Calico Dyeing and Printing Works Vs. Commissioner of Income-tax, Bombay City Ii

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Court : Mumbai

Decided On : Feb-25-1965

Reported in : [1966]59ITR221(Bom)

Judge : V.S. Desai and ;Y.S. Tambe, JJ.

Acts : Transfer of Property Act - Sections 118; Income Tax Act, 1922 - Sections 10(2)

Appeal No. : Income-tax Reference No. 7 of 1962

Appellant : Calico Dyeing and Printing Works

Respondent : Commissioner of Income-tax, Bombay City Ii

Advocate for Def. : G.N. Joshi, Adv.

Advocate for Pet/Ap. : S.P. Mehta, Adv.

Judgement :

Tambe, J.

1. This is a reference under section 66(1) at the instance of the assessee, and the answers to the two questions which have been referred to us turn on the construction of the agreement of date 1st June, 1955.

2. The matter arises thus : We are here concerned with the assessment year 1956-57, the relevant previous year being the calendar year 1955. The assessee is a partnership firm registered under the Indian Income-tax Act, carrying on business in dyeing and printing textile goods. The partners of the assessee-firm are two having a moiety in the business - Manilal Narbheram Parekh and Chandulal Narbheram Kothary. By an agreement dated 1st June, 1955, the assessee-firm purported to sell its entire business as a going concern for a sum of Rs. 8,22,001 to a private limited company - Calico Dyeing & Printing Works Limited. The aforesaid stipulated price was paid by the purchaser company partly in cash and partly by allotting fully paid up shares to the partners of the assessee-firm and their nominees. On payment of this price, the purchaser company took over all the assets and liabilities of the assessee-firm. It is an admitted position that by reason of the aforesaid transfer of assets, the assessee-company had realised a sum of Rs. 1,94,720 in excess of the written down value of its assets as on 31st December, 1954. The position is like this :

Rs.

'Sale price ... 8,22,001

Less : Written down value as on 31-12-1954 ... 6,27,281

Profit 1,94,720'

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3. For the assessment year 1956-57, the assessee filed a return on 12th October, 1956, wherein it returned an income of Rs. 3,92,479 earned by it during the period January 1, 1955, to May 1, 1955. The said amount of Rs. 3,92,479 included the aforesaid profits of Rs. 1,94,720 as profits arising under section 10(2) (vii). However, later on, on 2nd February, 1957, the assessee field a revised return and in this revised return, the aforesaid amount of Rs. 1,94,720 was shown by the assessee under part 'D' claiming exemption therefore, on the ground that on the true construction of the agreement dated June 1, 1955, the transaction was not of sale, and therefore the said amount of Rs. 1,94,720 was not liable to be taxed under the second proviso to section 10(2)(vii). The claim of the assessee was rejected by the Income-tax Officer. He held that the transaction was a sale and therefore the amount was liable to be taxed under the said provisions of section 10(2) (vii). As the aforesaid computation of profits of Rs. 1,94,720 had been made on the basis of the written down value on 31st December, 1954, the Income-tax Officer did not allow any further depreciation for the five months from 1st January, 1955, to 31st May, 1955, the period during which the business was carried on in the relevant previous year to the said assessment year. The amount of depreciation computable was Rs. 88,577. Against this order of the Income-tax Officer, the assessee appealed to the Appellate Assistant Commissioner. At the appellate stage, two contentions were raised on behalf of the assessee. Firstly, it was contended that the said amount of Rs. 1,94,720 was not liable to tax as the transaction was not of sale; and secondly, it was contended that the Income-tax Officer ought to have allowed a further depreciation to the extent of Rs. 88,577. Both these contentions have been rejected. The assessee took a further appeal to the Tribunal. The Tribunal rejected all the contentions raised before it and dismissed the appeal. It is not necessary to reproduce all the contentions raised by the assessee before the Tribunal, inasmuch as Mr. Mehta, learned counsel appearing for the assessee, has stated before us that he was not pressing them before us. The only contention on behalf of the assessee which he has pressed before us is that on a true construction of the agreement, the transaction is one of exchange and not of sale. It is also not in dispute that if we come to the conclusion that the transaction is one of sale, then the answer to both the questions must be against the assessee. On the other hand, if we come to the conclusion that it is exchange, the answers will have to be against the revenue.

4. On an application under section 66(1) of the Act, the Tribunal has stated the case referring the following two questions of law to us :

'(1) Whether, on the facts and in the circumstances of the case, the sum of Rs. 1,94,720 is liable to tax as provided in the second proviso to section 10(2) (vii) of the Income-tax Act

(2) If the answer is in the negative, whether the assessee is entitled to Rs. 88,577 by way of depreciation from the beginning of the previous year till the date of the transfer as a deduction from the assessment having due regard to the provisions of section 10(5B) ?'

5. As the decision depends on the construction of the aforesaid agreement, it will be convenient at this stage to refer to the relevant parts of the said agreement. This agreement is between the assessee on the one hand and the Calico Dyeing & Printing Mills Limited, a private limited company, on the other. In the preamble, the assessee-firm has been referred to as the vendors and the private limited company as the 'the company'. The preamble recites that the vendors were at the material time carrying on the business and the company has been constituted having one of its object of acquiring and carrying on the business of the vendors. For this purpose, this agreement had been made between the vendors and the company on the terms recited in the agreement. Clause 1 provides : 'The vendors shall sell and the company shall purchase upon the terms and conditions hereinafter mentioned.' Then follow the five sub-clauses of clause 1, giving details of the various items of properties which were sold under this agreement. Clause 2 is not relevant. Clause 3 provides that the purchase of all the 'above-mentioned' premises shall take effect as from 1st day of June, 1955. Clause 4 provides : 'The price to be paid by the company to the vendors in respect of such sale shall be ascertained as follows : 'then sub-clauses (a) to (g) mention the prices agreed to be paid by the company to the vendors item-wise. Each sub-clause opens with 'A sum of Rs..... shall be the price of...' The total of the amount mentioned in

sub-clause (a) to (g) comes to Rs. 8,22,001. Clause 4A provides : 'The purchase moneys payable under this agreement shall be paid and satisfied in the manner following' : Sub-clause (a) of clause 4A provides that the company promised to allot to the vendors before 30th Day of June, 1955, 4,000 fully paid ordinary shares in the capital of the company, and the vendors shall accept such shares as part payment to the extent of Rs. 4 lakhs. Clause (b) provides : 'The company has paid to the Vendors Rs. 2,00,000 on the execution of these presents and the balance of the consideration shall be paid by the company to the vendors within 60 days from the execution of these presents.' The other clauses are not material. Suffice it to say, in all these clauses, the assessee throughout has been mentioned as 'the Vendors'.

6. Mr. Mehta contends that the transaction between the parties is not one of sale but of exchange. In exchange the assessee-firm had given its property and the company in exchange had given its fully paid shares. Payment of money was only by way of adjustment. Referring us to the definitions of 'sale' and 'exchange' in the Sale of Goods Act as well as the Transfer of Property Act, Mr. Mehta argued that for a transaction to be a sale, it has to be for a price, i.e., money. Where the consideration under the transaction is not paid in cash, but on the other hand, it is paid partly in the shape of property and partly in the shape of money, the transaction is nothing else but an exchange. In support of his contention, Mr. Mehta has referred us to the three decisions in Ismail Shah v. Saleh Muhammad Shah, Randhir Singh v. Randhir Singh and Ram Badan Lal v. Kunwar Singh. It is not possible for us to accept the contentions raised by Mr. Mehta. It is indeed true that the shares would be goods within the meaning of the definition clause of the Sale of Goods Act. Sub-section (1) of section 4 of that Act defines a contract in following terms : 'A contract of sale of goods is a contract whereby a seller transfers or agrees to transfer property in the goods to the buyer for a price.' Price has been defined in sub-section (1) of section 4 : ''Price' means money consideration for the sale of goods.' Reading the meaning of the word 'price' in section 4, the material part would read : 'A contract of sale of goods is a contract whereby a seller transfers or agrees to transfer property in goods to the buyer for money consideration (price).' In our opinion, the definition of 'sale of goods' to which Mr. Mehta referred us is hardly of any assistance to him. The emphasis in section 4 is not on the mode in which the parties agree to pay the price. The emphasis is on the nature of the contract. If the contract is to transfer property in goods for a money consideration, the parties may agree to pay or receive it in any manner they like; that would not affect the nature of the contract. The contract between the parties in the instant case has been exactly the same. The assessee-company (vendors) had agreed to sell their business to the private limited company for a money consideration of Rs. 8,22,001. The contract between the parties, in our opinion, squarely falls within the definition of section 4. Section 54 of the Transfer of Property Act, which defines a 'sale' means 'a sale is a transfer of ownership in exchange for price paid or promised or part paid and part promised'. Price has not been defined. But the expression 'price' has been understood in the same sense as it is understood in the Sale of Goods Act, i.e., money consideration. In our opinion, this definition also is hardly of any assistance to the assessee in the present case. The position again is more or less the same as under section 4 of the Sale of Goods Act. The emphasis is not on the mode agreed between the parties to pay the price, but the emphasis is on the nature of transfer. If the transfer of ownership is for money consideration, it is a sale. We have already referred to the material parts of the agreement. Section 118 of the Transfer of Property Act defines 'exchange' as 'when two persons mutually transfer ownership of one thing for the ownership of another, neither any or both things being money only, the transaction is called an exchange. A transfer of property in completion of exchange can be made only in the manner provided for transfer of such property by sale. It has to be seen whether the transaction in the instant case falls under the aforesaid definition of 'exchange'. Now, for a transaction to be an exchange, there has to be a mutual transfer of ownership of respective properties of each to the other. In other words, the form of the transaction must be - A transferring to B his property X, and in exchange, B transferring his property Y to A. The difference, is any, may be adjusted by payment of money. But the essential thing is mutual transfer. There is nothing in the deed of agreement showing that the private limited company was transferring the shares to the assessee-firm in exchange of the assessee-company transferring its ownership in the business to the private limited company. The material part, namely, sub-clause (a) of clause 4A is in the following terms :

'(a) The company shall on or before the 30th day of June, 1955, allot to the vendors or as they shall direct 4,000 ordinary shares in the capital of the company of the nominal value of Rs. 100 each credited as fully paid up and such shares shall be designated upon the certificates thereof and otherwise as vendors, shares and shall be issued in connection with the provisions of this agreement and the vendors shall accept as part payment to the extent of Rs. 4 lakhs.'

7. The private limited company is not transferring its property to the assessee, but it is allotting the shares to the partners of the assessee-firm or their nominees as if in the ordinary course of business on receipt of the price of the shares. The transaction is not one of transfer of any shares owned by it by the private limited company to the assessee. Reading the agreement as a whole, there can hardly be any doubt that the contract between the parties was in express terms that of sale, whereunder the assessee-firm had sold its going concern to the company for a pre-determined agreed price of Rs. 8,22,001. As regards the payment of the price, it was agreed to be paid in cash to the extent of Rs. 2 lakhs on the date of the agreement in the shape of 4,000 fully paid up ordinary shares of the company at Rs. 100 each, before 30th June, 1955, and the balance of Rs. 2,22,001 within 60 days of the agreement. Undoubtedly, the contract is one of sale. The mere fact that the purchaser agrees to pay purchase money partly in the shape of cash and partly in the shape of allotment of its shares does not render a contract of sale into a contract of exchange. The transaction in substance is as if the purchaser company has paid Rs. 4 lakhs to the vendor firm, thereafter the firm has paid Rs. 4 lakhs to the company by way of subscription to its share capital and thereupon the said four thousand shares have been allotted by the company to the partners of the firm. It is open to the parties to a contract of sale to agree to receive the sale price otherwise than merely in cash. At page 3 of Bejamin on Sale, 8th edition, it has been made clear :

'So, in relation to the element of price. It must be money, paid or promised, according as the agreement may be for a cash or a credit sale; but, if the consideration given be something other than money, it is not a sale. If goods be given in exchange for goods, it is a barter. But the consideration may be partly the payment of money and partly the delivery of goods and in this case the contract is a contract of sale. Thus in Aldridge v. Johnson the contract was for the transfer of 52 bullocks, valued at pounds 5 each, against 100 quarters of barley, valued at pounds 2 a quarter, the difference to be paid in cash and this was held to be a contract of sale. It is also a contract of sale where the buyer has the option of delivering goods in lieu of the payment of the agreed money price.'

8. In the agreement it has been in terms provided that the allotment of shares was in lieu of payment of the purchase money, the assessee-firm having agreed to accept these shares as part of the payment of sale price to the extent of Rs. 4 lakhs. The decisions to which Mr. Mehta has drawn out attention arise out of pre-emption suits, and they are distinguishable on facts, the decisions having turned on the terms of the contract between the parties in each case. The position, however, has been made clear in Ram Badan Lal v. Kunwar Singh by the learned judges that 'no hard and fast rule can be laid down as to when two transactions amount to a sale or to an exchange.' Each case will have to be decided on its own facts ascertaining what the real nature of the transaction between the parties had been. The real nature of the transaction between the parties has to be decided having regard to the agreement between the parties and not on the mode in which the consideration under the contract has been paid. As we have already stated, the decision in those cases turned on the contracts in those cases. It is not necessary to refer in detail to those cases.

9. In the result, our answer to the first question is in the affirmative. In view of our answer to the first question, it is not necessary to answer the second question. The assessee shall pay the costs of the Commissioner.