

(1968) 11 MAD CK 0059

In the Madras High Court

Case No : Tax Case No. 91 of 1965 (Reference No. 30 of 1965)

R. Subba Naidu

APPELLANT

Vs

Commissioner of Gift Tax

RESPONDENT

Date of Decision : 21-11-1968

Acts Referred:

Citation : (1969) 39 CompCas 766 : (1970) ILR (Mad) 629 : (1969) 73 ITR 794

Hon'ble Judges : Veeraswami, J; Ramaprasada Rao, J

Bench : Division Bench

Advocate : T. Raghavan, for the Appellant; V. Balasubrahmanyam and Jayaraman, for the Respondent

Judgement

Veeraswami, J.—The substantial problem in the reference initiated by the assessee and relating to the assessment year 1959-60 is whether the inclusion of Rs. 38,880 for gift-tax is proper. That represented the total value of 208 "B" shares and 8 "A" shares held by the assessee in Udumalpet Palani Andavar Mills Limited. They stood registered in the books of the company right through in the name of the assessee. He was in receipt of the dividends referable to the shares, which he included in his income chargeable to tax. But the value of the shares was added to his return for purposes of gift-tax on the footing that he had by two settlement deeds dated respectively April 11, 1951 and March 31, 1959, made a gift of them absolutely to his daughter. She died on June 24, 1960 ; but the shares were not treated as part of her estate for estate duty. His case, which was not accepted by the Gift-tax Officer and the Tribunal, was that there was no actual transfer of the shares to his daughter. He maintained that by the first settlement deed he retained in himself a life interest in the first lot of shares, the remainder therein being vested absolutely in his daughter, that he had not handed over the certificates to his daughter, though the whole lot of shares was settled on her absolutely by the terms of the second settlement deed, and that neither a transfer deed was executed in favour of the daughter in relation to the shares nor a request was made to the company to transfer the shares to her

name, but that, on the other hand, his name continued in the share register of the company as the holder of the shares and he also continued to receive the dividends from the shares and treat and include the same as income chargeable to tax at his hands.

2. The Appellate Assistant Commissioner in deleting the addition was persuaded to the view that short of mutation of the register in favour of the daughter and because of the continuance of the assessee's name as the shareholder and his perception of the dividends, there was no transfer of the shares. The Tribunal disagreed with that view and held that the assessee having done everything in his power to divest himself of his title to the shares, there was a completed gift thereof to his daughter. A subsidiary point raised by the assessee but rejected by the Tribunal was that, in any case, the gift comprised but the vested remainder in the shares and not the assessee's life interest therein. A further fact to be noticed in this connection is that 8 "A" ordinary shares were not the subject-matter of a gift in favour of the daughter under the first settlement deed. The second settlement deed shows that the assessee's daughter surrendered whatever interest she had under the earlier settlement so that the assessee, jointly with his wife, could make a revised scheme of disposition of his properties and under the terms of the later document executed by the consent of all concerned including the assessee's daughter, the shares were given absolutely to her. The document also said that the settlor was to be in possession of whatever was settled under the document in her favour.

3. The actual reference is of two questions :

" 1. Whether there was any taxable gift of the 208 " B " shares and 8 " A " shares in Palani Andavar Mills for the assessment year 1959-60 ?

2. Whether, in any event, the value of the property gifted should not be restricted to the life interest of the donor in the said shares as on March 31, 1959?"

4. We are of opinion that the Tribunal was right in the view it took, namely, that the inclusion for purposes of gift-tax of the total value of the shares as on March 31, 1959, was correct. That means the questions under reference should be answered in favour of the revenue. The whole question turns on whether under either or both of the settlement deeds, there was a transfer of the shares by the assessee, who was the holder thereof to his daughter. Gift-tax, by Section 3 of the Gift-tax Act, 1958, is payable in respect of a gift made by a person during the previous year at the rate or rates specified in the Schedule to the Act. " Gift " means the transfer by one person to another of any existing movable or immovable property made voluntarily and without consideration in money or money's worth, and includes the transfer of any property deemed to be a gift u/s 4. The definition includes certain deemed gifts with which we are not concerned in the present context. " Transfer of property " has also been defined to mean any disposition, and, among other things, assignment, settlement or other

alienation of property, and the expression includes the creation of a trust in property or the creation of an interest in property. A transaction entered into with the intent thereby to diminish directly or indirectly the value of one's own property and to increase the value of the properties of any other person is also within the scope of the expression. "Property" includes any interest in property, movable or immovable. But for the interaction of the provisions of the Companies Act, which we shall presently advert to, the question of transfer of the shares to the daughter as a gift presents no difficulty. Factually, the second deed of settlement is explicit that a gift of the shares was made absolutely by its maker to his daughter. No doubt a life interest had been reserved in the assessee by the earlier document, but this need not detain us because in our view all the parties concerned consented to the execution of the second settlement deed with a recital that the daughter had surrendered whatever interest she had under the earlier settlement deed in favour of the assessee so that he might make a revised disposition. By Section 123 of the Transfer of Property Act, for the purpose of making a gift of movable property, the transfer may be effected either by a registered instrument signed by or on behalf of the donor and attested by at least two witnesses or by delivery. The second settlement deed complied with these requisites and, further, the assessee's daughter was a signatory thereto in token of her acceptance of the gift made thereunder in her favour. We have already noticed that the recital in the document specifically referred to possession of the properties gifted to the daughter having been handed to her though it would appear the physical custody of the shares continued to be with him. If the matter stood there, undoubtedly there was a valid transfer of the shares to the daughter which constituted a gift thereof to her.

5. But the contention for the assessee is that, in the absence of registration of the shares in the books of the company in the name of the daughter, there was no valid transfer and the assessee continued to be their owner ; in other words, there was no completed transfer of the shares to his daughter. In support of the contention we are referred to Section 82 of the Companies Act as well as *Société Générale de Paris v. Walker* , *Milroy v. Lord*. and *Howrah Trading Co. Ltd. v. Commissioner of Income Tax*. We accept the proposition that when joint stock is the subject matter of transfer, the provisions of the Transfer of Property Act are not conclusive and we should see whether there is a transfer in accordance with the provisions of the Companies Act. Section 82 treats shares as movable property transferable in the manner provided by the articles of the company. The articles of the *Udumalpet Palani Andavar Mills Ltd.* have not been exhibited as part of the record before us, but all the same, we have looked into them and find that they more or less conform to the regulations relating to transfer of shares contained in Table A in Schedule I to the Companies Act. Regulation 20 contains the form and regulation 19(2) says that the transferor shall be deemed to remain a holder of the share until the name of the transferee is entered in the register of members in respect thereof, Section 108(1) is to the effect that a company shall not effect a transfer of shares in or debentures of the company unless a proper

instrument of transfer duly stamped and executed by or on behalf of the transferor and by or on behalf of the transferee and specifying the name, address and occupation, if any, of the transferee has been delivered to the company along with the certificate relating to the shares or if no such certificate is in existence along with the letter of allotment of the shares. The first proviso to this provision refers to a case where the instrument of transfer has been lost. An application for registration of a transfer of shares may be made u/s 110(1) either by the transferor or by the transferee. Under regulation 19(1), the instrument of transfer of any share in the company shall be executed by or on behalf of both the transferor and transferee. Regulation 21 gives discretion to the board of directors, subject to the right of appeal conferred by Section 111, to decline to register in certain circumstances. The effect of these provisions appears to be this. There should first be a transfer properly made of shares which should then be presented along with the share certificates to the board of directors either by the transferor or transferee for change of registration in respect of them and, until such a change is effected in the books of the company, the transferor will continue to be the holder of the shares. The transfer of the interest in the shares from the transferor to the transferee appears, therefore, to be independent of the requirement of its registration for purposes of the Companies Act. Without an anterior transfer there can be no question of applying for registration of it. It is necessary to keep in view these two aspects separately, as, otherwise, the process of arriving at a correct view as to the effect of a transfer of shares as between the transferor and the transferee is apt to be clouded.

6. As between the transferor and the transferee, all that is required to effect a transfer of the shares is that both should combine in the execution of a transfer in the appropriate form and if such a transfer is not to be registered, no delivery of the shares may be required, but if it is to be registered, the transfer will have to be accompanied by delivery of the shares to the transferee. The transferor should have done everything that he can possibly do with a view to divest himself of all his interest in the shares. If that is done, we fail to see why the transfer is not a valid transfer and as complete as it could be as between the transferor and the transferee, except of course for purposes of the Companies Act. So far as the company is concerned, until registration of the transfer, the transferor continues to be the holder of the shares, particularly when the provisions of the Companies Act do not, broadly speaking, recognise any trusts in respect of shares. Inherent in this position is that while, as between the transferor and, the transferee, the latter acquires a complete interest under the transfer, the transferor appears to hold, from the standpoint of the company, the legal title to the shares, not as owner but as a trustee, and at the same time he is the holder of the shares for purposes of the company affairs under the provisions of the Companies Act and until the transfer is duly registered. Courts have sometimes described the interest acquired by the transferee as beneficial ownership as distinguished from legal ownership of the shares, but it seems to

us that, in practical application, the distinction may not be of much consequence unless equities, as between the claimants, are in conflict.

7. We do not think that any of the cases cited for the assessee runs counter to what we have said or establishes that, in the absence of registration, there is no transfer of any interest at all in the shares to the transferee. *Society Generals De Paris v. Walker* related to a contest between competing transferees. Under the first transfer, the certificates of shares along with a blank transfer were deposited with the transferee as security for a debt. Later, the holder fraudulently executed a blank transfer in respect of the shares and deposited it with the appellants before the House of Lords. They filled up the blanks and presented the transfer form to the company for registration of the transfer. By the articles of association, shares could be transferred only by a deed; lost certificates might be renewed upon satisfactory proof of the loss or, in default of proof, upon a satisfactory indemnity being given. The certificates bore an endorsement that no transfer of any portion of the shares represented by the certificates would be registered until the certificate had been delivered at the company's office. The company having refused to register the transfer in favour of the appellants, they sued for a declaration of their title to the shares as against the first transferee. The House of Lords held, all the law lords concurring in the opinion, that the title of the appellants to the shares was inchoate and they could not therefore succeed. The transfer was considered to be inchoate because the transfer form, which was in blank, was filled up by the appellants themselves and its presentation for registration was not also accompanied by the certificates which had been deposited with the earlier transferee. The equities arising between the two transferees, so to speak, were further looked at this way by the House of Lords:

" The respondents not only had the certificates, but they had the company's undertaking under seal that there should be no change of the registered title unless those certificates were produced. What more could be necessary, on any reasonable or intelligible principle, to " perfect" their equitable title, which they were under no obligation to convert into a legal title by registration ? "

8. This is no authority for the proposition that, in the absence of registration, the purported transfer of shares in the proper form would fail as a transfer.

9. Much stress has been placed by the assessee on *Milroy v. Lord* , which is a well-known case. But that again does not help him to establish that as between the transferor and transferee there can be no transfer of ownership without registration thereof, whatever may be the position of the transfer vis-a-vis the company. That was a case in which the transfer document itself was defective in certain particulars and the observations of the learned judges should have to be understood in that context. The finding was that there was no transfer at all in favour of the claimant and the legal title to the shares, therefore, never vested in him. The court, therefore, said that in such circumstances there was no equity which required to protect the imperfect gift.

10. Howrah Trading Co. Ltd. v. Commissioner of Income Tax was not concerned with the precise point which we are called upon to decide in this reference and what was held was only that a person who had purchased shares in a company under a blank transfer and in whose name the shares have not been registered in the books of the company, was not a shareholder in respect of such shares within the meaning of Section 18(5) of the Income Tax Act, notwithstanding his equitable right to the dividend on such shares and was not, therefore, entitled to have this dividend grossed up u/s 16(2). In the course of its judgment, the Supreme Court referred to Nanney v. Morgan and quoted from it with approval the following passage:

" " Therefore the transferor, until the delivery of the deed of transfer to the secretary, is subject to all the liabilities and entitled to all the rights which belong to a shareholder or stockholder, and, in my opinion, until the requisite formalities are complied with, he continues to be the legal proprietor of the stock or shares subject to that proprietorship being divested, which it may be at any moment, by a compliance with the requisite formalities." "

11. While stating that the same position obtains in India, the Supreme Court proceeded to observe :

" During the period that the transfer exists between the transferor and the transferee without emerging as a binding document upon the company, equities exist between them, but not between the transferee and the company. The transferee can call upon the transferor to attend the meeting, vote according to his directions, sign documents in relation to the issuance of fresh capital, call for emergent meetings and, inter alia, also compel the transferor to pay such dividend as he may have received. See E.D. Sasoon & Co. Ltd. v. Patch approved in Mathalone v. Bombay Life Assurance Co. Ltd. But these rights though they, no doubt, clothe the transferee with an equitable ownership, are not sufficient to make the transferee a full owner, since the legal interest vis-a-vis the company still outstands in the transferor; so much so, that the company credits the dividends only to the transferor and also calls upon him to make payment of any unpaid capital, which may be needed."

12. It may be seen that these observations related to the legal position as between the transferor and the company in relation to the former's transfer of shares which have not been registered in the books of the company in the name of the transferee.

13. We are of the view that Rose, In re: Rose v. Inland Revenue Commissioners lays down the true principles as to the legal effect of a transfer of shares as between the transferor and the transferee thereof. That was a case decided by the English Court of Appeal and related to estate duty. By a deed dated March 30, 1943, the deceased out of love and affection transferred to his wife, who was the plaintiff, 10,000 shares in an unlimited company. He had also made a further transfer of 10,000 shares in the same company to the plaintiffs in the second

action there as trustees to hold upon the trusts of a settlement of even date. It was common ground that the transfers were made in the form required by the company's articles of association, which authorised the directors to decline to register any transfer if they thought fit. On the same dates, the transferees were put in possession of the relative share certificates. The transfers were stamped subsequently on April 12, 1943, and were only registered in the books of the company on June 30, 1943. In the meantime the deceased had died on February 16, 1947. The Crown claimed estate duty on the shares on the ground that the gift of the shares was not completed before April 10, 1943, and that was the point the Court of Appeal had to decide. It held that the deceased having done everything in his power by executing the transfers to transfer his legal and beneficial interests in the shares to the transferees, they had become beneficial owners of the shares and between the dates of execution of the transfers and the registration of the transfers, the deceased could not have asserted any beneficial rights as registered holder. It was further held that the gifts of shares were completed on March 30, 1943, and on that date bona fide possession and enjoyment of the shares had been assumed by the transferees to the entire exclusion of the deceased or of any benefit to him by contract or otherwise. The Court of Appeal clearly rejected the Crown's contention that until registration on June 30, 1943, of the transfer of shares there had been no completed gift as on April 12, 1943. On the view that there had been a completed gift on that date, the Crown failed. Evershed M.R. noticed the argument of the Crown :

" The Crown says that until the transfers were registered in the books of the Leweston Estates Company on June 30, 1943, either there was no effective transfer of the shares to the donee or, alternatively, there was not until that date an entire exclusion of the donor from all benefit in respect of the shares."

14. We are not concerned in this case with the second aspect of the matter. The Master of the Rolls dealt with the first part of the Crown's argument thus:

" The form which followed was that which the deceased adopted. On its execution the deed of transfer was, beyond question, delivered to the transferee, together with the certificate relative to those shares. It follows, therefore, that so far as lay in his power, the deceased did all that he could--he followed carefully and precisely the obligations imposed on a proposing transferor by the article--to divest himself then and there in favour of his wife of all his interest, legal and equitable, in the 10,000 shares.

Approaching the matter then as one of common sense, or one from which the application of common sense is not excluded, and having regard to the terrors of the transfer I should have thought it was exceedingly difficult to contend successfully that on the date of the transfer, March 30, 1943, the deceased did not, within the terms of Section 38(2)(a) of the Act of 1881 make and Mrs. Rose did not take under a voluntary disposition purporting to operate as an immediate gift. That is not conclusive, for there still remains, on any view, the question whether, during the period up to June 30, 1943, the transferor did not, by virtue

of the peculiar characteristics attaching to shares in companies, and particularly in this company, retain an interest which interest did not cease until June 30, a date too late for the plaintiffs."

15. On the last aspect the Master of the Rolls further observed:

" So that vis-a-vis the company, this document did not, and could not, operate to transfer to Mrs. Rose the right against the company to claim and receive that dividend."

16. The rest of the discussion in the judgment of Evershed M. R. shows that the matter should be looked at as we outlined at the outset, in two independent facets, one the effect of the transfer as a valid completed gift of the shares as between the transferor and the transferee, and the other its effect vis-a-vis the company, and the learned judge held the view that, as between the parties to the transfer, it operated as a complete and immediate gift. He also noticed *Milroy v. Lord* but distinguished it by pointing out:

" It is plain that the basis on which they so decided was that this purported gift was incomplete or imperfect in this sense, that the donor had not done all that lay in his power to do in accordance with the terms on which the shares were held by him to make his gift effective and to divest himself of his beneficial and other interests in the shares. "

17. With reference to the other cases noticed, it was pointed out that they all turned on the fact that the deceased donor had not done all in his power according to the nature of the property given, to vest the legal interest in the property in the donee. The following observations of Evershed M. R. are even more positive on the point:

" then it seems to me that it cannot be asserted on the authority of *Milroy v. Lord* and I venture to think it also cannot be asserted as a matter of logic and good sense or principle, that because, by the regulations of the company, there had to be a gap before Mrs. Rose could, as between herself and the company, claim the rights which the shares gave her vis-a-vis the company, the deceased was not in the meantime a trustee for her of all his rights and benefits under the shares. That he intended to pass all those rights, as I have said, seems to me too plain for argument."

18. Jenkins L.J., concurring with Evershed M.R., stated :

"In my view, the directors of the company, when they registered the transfers, registered them because, by virtue of the transfers, the transferees had become owners of the shares, and as such had become entitled to get in the legal estate by being put on the register in respect of the shares. I adhere to the view I have already expressed, that these transfers were nothing more nor less than transfers of the whole of the deceased's title, both legal and equitable, in the shares, and all the advantages attached to the shares, as from the date on which he executed and delivered the transfers--subject, of course, as regards the legal

title, to the provisions of the articles of association of the company as to registration, and to the directors' discretionary power to refuse registration.

19. The same learned judge considered what was the position as to the effect of transfers before the registration and observed:

" The answer can only be, in my view, that he (transferor) had no beneficial interest left whatever : his only remaining interest consisted in the fact that his name still stood on the register as holder of the shares ; but having parted in fact with the whole of his beneficial interest, he could not, in my view, assert any beneficial title by virtue of his position as registered holder. In other words, in my view the effect of these transactions, having regard to the form and the operation of the transfers, the nature of the property transferred, and the necessity for registration in order to perfect the legal title, coupled with the discretionary power on the part of the directors to withhold registration, must be that, pending registration, the deceased was in the position of a trustee of the legal title in the shares for the transferees."

20. On the footing that the transferee had beneficial ownership, there was this further significant remarks :

" After all, where duty is concerned, the only relevant type of ownership is beneficial ownership, and the situation of the legal estate does not affect the question."

21. We have taken the liberty of extracting extensively from Rose, In re: Rose v. Inland Revenue Commissioners , the only excuse being that it seems to provide a complete answer to the reference against the assessee.

22. The registered settlement deed of March 31, 1959, substantially complied with the requisites of the form of transfer prescribed by the articles of association of the company or the regulations in the Companies Act. It may be that the physical custody of the shares, as observed earlier, continued with the assessee. But its effect will have to be assessed in the light of the recital in the settlement deed that possession of the property settled on the daughter had been handed over to her. If the assessee received the dividends, it was because he continued to be the registered holder of the shares. If he chose to include the dividends in his income chargeable to tax, that made no difference and it could not affect the rights of the transferee under the settlement deed. Nor the fact that the shares were not included for purposes of estate duty on the death of the daughter affected her legal rights under the transfer. In our opinion, there was a completed gift of the shares to the daughter of the assessee and it operated with full force as between him and his daughter, notwithstanding that, vis-a-vis the company, he continued to be the holder of the shares in the absence of registration of the transfer.

23. There remains the question whether what passed under the second settlement deed was only a life interest of the assessee in the shares. This

aspect we have already dealt with. In our opinion, the first settlement deed, in so far as it retained in the assessee a life interest in the shares, cannot be regarded as being in the form requisite for a valid transfer of shares. Secondly, we think, by consent of all the parties, the second document was executed, the assessee's daughter having surrendered whatever interest she had in the shares under the first document. In the circumstances, therefore, the transfer under the 1959 settlement deed was of the entire interest in the shares to the assessee's daughter.

24. We answer both the questions under reference against the assessee with costs. Counsel's fee, Rs. 250.