

(1981) 05 DEL CK 0003
In the Delhi High Court
Case No : IT Reference No. 32 of 1970

R. Dalmia

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 29-05-1981

Acts Referred:

Income Tax Act, 1922 — Section 2(4), 2(6C), 66(1)
Income Tax Act, 1961 — Section 10, 23(3), 4(3)(vii)

Citation : (1981) 7 TAXMAN 284

Hon'ble Judges : N.N. Goswamy, J

Bench : Single Bench

Advocate : G.C. Sharma, Bishamber Lal, E.D. Helms, D.N. Banerjee and Anoop Sharma, for the Appellant; D.K. Jain and D.P. Wadhwa, for the Respondent

Judgement

Goswamy, J.—At the instance of the assessee the following questions of law have been referred to this court for opinion by the income tax Appellate Tribunal u/s 66(1) of the Indian income tax Act, 1922: 1. Whether on the facts and in the circumstances of the case, the Tribunal is correct in holding that the amount of Rs. 47,30,892 was income taxable under the head "Business"? and

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the transaction in question amounted to an adventure in the nature of trade or that it produced business income within the meaning of section 2(6C) of the Act?

Assessment year in question is 1960-61, for which the previous year ended on September 30, 1959. The admitted facts are that Dalmia Jain Airways Ltd. was floated as a public limited company on July 9, 1946. The subscribed capital which was all paid up, amounted to Rs. 31½ crores in the form of 35 lakhs shares of the face value of Rs. 10 each. Another company in the name of Dalmia Jain Aviation Ltd. was incorporated as a public limited company on March 11, 1948. It was converted into a private Ltd. company on April 26, 1952. One of the shareholders of the Dalmia Jain Airways Ltd. filed a petition u/s 162 of the Indian

Companies Act, 1913, for the compulsory winding up of that company. However, after the petition was filed the company went into voluntary liquidation in pursuance of a special resolution passed on June 13, 1952. On November 16, 1952, five shareholders of Dalmia Jain Airways Ltd. wrote to the voluntary liquidator, that on negotiations carried on by them with Dalmia Jain Airways Ltd., the latter company had agreed to take over the entire existing assets and liabilities of Dalmia Jain Airways Ltd., provided the draft scheme, which was enclosed with the letter, was sanctioned by the court. On December 3, 1952, the voluntary liquidator filed Miscellaneous Case No. 941 of 1952 in the Court of the District Judge, Delhi, proposing a scheme of arrangement under sections 153 and 153A of the Indian Companies Act, 1913. A meeting of the members had been called to consider the scheme which was unanimously approved at the meeting. While approving the scheme the district judge stated in his order dated February 10, 1953, as follows: The main feature of the proposed scheme of arrangement as approved in the members' meeting was that the entire assets of the company be transferred to another Dalmia Jain Company called "M/s. Dalmia Jain Airways Ltd."; and that company agreed that the shareholders be given the option of receiving a sum of Rs. 5 per share of the face value of Rs. (10 immediately, or a sum of Rs. 6 per share within five years, or a sum of Rs. 10/4 per share within twelve years.

2. The scheme was later modified and under the modified scheme the proposal was to pay--

(1) Rs. 5/4 per share immediately to such shareholders who wished to avail of the option;

(2) in the alternative, Rs. 7 per share in five years; and

(3) in the alternative, Rs. 10/4 per share in ten years.

The district judge further stated in the order that to ensure the payment by M/s. Dalmia Jain Airways Ltd. to meet the obligation undertaken, Seth R. Dalmia, the assessee, had undertaken to guarantee the proposed payments with his own property and that, as required, a formal deed of guarantee executed by the assessee had been filed in court. The court held that the proposed arrangement was better than the ordinary winding-up and as such the scheme of arrangement was sanctioned.

3. By a subsequent order dated February 10, 1953, the district judge, Delhi, also ordered that the whole of the property of the transferor-company stood transferred to and vested in M/s. Dalmia Jain Airways Ltd; and all the liabilities of the transferor-company were, by virtue of the order, transferred to and became the liabilities of the said transferee-company. The voluntary liquidator was given liberty to apply to the court for subsequent orders on incidental, consequential and supplemental matters which were considered necessary to secure that the scheme was fully and effectively carried out. The relevant clauses of the scheme are clause 3,4,5, 6, 8 and 9, which are as under:

3. The transferee-company shall pay to the members of the transferor-company a sum Re. 1 per share of Rs. 10 each (fully paid up) within two weeks of the notice served by the members of the transferor-company on the transferee-company in the manner prescribed in para. 9 hereinafter.

4. The transferee-company shall, in addition to the payment described in the preceding paragraph, undertake to pay the following amounts to all the members of the transferor-company (except those specified in para. 6 hereinafter) in full and final settlement of all their rights and interests in the transferor-company as contributories:

(a) three yearly instalments of annas 0-12-0 each, first instalment being payable one year after the payment of Re. 1 per share as provided in paragraph 3 above.

(b) seven yearly instalments of Re. 1 each, first instalment being payable one year after the last instalment under (a) above.

The transferee-company shall issue deposit receipts or other suitable, documents in favour of each member or his nominee giving the total amount payable to them and the conditions attaching thereto as set out in the scheme,

5. Each member of the transferor-company in lieu of payment of Rs. 10-4-0 by instalments as described in paragraphs 3 and 4 above, may, in his discretion, agree to accept:

(a) a cash payment of Rs. 5-4-0 per share to be paid within two weeks of the said notice, or

(b) a sum of Rs. 7 to be paid in five yearly instalments of Re. 1 each, first being payable within six weeks of the said notice, and a final instalment of Rs. 2 on the expiry of the one year after the fifth instalment.

Any member who desires to avail of any of the aforesaid two options must give information to the transferee-company of his intention to do so by registered post within four weeks of the publication of the notice sanctioning the scheme as provided in para. 8 hereafter.

6. Fifteen lakhs shares of the transferor-company are held by certain persons or joint stock companies associated directly or indirectly with Seth R. Dalmia. The rights and interests of the contributories in respect of the said shares shall be adjusted, in full and final settlement as follows:

(a) Payment at the rate of Re. 1 per share in accordance with the terms of para. 3 above.

(b) Subject to the requisite consent of the Controller of Capital Issues and/or other appropriate authorities the transferee-company shall allot its fully paid-up ordinary shares of the face value of Rs. 60,00,000 to the members of the transferor-company or their nominees at the rate of two shares for every five shares held by them in the transferor-company.

In case the requisite sanction for the issue of the additional capital cannot be obtained in whole or in part, an amount equivalent to the face value of the share capital, not allowed to be issued, shall be payable to the respective member or their nominees on the expiry of six years from the date of the sanction of the scheme.

(8) The transferee-company shall publish the notice of the sanction of the scheme of arrangement by advertisement in the newspapers in accordance with the directions of the court.

(9) Each member in order to avail of his rights under this scheme, must give notice of his address and surrender his share scrips to the transferee-company within a period of six months from the date of publication of the notice referred to in para. 8 above.

5. Clause 10 of the scheme provided that Seth R. Dalmia, assessee, should guarantee the payment of all amounts due to the members under paras. 3, 4 and 5 of the scheme. Accordingly, a deed of guarantee was executed by the assessee on January 16, 1953.

6. The notice referred to in para. 8 of the scheme was published in the newspapers on February 20, 1953. According to para. 9 of the scheme, any member who wished to avail of his right under the scheme, had to give notice of his address and surrender his share scrips to the transferee-company within a period of six months from the date of publication of the notice, that is to say, before August 20, 1953. However, in the meantime, the name of the transferee-company was changed on July 25, 1953, to Asia Udyog (P.) Ltd. A few months thereafter, that is to say, on March 24, 1953, an agreement was entered into by the assessee with Asia Udyog Pvt. Ltd. The preamble to the agreement recited, inter alia, that the assessee at the request of the transferee-company, had given the guarantee to the members of Dalmia Jain Airways Ltd. and that it was also agreed among the transferee-company and the guarantor that after the expiry of five years from the date of the passing of the said scheme by the court, i.e., February 10, 1953, whatever amount shall remain to be paid to the members of the transferor-company in accordance with the terms of the said scheme, the transferee-company would transfer that liability to the guarantor within one year after the expiry of the aforesaid five years, at the convenience of the guarantor and pay the amount to him. On September 26, 1958, there was another agreement executed by the assessee and M/s. Asia Udyog Pvt. Ltd. One of the recitals in the preamble was that Asia Udyog Pvt. Ltd. has still a liability of little over Rs. 60,00,000 in respect of the payments to be made to the shareholders of the company in liquidation, in accordance with the scheme. Clauses 1 to 4 of the agreement read as under:

1. That the first party hereby agrees to transfer its liability for the payment to be made to the shareholders of the company in liquidation, in accordance with the scheme amounting to a little over Rs. 67,00,000 pursuant to the said scheme of

arrangement against a consideration of Rs. 67,00,000 (rupees sixty seven lakhs only).

2. That the second party hereby agrees to take over the aforesaid liability of a little over Rs. 67,00,000 of the first party for the payment to be made to the shareholders of the company in liquidation in accordance with the scheme against a consideration of Rs. 67,00,000.

3. That the aforesaid liability of the first party towards the payment to the shareholders of the company in liquidation, in accordance with the scheme shall stand transferred to the second party against a consideration of Rs. 67,00,000 (Rupees sixty-seven lakhs only).

4. That the first party shall stand absolved from all liabilities and responsibilities towards the shareholders of "the company in liquidation" in accordance with the scheme and the payment to the shareholders of "the company in liquidation" in accordance with the scheme shall be made by the second party subject to clauses 5 and 6 mentioned herein after.

7. Under clause 8 the agreement came into force w.e.f. October 1, 1958. By letter dated February 8, 1965, the ITO issued notice to the assessee u/s 23(3) requiring copies of the accounts of Dalmia Jain Airways Ltd. for the subsequent years till date. It was stated in the said notice:

The purpose is to find out what you have actually paid to the shareholders of Dalmia Jain Airways Ltd. which liability was taken over by you for a consideration of Rs. 67,00,000. Please explain with reference to the scheme sanctioned by the court how the shareholders' liability was determined at a little over Rs. 67,00,000. Since the whole scheme of transfer of shareholders' liability from Asia Udyog Pvt. Ltd. to you appears to be pre-planned with a view to make profits (vide your agreement dated March 24, 1958, with Asia Udyog Pvt. Ltd.). Please show cause why the difference between the actual liability in respect of the shareholders of Dalmia Jain Airways Ltd. and Rs. 67,00,000 should not be assessed as your income during this year.

8. On receipt of the aforesaid notice the assessee filed copies of Dalmia Jain Airways Ltd. shareholders' accounts for the years up to September 30, 1964, and also from October 1, 1964 to January 31, 1965, as required. The assessee also submitted a statement prepared by M/s. Asia Udyog Pvt. Ltd. showing how the shareholders' liability was determined by them on the date of transfer of the same to him. The statement filed by the assessee showed that on October 1, 1958, there were 4,72,549 shares unsurrendered and that the value of these shares were calculated at Rs. 10-4-0 per share which amounted to Rs. 48,43,625 against the face value of Rs. 47,25,490. The ITO was of the view that nothing was payable under the scheme in respect of the said unsurrendered shares because of the non-compliance with clause 9 of the scheme. The ITO was further of the view that the obligation to make payments against the shares had ceased in law and if the assessee accepted any claim in regard to any of them, it would

not be because of any enforceable obligation. The ITO calculated the value of the liability as on October 1, 1958, as worked out in the assessment order at Rs. 17,94,620 against which the assessee received payment of Rs. 67,00,000. Accordingly, the ITO held that the assessee had received a surplus of Rs. 49,05,380 which was his income from business.

9. Aggrieved by the assessment order, the assessee filed an appeal before the AAC. The AAC while agreeing with the findings of the ITO also concluded that the appellant had not taken over any real liability to the extent of over Rs.68,00,000 in consideration of Rs.67,00,000 received by him and that the assessee had derived a gain by a conscious and planned effort which was possible because of his close association with the companies in question and that gain had resulted to the assessee from an activity which was itself a business activity. The appeal was accordingly dismissed. The second appeal of the assessee before the Tribunal also met with the same fate. The Tribunal, however, held that the payments to be made by the assessee aggregated to Rs. 20,30,892 and, therefore, the net assessable business income was Rs. 47,30,892. The Tribunal also recorded the following findings:

Having regard to all the facts we are inclined to agree with the view of the Appellate Assistant Commissioner that the assessee availed of his position vis-a-vis Asia Udyog Pvt. Ltd. and the original guarantee to derive gain from out of so-called "liability" to the shareholders that, both the agreements were only by way of camouflage to conceal the real gain and that such gain resulted from an activity which by itself was a business activity.

10. The Tribunal also held that the bargain in any case amounts to an adventure in the nature of trade and as such was taxable income from business.

11. Mr. G. C. Sharma, the learned counsel for the assessee before us, contended that the Tribunal was wrong in holding that the income was a business income because the assessee was not engaged in the business of controlling companies. The argument overlooked the definition of "business " as given in section 2(4) of the Indian income tax. Act, 1922, which is inclusive and not exhaustive. The definition is, as follows:

2. (4)"Business" includes any trade, commerce or manufacture or any adventure or concern in the nature of trade, commerce or manufacture.

12. In G. Venkataswami Naidu and Co. Vs. The Commissioner of Income Tax, , the assessee firm which was acting as managing agents purchased for a total consideration of Rs. 8,713 four contiguous plots of land adjacent to the place where the mills of the company managed by it were situated.

13. The four purchases were made on different dates. The assessee-company made no efforts to cultivate the said land or erect any superstructure on them but allowed them to remain unutilised except for the rent received from the house which existed on one of the plots. The assessee sold those lands to the

managed company and the question arose whether the sum of Rs. 43,887, being the excess realised by the assessee on the two sales over its purchase price, was assessable to income tax. The Appellate Tribunal rejected the contentions of the assessee that the properties were bought as an investment and that the plots were acquired for building tenements for the labourers of the mills as well as the alternative contention that the managed company desired to purchase the plots on account of an award of an industrial tribunal recommending that the company should provide tenements for its labourers, and held that since the appellant was in a position to influence the decision of the managed company to purchase the properties, the plots were purchased by the assessee wholly and solely with the idea of selling them at a profit to the company. The Tribunal, therefore, came to the conclusion that the amount was not a capital accretion but was a gain made by an adventure in the nature of business and was, therefore, taxable. The High Court also agreed with the Tribunal and held that the transaction was an adventure in the nature of trade and that the department was justified in taxing the amount. On appeal to the Supreme Court it was held that the Appellate Tribunal was right in inferring that the appellant knew that it would be able to sell the lands to the managed company whenever it thought it profitable so to do. It was further held that the assessee had purchased the four plots of land with the sole intention of selling them to the mills at a profit, which intention raised a strong presumption in favour of the view taken by the Tribunal and in this situation the High Court was right in holding that the transaction in question was an adventure in the nature of trade. The facts in the present case are more or less identical to the facts in the case of *G. Venkataswami Naidu and Co. Vs. The Commissioner of Income Tax*, . In the present case, the findings of the Tribunal, which are findings of fact, are that the assessee availed of his position vis-a-vis Asia Udyog Pvt. Ltd. and the original guarantee to derive a gain from out of the so-called "liability" to the shareholders, that both the agreements were only by way of a camouflage to conceal the real gain and that such gain resulted from an activity which by itself was a business activity. At no stage it was disputed by the assessee that he was controlling both the companies and the nature of the transaction clearly goes to show that it was well organised and pre-planned with a view to make a profit. There is no doubt in our minds that the whole affair was pre-planned with a view to make a profit and this the assessee could do, because, admittedly, he was controlling the companies. The activity of controlling the companies in such a way as to earn profits certainly fell within "business, profession or vocation".

14. The next contention of the learned counsel for the petitioner was that the transaction could not be said to be an adventure in the nature of trade because it was not connected with the trade of the assessee and was an isolated transaction. He contended that the receipt should have been taken as casual and non-recurring. When section 2(4) of the Indian income tax. Act, 1922, refers to an adventure in the nature of trade, it clearly suggests that the transaction in question cannot properly be regarded as a trade or business. It is allied to

transactions that constitute trade or business but may not be a trade or business by itself. It is characterised by some of the essential features that make up a trade or business, but not by all of them, and so even an isolated transaction can satisfy the description of an adventure in the nature of trade provided at least some of the essential features of the trade are present in the isolated or single transaction. To determine the nature of the transaction the dominant intention of the assessee has to be seen. If the intention is to embark on a venture in the nature of trade as distinguished from a capital investment it would make no difference even if the transaction is a single and isolated one. In the case of *Dalmia Cement Ltd. Vs. Commissioner of Income Tax, New Delhi*, the appellant which owned some cement factories in various parts of India placed an order in 1946 with M/s. Smidth & Co. of Copenhagen for the supply of four cement plants at four places including Dandot and the order was confirmed on August 6, 1947. The supply of the plant intended for Dandot was to commence in February, 1948. In the meantime, India was partitioned and Dandot fell in the territory of Pakistan. The appellant did not cancel the order but carried on negotiations with the Orissa Govt. in 1947 and 1948 for the installation of the cement factory in Orissa. The negotiations proved fruitful and the appellant obtained an import licence and wrote to M/s. Smidth & Co. informing them that the plant meant for Dandot should be diverted to Orissa. When the machinery arrived the appellant transferred it to Orissa Cement Ltd. and debited its actual cost to that company. Thereafter, in April 1950, the assessee asked for revaluation of the price owing to the rise in prices after the machinery was ordered and the matter was referred to an expert who reported that the Orissa Cement Ltd. had benefited to the extent of Rs. 21,00,000. A further sum of Rs. 7,00,000 being allowed by the Orissa Govt., the Orissa Cement Ltd. allotted to the appellant fully paid up shares of the value of Rs. 7,00,000. The Appellate Tribunal and, on a reference, the High Court held that the sum of Rs. 7,00,000 was received pursuant to an adventure in the nature of trade and as such was taxable as the appellant's income under the Indian income tax. Act, 1922. On appeal to the Supreme Court, it was held that the intention of re-sale was there almost from the beginning and was really the dominant intention in importing the machinery after the partition of the country. The transaction was, therefore, by way of an adventure in the nature of trade and was as such a business transaction within the meaning of section 2(4) of the Act. It did not matter that the appellant did not earn a profit immediately on delivering the machinery and sold it without any profit in the first instance, because even if the appellant had not earned any profit whatsoever at the time of sale or even thereafter, the transaction would none the less have been an adventure in the nature of trade. In *Kanwarlal Manoharwal Vs. Commissioner of Income Tax*, the assessee, a pawn-broker, obtained an assignment of a decree for Rs. 8,000 for a consideration of Rs. 4,000. Thereafter he purchased the house property from the judgment-debtor for a consideration of Rs. 21,500 and adjusted the sum of Rs. 8,000 due under the decree in part payment of the consideration for the sale. The ITO assessed the profit of Rs. 4,000 made by the assessee in the transaction relating to the assignment of the decree as business

profit. This was confirmed by the AAC and the Tribunal. On a reference to the High Court of Madras, the High Court held that the absence of any prior or subsequent dealings of any purchase of decree by the assessee had no significance because, even a first venture could be an adventure in the nature of trade. In *Surangmali Punamchand Surana Vs. Commissioner of Income Tax, Assam, Tripura, Manipur*, the assessee which carried on business in potatoes, oilcakes, etc., and commission agency business, had borrowed large amounts from a bank on an overdraft account. When in May, 1948, the bank suspended operation and applied for a scheme of arrangement the amount outstanding on this account was Rs. 35,912. The assessee obtained a concession from the bank whereunder it paid in cash Rs. 5,000 and purchased from several persons, who held deposits with the bank, their fixed and other deposits, tendered them to the bank and obtained an adjustment for Rs. 23,866. As, however, the assessee had paid only Rs. 5,677 to purchase these deposits, the ITO assessed the difference of Rs. 16,995 as business profit. The Assam High Court held that the purchase of the deposits with a view to derive the full benefit of the sums which the depositors held in the bank and deriving that benefit from the bank by adjustment amounted to "business" and the profit derived therefrom came within the scope of "profits or gains of business" within the meaning of section 10 of the income tax. Act; and being a receipt from business it was not a casual or non-recurring receipt within the meaning of section 4(3)(vii).

15. From the facts in the present case, the Tribunal recorded the findings of fact which are that the assessee was in a position to have a fair idea of the liability of the shareholders pursuant to the scheme approved by the court. There was a large number of shareholders of the Dalmia Jain Airways Ltd. from the regions which went over to Pakistan. The assessee, therefore, knew in 1953 that these shareholders would not be coming forward to claim any compensation under the scheme. The assessee, therefore, conceived the idea of taking advantage of his position vis-a-vis Asia Udyog (P.) Ltd. and the guarantee given by him. Again it is significant that neither of the two agreements which had earlier approved the scheme and which was really safeguarding the interests of the shareholders was brought to the notice of the district judge. In fact, neither the court's order nor the scheme as approved by the shareholders, contemplated any transfer of liability from Dalmia Jain Airways Ltd., to any other person, much less to the guarantor. Moreover, it is clear from the chart of the liabilities that as on October 1, 1958, there were 4,72,549 shares which had not till that date been surrendered and that the liability in respect of them was calculated on the basis of Rs. 10-4-0 per share at Rs. 48,43,627 and the calculation was not made at Rs. 5 per share. The assessee produced before the authorities a statement showing that the payments had been made by him for the period October 1, 1958. The authorities came to the conclusion that the said payments made did not exceed even the interest payable at Rs. 67,00,000 in any one year at the usual rate of interest. In view of these findings, the irresistible conclusion is that the dominant intention of the assessee was to embark on a venture in the nature of trade and

the gain resulting therefrom was as a result of an activity, which itself was a business activity. For the reasons recorded above, we will answer both the questions referred to us in the affirmative, i.e., in favour of the department and against the assessee. The assessee will pay costs. Counsel's fee Rs. 500.