

(2014) 02 GUJ CK 0002

In the Gujarat High Court

Case No : Special Civil Application No. 18008 of 2005

Suresh Narain Bhatnagar

APPELLANT

Vs

Income Tax Officer

RESPONDENT

Date of Decision : 19-02-2014

Acts Referred:

Companies Act, 1956 — Section 43A
Constitution of India, 1950 — Article 265
Income Tax Act, 1961 — Section 144, 179, 179(1)

Citation : (2014) 367 ITR 254

Hon'ble Judges : Sonia Gokani, J; Akil Abdul Hamid Kureshi, J

Bench : Division Bench

Advocate : Manish J. Shah, Advocate for the Appellant; K.M. Parikh, Advocate for the Respondent

Judgement

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Akil Abdul Hamid Kureshi, J.—The petitioner had challenged an order dated January 3, 2005, passed by the Income-tax Officer under section 179 of the Income-tax Act, 1961 ("the said Act" for short).

Brief facts are as under:

1.1 The petitioner was a director of one M/s. Sirs Engineering P. Ltd. ("the company" for short). For the assessment year 2000-01, the Assessing Officer passed order of assessment on March 28, 2003, raising tax demand of Rs. 40,99,967. With penalty, it came to Rs. 41,09,967. Five more separate orders of assessment dated February 27, 2004, were also passed in the case of the same company for the assessment years 1996-97 to 1999-2000 and 2001-02 raising different tax demands.

1.2 On March 22, 2004, the Income-tax Officer issued a notice to the petitioner indicating that a tax demand of the said company of Rs. 41,11,967 for the assessment year 2000-01 was still outstanding. He was the director of the

company during the relevant period. He was asked to show cause why he should not be held personally liable for such recovery under section 179 of the said Act.

1.3 The petitioner filed several replies to the said notice. In his first reply dated March 30, 2004, he conveyed that records of the company were lost; that he himself was suffering from heart problem. During the assessment year 2002-03, he was totally immobile and was not able to attend any of the meetings or day-to-day business of the company. He was, therefore, not responsible for negligence, misfeasance or breach of duty in connection with the affairs of the company. Yet another reply came to be filed on September 28, 2004, in which he contended that he was only supplying technical support to the company. He was rendering such service for various other companies. He was never engaged in the day-to-day business of the company. In yet another reply dated October 13, 2004, he contended that he had already resigned from the company on February 25, 1996. He also contended that by virtue of section 43A of the Companies Act, 1956, since the company's turnover had crossed the threshold limit, the company would be a deemed public company. In his further reply dated October 26, 2004, he reiterated this aspect and stated thus:

"Further, by the virtue of the provisions of section 43A of the Company's Act Sirs Engineering Pvt. Ltd. has become a public company by crossing the turnover criterion and the same has also been certified by the assessment order passed for the assessment year 1996-97."

1.4 In his further reply which is produced at annexure L, he elaborated the question of company having become a deemed public company and contended as under:

"(c) I am advised by my chartered accountant that this company falls in the category of deemed public limited in view of its turnover being more than Rs. 1 crore as estimated by the Department under section 144 of the Income-tax Act, therefore, the section relating to personal liability of the director does not arise in this case if the assessment of income is correct by the Department. This issue has been raised by me in my first submission itself. A copy of the said section 43A of the companies Act is attached herewith."

1.5 In his last reply dated January 1, 2005, he once again asserted that:

"5. Further, it has also brought to the notice of the learned Income-tax Officer that under section 43A of the Companies Act states that where one of the shareholders of the company is a body corporate holding more than 25 per cent, of its paid-up capital it should be treated as public limited company. I have also provided the copy of the annual return for the financial year 1994-95 along with the copy of the shareholders register, which I could found from the factory premises of the company after so many efforts. They are provided along with the letter dated December 30, 2004, which is also enclosed herewith."

2. The Assessing Officer passed his impugned order dated January 3, 2005.

Regarding the petitioner's resignation, he observed that he had signed and verified the return of the income of the company for the assessment year 2001-02 on March 23, 2003. He had also filed appeals before the Commissioner (Appeals) for the assessment year 1996-97 to 2001-02 which prove that he continued to be the director of the company even after the submission of his resignation.

2.1 With respect to his involvement in the company, the Income-tax Officer held that he failed to prove that non-recovery of tax cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company. His contention that he was only a technical director was negated observing that section 179 includes every person who is a director of a private company and the onus is on such director to prove non-negligence, non-misfeasance or non-breach of duty on his part. In the present case, the petitioner failed to produce any evidence to prove such facts.

2.2 With respect to the status of the company being a deemed public company, the Assessing Officer observed as under:

"Another argument raised by him is M/s. Sirs Engg. Pvt. Ltd. is a deemed public company under section 43A of the Companies Act, 1956, in view of its turnover being more than Rs. 1 crore as estimated by the Department in the assessment order. Section 179 specifically overrides the provisions of the Companies Act, 1956. Section 179 deals with only private limited companies. Hence, this contention is not tenable."

3. Having heard learned counsel for the parties and having perused the documents on record, the following facts emerge:

(1) Notice under section 179(1) of the Act was issued only for recovery of tax due pertaining to assessment year 2000-01.

(2) Without any further notice, the final order under section 179 was passed for recovery of dues of the company for all the years from 1996-97 to 2001-02.

4. The recovery demand, therefore, for the assessment years 1996-97 to 1999-2000 and 2001-02 must fail on two counts. Firstly, there was no notice for recovery of such amounts. More importantly, the only notice of show cause which was issued was dated March 22, 2004. The assessment orders of the said assessment years were passed on February 27, 2004. Thus, within less than a month of passing of the assessment orders, the notice came to be issued. The first requirement of application of section 179 is that any tax due from a private company cannot be recovered from such company. When obviously thus the Assessing Officer had and could not have made any efforts for recovery of such tax dues, the question of inquiring with the petitioner as a director of the company to pay up the same amount or else be held liable under section 179 of the Act would not arise. In the case of Bhagwandas J. Patel Vs. Deputy Commissioner of Income Tax, , the court had held that before recovery in respect

of dues from the private company can be initiated against the directors, it is necessary for the Revenue to establish that such recovery cannot be made against the company and then alone it can reach the directors who were responsible for the conduct of the business during the previous year in relation to which liability existed.

5. Our inquiry, therefore, regarding the impugned order of the Assessing Officer would be confined to the demands for the assessment years 2000-01. In this context, we are unable to hold that the petitioner having already resigned from the position of a director in the year 1996, could no longer be held responsible under section 179 of the Act. The undisputed facts which have come on record are that in the year 2003, the petitioner signed the returned of the company as its director. In the year 2004, the petitioner filed appeals against the orders of assessment passed by the Assessing Officer for the assessment year 1995-96 and onwards. Thus, even if we believe that the petitioner had tendered his resignation as a director, he continued to act as one. Neither the company nor the petitioner acted on such resignation.

6. The crucial question, however, is of the status of the company. As noted, the petitioner time and again contended before the Assessing Officer that the company had ceased to be a private company by virtue of provisions of section 43A of the Companies Act the company having crossed the maximum threshold turnover limit and also by virtue of 25 per cent, of its share capital being held by another company, had become a deemed public company. It was open for the Assessing Officer to inquire into these aspects. The question raised by the petitioner was a mixed question of fact and law. If the facts as asserted by the petitioner were established, the legal implications flowing thereof must follow. The Assessing Officer, however, brushed aside this contention and held that whatever be the status of the company for the purpose of the Companies Act, section 179 of the Income-tax Act would continue to apply. It was not a case of the Assessing Officer that the facts asserted by the petitioner were not correct or that for any other reason, the company had not become a deemed public company under section 43A of the Companies Act, 1956. This being the position, the decision of the Supreme Court in case of *M. Rajamoni Amma (Smt) and Another Vs. Deputy Commissioner of Income Tax (Assessment) Trivandrum and Others*, , would apply. In the said decision, it was held and observed as under (page 876):

"Before us, learned counsel for the appellants relied upon the above communication from the Registrar of Companies but since the genuineness of this letter was doubted we issued notice to the Registrar of Companies, Kerala. An affidavit has now been filed on behalf of the Registrar. It clearly shows that the company had become a public limited company by virtue of section 43A of the Companies Act, with effect from October 1, 1975. As already mentioned, the arrears sought to be recovered from the appellants relate to the assessment years 1977-78 to 1982-83. Obviously, the company being a public limited

company, proceedings against the directors for recovery of the tax due from the company cannot be taken, and certainly not proceeded with, under section 179 of the Income-tax Act, 1961. We need hardly say article 265 of the Constitution clearly prohibits any attempt to recover taxes except under the authority of law. It is, therefore, clear that further proceedings against the appellants for recovery of the tax due from the company have to be stayed."

7. Learned counsel for the Revenue, however, contended that in a given case, if a private company is a closely held company, it would still be open for the Revenue to contend that despite being converted into a deemed public company by virtue of operation of statute, section 179 would apply. Such are not the facts here raised by the Revenue. In the absence of any such foundation, we would not answer such a question in this petition.

8. Under the circumstances on this count, the petition is required to be allowed. We may briefly state that we are not influenced by the petitioner's contention that merely being a technical director, section 179 of the Act would not apply to him. We are also broadly in agreement with the view of the Assessing Officer that duty is cast on the directors to establish that non-recovery was not due to any gross neglect, misfeasance or breach of duty on his part and in the present case, he produced no material to establish such facts. Nevertheless, when section 179 of the Act itself does not apply, the question of seeking any recovery personally from the director would not arise. In the result, the impugned order dated January 3, 2005, is quashed. Rule made absolute. The petition is disposed of.