(1986) 01 KL CK 0034

In the High Court Of Kerala

Case No : M.F.A. No. 256 of 1980

Income Tax Officer APPELLANT

Vs

Official Liquidator RESPONDENT

Date of Decision : 29-01-1986

Acts Referred:

Companies Act, 1956 — Section 446, 528, 529, 530
Income Tax Act, 1961 — Section 156, 220, 220(2), 221

Citation : (1986) 59 CompCas 514 : (1986) 158 ITR 791

Hon'ble Judges : U.L. Bhat, J;K.T. Thomas, J

Bench : Division Bench

Advocate : P.K. Raveendranatha Menon, for the Appellant; T.V. Ramakrishnan, for the Respondent

Final Decision : Dismissed

Judgement

Bhat, J.—The Income Tax Officer, Ernakulam, has filed this appeal against the order of the learned single judge in company jurisdiction dismissing Application No. 239 of 1979 in B.C.P. No. 4 of 1961 (Income Tax Officer Vs. Official Liquidator,), filed by him.

2. Respondent is the official liquidator, the liquidator appointed in connection with the winding up of a company. The winding-up order was passed on October 30, 1961. The liquidator invited proof of claims and settled a list of creditors and filed the same in court on July 5, 1962. Subsequently, Income Tax assessment was completed in respect of the company for the years 1955-56 to 1958-59. Demand notices were served on the liquidator on February 23, 1963. Additional demand was made for the year 1955-56 by notice served on February 5, 1967. Thereafter, the Income Tax Officer filed Applications Nos. 3 of 1964 and 248 of 1968 for varying the list of creditors and that was allowed. The Department by letter dated January 29, 1971, required the liquidator to pay up the arrears of tax together with interest levied u/s 220(2) of the Income Tax Act. The Department sought to prove the debt before the liquidator by way of an affidavit

filed in August, 1969. The liquidator by order dated July 27, 1973, recognised the tax arrears as debt but declined to recognise the interest claimed u/s 220(2) as debt.

3. Thereupon, the Department filed Application No. 315 of 1973 before the company court contending that interest also should have been recognised. This was dismissed on the ground that priority claimed u/s 530 of the Companies Act, 1956, could not be recognised. The Department filed A.S. No. 563 of 1974 challenging this order. The appeal was allowed permitting the Department to prove the claim for interest before the liquidator as an unsecured creditor and the liquidator was directed to adjudicate upon the claim in accordance with law, particularly the provisions of the Companies Act and the Rules framed thereunder. The liquidator passed an order afresh on March 15, 1979, rejecting the claim for interest on two grounds, viz., that the claim was not supported by sanction obtained from the company court u/s 446(1) of the Companies Act and that the special provisions of the Companies Act will prevail over the provisions of the Income Tax Act, so that the Department cannot claim interest from the company in liquidation in respect of assessment made subsequent to the winding up. This order was challenged by the Department before the company court in Application No. 239 of 1979 which was rejected by the company court. It is this order which is now challenged in appeal.

4. The liquidator has recognised the demand for arrears of tax for the assessment years 1955-56 to 1958-59. Though the period in question is prior to the winding-up order, assessments were completed only thereafter. Therefore, the claim for arrears of Income Tax would be a debt provable in liquidation proceedings by the Department. The proof has been accepted. Consequently, the Department would be treated as an unsecured creditor and would be treated pari passu.

5. The dispute in the appeal relates to the claim for interest u/s 220(2) of the Income Tax Act. Section 156 of the Income Tax Act states that when any tax, interest, penalty, fine or any other sum is payable in consequence of any order passed under the Act, the Income Tax Officer shall serve upon the assessee a notice of demand in the prescribed form specifying the sum so payable. In regard to the original assessment, notice of demand was served in February, 1963. In regard to the additional assessment, notice of demand was served in February, 1967. Ordinarily, the assessee is liable to pay the demand within 35 days from the date of service of notice as laid down in Section 220(1), subject of course to the other provisions in that section. Sub-section (2) states that if the amount specified in any notice of demand u/s 156 is not paid within the period limited under Sub-section (1), the assessee shall be liable to pay simple interest at fifteen per cent, per annum from the day commencing after the end of the period mentioned in Sub-section (1). This provision also is subject to the other provisions of the section. u/s 221 of the Income Tax Act, penalty is leviable in addition to interest. Section 222 and the succeeding Sections relate to recovery.

Recovery could be made by attachment and sale of the assessee''s movable property or his immovable property, by arrest of the assessee and his detention in prison or by appointing a receiver for the management of his properties. Other modes of recovery are prescribed in Section 226 of that Act. Section 229 states that any sum imposed by way of interest, fine, penalty or any other sum payable under the provisions of that Act shall be recoverable in the manner provided in the Chapter for recovery of arrears of Income Tax.

6. Admittedly, the liquidator did not and could not comply with the demands made in the demand notices issued u/s 156 of the Income Tax Act. Payment was not made within 35 days or even thereafter. According to the Department, in these circumstances, Sub-section (2) of Section 220 came into operation and the assessee is liable to pay interest. The Department levied interest and moved the liquidator for recognising the claim. The liquidator held that the claim cannot be recognised for want of sanction u/s 446 of the Companies Act, and this view has been upheld by the learned single judge.

7. This view is evidently supported by a decision of a learned single judge of this court in Official Liquidator Vs. Income Tax Officer, , upheld by a Division Bench of this court in Income Tax Officer Vs. Official Liquidator, Swaraj Motors (P.) Ltd. (In Liquidation), . But, to the extent these decisions lay down that sanction is necessary before levying interest or making the claim, they have been overruled by a Full Bench of this court in Income Tax Officer Vs. Official Liquidator, . The view taken by the Full Bench is in consonance with the decision of the Supreme Court in S.V. Kondaskar, Official Liquidator and Liquidator of the Colaba Land and Mills Co. Ltd. Vs. V.M. Deshpande, Income Tax Officer, Companies Circle I(8), Bombay and Another, .

8. The learned single judge, however, held that the claim for interest u/s 220(2) of the Income Tax Act cannot be recognised also because that provision is in conflict with the provisions and the scheme of the Companies Act in regard to companies in liquidation and, therefore, the provision is not applicable to such companies in liquidation. This ground also is seriously challenged by the learned counsel for the appellant.

9. The scheme of the provisions of the Income Tax Act found in Sections 156, 220 and other provisions would clearly indicate that the liability to pay interest is incurred on default to meet a valid demand made u/s 156 of the Income Tax Act. This is a statutory liability incurred by the assessee under this provision. When a company is not in liquidation, this provision of the Income Tax Act would apply to the company and a claim for interest would be valid. The question for consideration is whether this provision could be treated as applicable to a company in liquidation.

10. In this connection, it is necessary to notice some of the provisions of the Companies Act, Part VII of the Act deals with winding up. Chapter II of this Part deals with winding up by court. In a case like the present one, by virtue of

Section 441, winding up shall be deemed to have commenced at the time of presentation of the petition for winding up. That was in 1961. Section 442 deals with the power of a court to stay or restrain proceedings against the company. Section 446 deals with the power of the company court. u/s 454, a statement of affairs indicating particulars of the company including assets, debts, liabilities, creditors, etc., has to be made to the official liquidator. u/s 455, the official liquidator has to make a preliminary report to the court indicating, inter alia, the estimated amount of assets and liabilities. Custody of the company''s property is to be taken by the official liquidator and all the property shall be deemed to be in the custody of the court as indicated in Section 456. Section 457 deals with powers of the liquidator. He has to realise the assets of the company and distribute the same. Section 467 states that the court shall settle a list of contributories and cause assets of the company to be collected and applied in discharge of its liabilities. u/s 474, the court may fix a time within which the creditors are to prove their debts or claims, or to be excluded from the benefit of any distribution before those debts or claims are proved.

11. Section 528 states that in every winding up (subject in the case of insolvent companies to the application in accordance with the provisions of this Act or the law of insolvency), all debts payable on a contingency, and all claims against the company shall be admissible to proof against the company, a just estimate being made, so far as possible, of the value of such debts or claims. Section 529 states that in the winding up of an insolvent company, the same Rules shall prevail and be observed with regard to debts provable, the respective rights of secured and unsecured creditors, as are in force for the time being under the law of insolvency. Section 530 deals with preferential payments. The highest priority is to all revenues, taxes, cesses and rates due from the company to the Central or a State Government or to a local authority at the relevant date as defined in Clause (c) of Sub-section (8) and having become due and payable within the 12 months next before that date. The relevant date is the date of appointment of provisional liquidator or if no such appointment is made, the date of winding-up order.

12. Arrears of tax and interest claimed became due long after the winding-up order was passed, that is, long after the relevant date mentioned in Section 530(1)(a). Hence, priority u/s 530 will not apply to these claims. Therefore, the Department is to be treated only as an unsecured creditor who can look to payment of the debt only in liquidation proceedings. The Department is subject to the jurisdiction of the liquidator and the company court. This, of course, is not specifically stated in the Income Tax Act. But that is the consequence naturally flowing from the provisions of the Companies Act. That is why the Department moved the liquidator for recognising the claim for arrears of tax and interest. If in all cases the liquidator is bound to accept or recognise a claim, no purpose will be served by the law insisting on any creditor to approach the liquidator or the company court for discharge of the debt.

13. From a combined reading of Sections 156 and 220 of the Income Tax Act, it is obvious that an assessee who is served with a valid demand notice and fails to pay the tax within the statutory period, incurs the liability to pay interest on the arrears of tax. These provisions are certainly based on the assumption that the assessee is a free agent who is by himself in a position to discharge the tax. Being such a free agent, it is up to him to make the payment and any failure to make the payment would be visited with the liability to pay interest. But this cannot be the consequence where the assessee is a company in liquidation within the control of the liquidator and the company court. The Department, in regard to the claim we are considering, is only in the position of an unsecured creditor. An unsecured creditor cannot seek to recover the debt due to him outside the framework of the liquidation proceedings. He has to look to the liquidator and the company court for payment. He can expect to receive the payment only pan passu along with other unsecured creditors out of the funds available for such discharge from what is realised by the liquidator. The Department has no priority even in regard to the claim involved in this case. Its position is the same as that of any other unsecured creditor. The company in liquidation is not a free agent; nor is the liquidator a free agent who could pay the arrears of tax from the funds available with him, of his own volition. He can only make a pro rata payment out of the assets realised and after settling the list of creditors and determining the debts due to various creditors. Therefore, when the liquidator falls to make payment within 35 days of the service of demand notice on him, it cannot be said that he is a defaulter who is to be visited with the liability to pay interest u/s 220 or even the penalty u/s 221.

14. Provisions of the Companies Act clearly indicate that an unsecured creditor must prove his debt and all such debts are to be paid pari passu. Consequently, the claim of the Department for arrears of tax has to be proved in liquidation proceedings. The Department also must stand in the queue to receive its due. The liquidator is not a free agent to make payment of arrears of tax. It is only where an assessee has no legal impediment to pay the arrears of tax but nevertheless fails to pay the tax that the liability to pay interest u/s 220 can be said to have been incurred. That certainly cannot apply to a company in liquidation or the liquidator. Therefore, it is evident that the provisions of Section 220 cannot apply to a company in liquidation governed by the provisions of the Companies Act. The fundamental basis of Section 220 of the Income Tax Act is in clear conflict with the scheme and provisions of the Companies Act. Therefore, we hold that Section 220 of the Income Tax Act cannot apply to a company in liquidation which is governed by the provisions of the Companies Act.

15. We seek support for this view from the decision of the Supreme Court in Union of India (UOI) and Another Vs. India Fisheries (P) Ltd., . The provision which came up for consideration was Section 49E of the Indian Income Tax Act, 1922, which is similar to Section 245 of the Income Tax Act, 1961. According to this provision, where refund is found to be due to any assessee, the Department may, in lieu of payment of the refund, set off the amount to be refunded against

the sum, if any, remaining payable under the Act by the assessee, after giving an intimation in writing of the action proposed to be taken. The winding-up order in that case was passed on October 11, 1950, and for the assessment year 1948-49, assessment was made after winding up, viz., December 8, 1950. The amount was claimed from the official liquidator in 1951. The claim was adjudged and allowed as an ordinary claim in 1952. In 1952, the liquidator declared dividend of 9 1/2 annas in a rupee and paid a portion of the claim. For the assessment year 1955-56, the Department claimed advance tax. That was paid. In the regular assessment, the amount of tax determined was much less than the advance tax paid. Instead of returning the balance, the Department sought to set it off against the balance due for the assessment year 1948-49. Certainly, under the provisions of the Income Tax Act, the Department was entitled to set off the amount otherwise refundable. That would have meant that the Department could collect the debt due to it not pro rata as other unsecured creditors but could collect something more. That would be against the scheme of the provisions of the Companies Act regarding a company in liquidation, though the provision of the Income Tax Act is not subject to any other provision of law on the basis of which the Supreme Court held that the provision would not be applicable to companies in liquidation but are governed by the provisions of the Companies Act. The court observed (at pp. 334 and 335 of 57 ITR and pp. 672 and 673 of 35 Comp Cas):

" The effect of these statutory provisions is, inter alia, that an unsecured creditor must prove his debts and all unsecured debts are to be paid pari passu. Therefore, once the claim of the Department has to be proved and is proved in the liquidation proceedings, the Department cannot by exercising the right u/s 49E of the Income Tax Act get priority over the other unsecured creditors. If we were to read Section 49E in the way suggested by the learned Additional Solicitor-General, it would be defeating the very object underlying Sections 228 and 229 of the Indian Companies Act, 1913. If there is an apparent conflict between two independent provisions of law, the special provision must prevail. Section 49E is a general provision applicable to all assessees and in all circumstances; Sections 228 and 229 deal with, the proof of debts and their payment in liquidation. In our opinion, Section 49E can be reconciled with Sections 228 and 229 by holding that Section 49E applies when insolvency Rules do not apply. Accordingly, agreeing with the High Court, we hold that the Income Tax Officer was in error in applying Section 49E and setting off the refund due."

16. We notice that Sections 528 and 229 of the Companies Act, 1956, correspond to Sections 228 and 229 of the Indian Companies Act, 1913. The principle laid down in the above decision is fully applicable to the facts of the present case.

17. On the basis of the observations of the Supreme Court in S.V. Kondaskar, Official Liquidator and Liquidator of the Colaba Land and Mills Co. Ltd. Vs. V.M. Deshpande, Income Tax Officer, Companies Circle I(8), Bombay and Another, and

the observations of the Full Bench of this court in Income Tax Officer Vs. Official Liquidator, , learned counsel for the appellant contended that the validity of the demand for interest can be decided only when recovery is sought for and not at any previous stage. We do not think this argument is available to the appellant. It was the appellant who approached the liquidator for recognising the claim for arrears of interest. Naturally, the recognition would be followed by payment pari passu, subject to availability of funds. The claim put forward before the liquidator and the company court is part of the process of recovery. Further, the Department subjected itself to the jurisdiction of the liquidator and the company court in making the claim before them. The Department cannot now turn round and say that the liquidator and the company court have no jurisdiction to hold that the claim is not valid.

18. We find no merit in the appeal and the same is dismissed with costs.