Assessing Officer who is entitled to assess the income of the company. Sub-section (2) of the same section provides that the Assessing Officer shall after making such inquiry or calling for such information as he may deem fit, notify the liquidator within three months from the date on which he receives notice of the appointment of the liquidator, the amounts, which in the opinion of the Assessing Officer would be sufficient to provide for any tax which is then or is likely thereafter to become payable by the company. In other words what is contemplated is that within three months of receipt of the communication by the liquidator of his appointment, the Assessing

Officer must assess tax which is due or likely thereafter to become payable by the company. The Assessing Officer therefore will consider the material then available for the purpose of determining the tax dues. What becomes clear is that what transactions may come in future and in respect of which tax may become payable prima facie cannot be the subject-matter of the order which the Assessing Officer may pass.

9. Sub-section (3) is also relevant for the purpose of discussion. The said sub-section in Clause (a) provides that liquidator shall not without leave of the Chief Commissioner or Commissioner part with any assets of the company or the properties in his hands until he has been notified by the Assessing Officer under Sub-section (2) ; by Clause (b) it provides that on being so notified the liquidator shall set aside the amount equal to the amount notified and until he so sets aside such amount he shall not part with any of the assets of the company or the properties in his hands. It is thus clear that under Clause (a) of Sub-section (3) the liquidator cannot part with any of the assets of the company or the properties in his hands until he has been notified in terms of Sub-section (2) of Section 178. Sub-clause (b) of Sub-section (3) provides for a situation on being notified. It provides that the liquidator on being so notified shall set aside an amount equal to the amount notified and until he so sets aside such amount he shall not part with any of the assets of the company or the properties in his hands. In other words, until he has made provision for meeting the tax liability as assessed by the Assessing Officer the liquidator is prohibited from parting with the assets and properties of the company in his hands. Sub-section (3) therefore deals with parting with the assets of the company.

10. The important part however is the proviso to Sub-section (3) which provides that nothing contained in that sub-section shall debar the liquidator from parting with such assets or properties for the purpose of payment of the tax payable by the company or for making any payment to the secured creditors whose debts are entitled under law to priority of payment over debts due to Government on the date of liquidation or for meeting such costs and expenses of the winding up of the company as are in the opinion of the Chief Commissioner or Commissioner reasonable. The embargo created by Sub-clauses (a) and (b) of Sub-section (3) in the event the liquidator has to part with assets or properties, is not applicable in the event the liquidator has to dispose of assets or properties for payment of tax payable by the company ; or making any payment to secured creditors whose debts are entitled under law to priority of payment over others or for meeting such costs and expenses of the winding up of the company as are in the opinion of the Chief Commissioner or Commissioner reasonable. In such a situation the liquidator has power to part with the assets or properties notwithstanding Sub-clauses (a) and (b) of Sub-section (3).

11. The scheme and purpose, therefore, which emerges is that the liquidator is bound to make provision for payment determined under Sub-section (2). Once he makes the provision, the bar of Section 178 goes. In other words, once the

amount is set aside, as assessed for tax the liquidator is not precluded from disposing of the assets or properties of the company. Sub-sections (1), (2) and (3) therefore read in harmony do not mean that transactions that take place after the compliance by the liquidator with Sub-clause (b) of Sub-section (3), are prohibited. The very proviso to subsection (3) treats tax, secured creditors and costs and expenses of winding up on the same footing. Section 178(1) and (2), therefore, do not place transactions of safe of assets subsequent to the order of the Assessing Officer as a preferential payment over other secured creditors. Therefore, the judgment of the apex court is referable only to the "amount" assessed u/s 178(2) of the Income Tax Act. So read and in order to be in conformity with the "amount" assessed, if no money is available for payment of the amount assessed, the assets/properties in the first instance will have to be sold for meeting the liability u/s 178(2) notwithstanding the proviso to Sub-section (3).

12. If this construction is not followed it will be impossible to construct Section 178 of the Income Tax Act and Sections 529A and 530 of the Companies Act harmoniously. Section 178 of the Income Tax Act was introduced in 1961, whereas Section 529A and the amendment to Section 530 of the Companies Act have been brought by an amendment in the year 1985. Section 529A has been given overriding effect over other dues including the dues u/s 530(1)(a) and also any other law for the time being in force. A proper reading of these two sections of the Companies Act read with Section 178 of the Income Tax Act as interpreted by the apex court must clearly therefore lead to the conclusion that after the requirement of Section 178(2) has been complied with the subsequent tax dues are subject tu Sections 529A and 530 of the Companies Act. Dues u/s 529A thus will have precedence over dues u/s 530(1)(a). In my view, therefore, the capital gains tax or subsequent tax dues on account of the sale of the properties by the liquidator do not have preferential rights over the dues of workers and other secured creditors and these rights must have precedence over the tax dues of the Department u/s 530(1)(a). Section 178 of the Income Tax Act will have precedence only over tax assessed u/s 178(2).

13. In the light of the above, the objections by the Department to the payment of interest ordered by this court to the workers is rejected. The workers therefore would be entitled to the interest as ordered by the single judge of this court vide his order dated August 31, 1996.

14. In view of the above, the official liquidator''s report dated March 18, 1998, is allowed in terms of directions at (b) and (c) except the dates "April 1, 1998, to September 30, 1998", to read as "September 1, 1998, till February 28, 1999", in direction Clause (c).

