

Commissioner of Income Tax Vs Gira Sarabhai

Income-tax Reference No. 529 of 1980

Court: Gujarat High Court

Date of Decision: Sept. 16, 1993

Acts Referred:

Income Tax Act, 1961 "Section 45, 48, 52, 52(1), 52(2)

Citation: (1994) 209 ITR 356

Hon'ble Judges: M.B. Shah, J; J.M. Panchal, J

Bench: Division Bench

Advocate: B.J. Shelat, for the Appellant; D.A. Mehta and R.K. Patel, for the Respondent

Judgement

J.M. Panchal, J.

At the instance of the Commissioner of Income Tax, Gujarat-I, Ahmedabad, the Income Tax Appellate Tribunal,

Ahmedabad Bench "B", has made the reference to this court u/s 256(1) of the Income Tax Act, 1961 ("the Act", for short), as the Tribunal was

satisfied that eight questions of law arise out of the order dated November 29, 1979, passed by it in Income Tax Appeals Nos. 233 and

228/(Ahd.) of 1978-79, relating to the assessment year 1973-74.

2. The assessee, Smt. Gira Sarabhai, derives income from partnership firms as well as by way of remuneration as one of the directors in different

companies, dividends and insurance commission, etc. The assessee submitted a return on January 23, 1974, showing an income of Rs. 1,39,810.

3. During the accounting year 1973-74, the assessee had received remuneration of Rs. 60,000 from Sarabhai Technological Development

Syndicate Pvt. Ltd., Rs. 60,000 from Karamchand Premchand Pvt. Ltd., Rs. 60,000 from Sarabhai M. Chemicals Pvt. Ltd. and Rs. 30,000 from

Sercon Pvt. Ltd., as one of the directors. The assessee claimed that the above remuneration should be treated as salary. The Income Tax Officer

did not accede to the said claim and treated the abovereferred receipt as income from other sources in view of the assessment orders passed for

the assessment year 1970-71. Since the remuneration received from the companies was not treated as salary in the hands of the assessee, the

Income Tax Officer held that the assessee was not eligible for the exemption of an amount of Rs. 21,000 contributed by the companies to the

provident fund and Rs. 31,500 contributed to the superannuation fund for concessional treatment in respect of those contributions under the

provisions of section 80C of the Act. Similarly, interest amount of Rs. 14,281 on the contributions to the provident fund and Rs. 9,656 on the

contributions to the superannuation fund were also held to be not eligible for exemption and the same were included in the total income of the

assessee.

4. Before the Income Tax Officer, the assessee claimed exemption of medical reimbursement of Rs. 6,428 received from two companies. The

assessee claimed exemption for the said amount in view of Circular No. 33 (LXXV-1.5) of 1955, dated August 1, 1955, issued by the

board. The Income Tax Officer took the view that the circular was applicable only in the case of employees and the assessee being not an

employee of the companies from which she had received reimbursement of medical expenses, the claim was not allowed.

5. The assessee was holding 1,000 shares in a company known as Hansol Farm Pvt. Ltd. the assessee sold those shares in October, 1972, to

Gira Sarabhai Trust No. 2 at the price of Rs. 45 per share. The assessee was also holding 175 shares in Sarabhai Nursery Pvt. Ltd. and those

shares were sold by the assessee at Rs. 41 per share to Gira Sarabhai Trust No. 1. The shares sold were earlier purchased by the assessee at the

rate of Rs. 100 per share during the assessment year 1971-72. In the return of income, the assessee claimed total short term capital loss of Rs.

65,325 on the sale of 1,000 ordinary shares of Hansol Farm Pvt. Ltd. and 175 ordinary shares of Sarabhai Nursery Pvt. Ltd., in the month of

October, 1972, to Gira Sarabhai Trust No. 2 and Gira Sarabhai Trust No. 1, respectively. The shares should in October, 1972, of both the

companies were considered for the assessment year 1973-74. The Income Tax Officer, applying the provisions of section 52(2) of the Act,

estimated the fair market price of the shares at Rs. 190 per share and disallowed the short-term capital loss claimed by the assessee.

6. The assessee along with her brother, Gautam Sarabhai, had formed a partnership by name Messrs. Karigari on October 28, 1971. In the

assessment year 1973-74, the assessee contributed 70 shares of Sarabhai M. Chemicals, 71 ordinary shares of Messrs. K. P. P. L. and 890

shares of Calico Mills as contribution of capital on March 22, 1973. The difference of Rs. 2,25,125 between the book value and the fair market

value was sought to be added as the capital gain of the assessee. The assessee claimed exemption on the ground that such capital contribution in

kind does not amount to transfer of a capital asset as defined in section 2(47) of the Act. The Income Tax Officer took the view that capital

contribution in kind amounted to transfer of capital assets within the meaning of section 45 of the Act and a long-term capital gain on the transfer of

shares to the partnership having accrued to the assessee, the assessee was liable to pay tax on capital gains on the amount indicated in the

computation of income. The Income Tax Officer accordingly assessed the assessee and passed an order on August 24, 1976.

7. Feeling aggrieved by the abovereferred order, the assessee preferred an appeal before the Appellate Assistant Commissioner of Income Tax

who allowed the appeal partly. The Appellant Assistant Commissioner, following the view taken by the Tribunal, held that the amount received by

way of remuneration was taxable as salary income and consequently the contributions made by the companies to the provident fund and

superannuation fund and interest therein were exempt. Before the Appellate Assistant Commissioner, it was claimed by the Income Tax Officer

that the superannuation schemes of the companies were not approved by the Commissioner of Income Tax and hence the additions were justified.

The Appellate Assistant Commissioner accepted the objections and directed deletion of such additions as and when recognition was accorded to

the said funds by the Commissioner of Income Tax for the assessment year 1973-74. Regarding contributions of shares as capital by the assessee,

the Appellate Assistant Commissioner held that the market value was Rs. 1,370 per share and not Rs. 1,295 as claimed by the assessee. The

Appellate Assistant Commissioner further held that as the difference was less than 15 per cent. between apparent consideration and fair market

value of the shares, section 52(2) of the Act had no application and deleted the additions made by the Income Tax Officer on this count. The

Appellate Assistant Commissioner confirmed the rest of the order passed by the Income Tax Officer.

8. Feeling aggrieved, the Income Tax Officer preferred Income Tax Appeal No. 233 of 1980 before the Tribunal, whereas the assessed preferred

Income Tax Appeal No. 228 of 1980. The Tribunal, by judgment and order dated November 29, 1979, dismissed the appeal filed by the

Revenue and allowed the appeal filed by the assessee. The Commissioner of Income Tax, Gujarat-I, Ahmedabad, filed an application u/s 256(1)

of the Act requiring the Tribunal to draw up a statement of case and refer questions of law to the High Court for its decision. The Tribunal was

satisfied that eight questions of law arose out of the order dated November 29, 1979, and, therefore, after drawing up the statement of case, has

referred the following eight questions of law for the decision of this court :

(1) Whether, on the facts in the circumstances of the case, the Income Tax Appellate Tribunal was right in law in holding that the remuneration

received by the assessee as director from the companies was taxable under the head "Salaries" and not under the head "Income from other

sources" ?

(2) Whether the order of the Appellate Assistant Commissioner directing the Income Tax Officer to delete the addition as and when the

Commissioner of Income Tax recognised the funds and if the recognition extended to the assessment year 1973-74 was rightly upheld by the

Tribunal ?

(3) Whether in the absence of any evidence to show that something more than the apparent consideration was in fact paid, section 52(2) of the

Income Tax Act, 1961, could not be invoked ?

(4) Whether, on the facts and in the circumstances of the case, the assessee as a director of the companies was liable to be taxed on Rs. 6,428

received as reimbursement of medical expenses from Sarabhai Technological Development Syndicate Private Limited ?

(5) Whether the provisions of section 52(2) of the Income Tax Act, 1961, could not be applied in respect of sale of shares of Hansol Farm Pvt.

Ltd. and Sarabhai Nursery Pvt. Ltd. in favour of Gira Sarabhai Trust No. 2 ?

(6) Whether the provisions of section 52(2) of the Act could not be applied to the facts and circumstances of the case in respect of 175 shares of

Sarabhai Nursery which were sold to the trust at Rs. 41 per share in October, 1972 ?

(7) Whether when a partner contributes certain shares of limited companies as contribution of capital, it amounts to transfer exigible to capital gains

tax u/s 2(47) read with section 45 of the Act ?

(8) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the transaction did not yield

any capital gains to the assessee and the question of quantum of capital gains did not arise ?

9. Reasons :

(1) So far as answer to question No. 1 is concerned, it cannot be said that, on the facts and in the circumstances of the case, the Tribunal

committed any error in holding that the remuneration received by the assessee as director from the company was taxable under the head ""Income

from salaries"" and not under the head ""Income from other sources"". The answer to the question whether remuneration received by a director is

taxable under the head ""Income from salaries"" or not depends upon the answer to the question as to whether the director is an employee of the

company or not. For deciding the question whether a director is an employee of the company or not, one has to find out as to whether the

relationship of master and servant exists between the company and the director or not. This question is covered by the decision of this court

rendered in the case of CIT v. Gautam Sarabhai [1984] 19 Taxman 353 (Guj). In the said case, the question was whether the remuneration

received by the assessee from Karamchand Premchand Pvt. Ltd. and other three companies was assessable under the head ""Income from other

sources"" or as ""Income from salary"". Following the decision in Income Tax Reference No. 170 of 1976 holding that the assessee was an employee

of Karamchand Premchand Pvt. Ltd., the said question was answered in favour of the assessee and against the Revenue. Relying upon the

decision in CIT v. Gautam Sarabhai [1984] 19 Taxman 353 (Guj) in Income Tax Reference No. 200 of 1976 decided on August 5, 1985, it has

to be held by this court that the present assessee was an employee of Karamchand Premchand Pvt. Ltd. and other companies and, therefore, the

remuneration received by her as managing director was taxable under the head ""Income from salary"". In view of the above decision of this court,

we hold that, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the remuneration received by the

assessee as director from the companies was taxable under the head ""Income from salaries"" and not under the head ""Income from other sources"".

The said question is, therefore, answered in favour of the assessee and against the Revenue.

(2) The second question posted in this reference is whether the Tribunal rightly upheld the order of the Appellate Assistant Commissioner directing

the Income Tax Officer to delete the addition as and when the Commissioner of Income Tax recognised the funds for the assessment year 1973-

74 ?

The matter regarding recognition of the funds has been taken up with the Commissioner of Income Tax. However, as on today no recognition has

been accorded by the Commissioner of Income Tax to the contributions made by the companies to the provident fund and superannuation funds

under the Act. Therefore, in our view, the Tribunal rightly held that the additions were justified. The Income Tax Officer's objection was well-

founded since the contribution to the unrecognised provident fund and superannuation fund did not satisfy the conditions laid down in the Fourth

Schedule to the Act. In fact, this point has been answered by the Tribunal in favour of the Revenue. However, the direction given by the Appellate

Assistant Commissioner and confirmed by the Tribunal to delete the additions as and when the Commissioner of Income Tax accords recognition

to the funds in question for the assessment year 1973-74 is perfectly just and proper in view of the different provisions of the Act. Therefore, our

answer to question No. 2 is that the Tribunal has rightly upheld the order of the Appellant Assistant Commissioner directing the Income Tax

Officer to delete the additions as and when the Commissioner of Income Tax recognised the funds for the assessment year 1973-74. The said

question is answered against the Revenue and in favour of the assessee.

(3) Questions Nos. 3, 5, and 6 are in a way inter-connected and, therefore, they have been dealt with together.

Question No. 3, which arises for consideration of this court is whether in the absence of any evidence to show that something more than the

apparent consideration was in fact paid, section 52(2) of the Income Tax Act, 1961, could be invoked or not ?

Question No. 5 posed in the reference is whether the provisions of section 52(2) of the Income Tax Act, 1961, could not be applied in respect of

sale of shares of Hansol Farm Pvt. Ltd. and Sarabhai Nursery Pvt. Ltd. in favour of Gira Sarabhai Trust No. 2 ?

Question No. 6 referred to this court is whether the provisions of section 52(2) of the Act could not be applied in the facts and circumstances of

the case in respect of 175 shares of Sarabhai Nursery, which were sold to the trust at Rs. 41 per share in October, 1972 ?

As all the abovereferred three questions pertain to the scope and interpretation of section 52(2) of the Act, for the sake of convenience, they are

discussed together hereunder :

The assessee sold 1,000 shares of Hansol Farm Pvt. Ltd. at the rate of Rs. 45 per share whereas she effected sale of 175 shares of the Sarabhai

Nursery Pvt. Ltd. at the rate of Rs. 41 per share. The Income Tax Officer after applying the provisions of section 52(2) of the Act, estimated the

fair market price of the shares at Rs. 190 per share and disallowed the short-term capital loss claimed by the assessee. The Appellate Assistant

Commissioner confirmed that order. However, the Tribunal took the view that there was nothing to show that the assessee in fact revived more

than the apparent consideration and allowed the claim of the assessee.

In the case of K.P. Varghese Vs. Income Tax Officer, Ernakulam and Another, the Supreme Court considered the scope of sections 48, 52(1)

and 52(2) of the Act. After considering the scheme of the abovereferred provisions, it has been held that sub-section (2) of section 52 of the Act

can be invoked only where the consideration for the transfer has been understated by the assessee or, in other words, the consideration actually

received by the assessee is more than what is declared or disclosed by him and the burden to prove such understatement or concealment is not the

Revenue. It has been further held that the burden must be discharged by the Revenue by establishing facts and circumstances from which a

reasonable inference can be drawn that the assessee has not correctly declared or disclosed the consideration and there is an understatement or

concealment of the consideration in respect of the transfer. It has been also held that sub-section (2) of section 52 of the Act has no application in

the case of an honest and bona fide transaction where the consideration received by the assessee has been correctly declared or disclosed by him

and there is no concealment or suppression of the consideration.

(4) In the facts of the present case, there is nothing on the record to indicate that while effecting the transfer, the assessee had understated the

consideration or that the consideration actually received by the assessee was more than what was declared or disclosed by her. The Revenue has

not discharged the burden of proof by establishing facts and circumstances from which a reasonable inference can be drawn that the assessee has

not correctly declared or disclosed the consideration received by her and there is an understatement or concealment of the consideration in respect

of the transfer. In this view of the matter, we are of the opinion that in the absence of any evidence to show that something more than the apparent

consideration was in fact paid, section 52(2) of the Income Tax Act, 1961, could not have been invoked by the Income Tax Officer and the

finding of the Tribunal is just and proper in this regard. Therefore, question No. 3 is answered in favour of the assessee and against the Revenue.

For the same reason, we hold that the provisions of section 52(2) of the Income Tax Act, 1961, could not be applied in respect of sale of shares

of Hansol Farm Pvt. Ltd. in favour of Gira Sarabhai Trust No. 2. Our answer to the said question is in favour of the assessee and against the

Revenue. Similarly, our answer to question No. 6 is that the provisions of section 52(2) of the Act could not be applied to the facts and

circumstances of the case in respect of 175 shares of Sarabhai Nursery which were sold to the trust at Rs. 41 per share in October, 1972.

Question No. 6 is answered in favour of the assessee and against the Revenue.

(5) Question No. 4 posed for consideration in this reference is whether, on the facts and in the circumstances of the case, the assessee as director

of the companies was liable to be taxed on Rs. 6,428 received as reimbursement of medical expenses from Sarabhai Technological Development

Syndicate Pvt. Ltd. and Karamchand Premchand Pvt. Ltd. A similar question arose for the consideration of this court with reference to this very

assessee in Income Tax Reference No. 2000 of 1976 for the assessment year 1967-68 to the assessment year 1969-70. The question therein

considered was whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that the reimbursement of

medical expenses by Karamchand Premchand Pvt. Ltd. to the assessee is not liable to be assessed in the hands of the assessee for the years under

reference.

Relying upon the decision of this court in CIT v. Gautam Sarabhai [1984] 19 Taxman 353 (Guj) the said question has been answered in the

affirmative by this court. In the judgment dated August 5, 1985, delivered in the abovenumbered Income Tax reference, this court has taken the

view that the Board's Circular No. 32 of 1955, dated July 18, 1955, makes no distinction between reimbursement of expenses incurred to an

employee and medical facilities extended to an employee. In view of the aboveresferred decision of this court, we are of the view that the assessee

as a director of the companies was not liable to be taxed on Rs. 6,428 received as reimbursement of medical expenses from Sarabhai

Technological Development Syndicate Pvt. Ltd. and Karamchand Premchand Pvt. Ltd.

Having regard to the position as obtaining above, question No. 4 is answered in the negative, i.e., in favour of the assessee and against the

Revenue.

(6) Questions Nos. 7 and 8 are related to each other and, therefore, a common decision is rendered therein.

Question No. 7 is whether when a partner contributes certain shares of limited companies as contribution of capital to a firm in which the assessee

is one of the partners, it amounts to transfer exigible to capital gains tax u/s 2(47) read with section 45 of the Act?

The abovereferred point is squarely concluded by the judgment of the Supreme Court rendered in the case of Sunil Siddharthbhai Vs.

Commissioner of Income Tax, Ahmedabad, Gujarat, . After examining the scheme of the Income Tax Act, 1961, and the rights and liabilities of the

partner of a firm, it has been held that when the partner of the firm makes over capital assets to a firm as his contribution towards capital, there is a

transfer of a capital asset within the terms of section 45 of the Income Tax Act, 1961, because an exclusive interest of the partner in personal

assets is reduced, on their entry into the firm, into a share interest.

In view of the above ruling of the Supreme Court of India, it is clear that when a partner contributes certain shares of limited companies as

contribution of capital, it amounts to transfer exigible to capital gains tax u/s 2(47) read with section 45 of the Act. Therefore, question No. 7 is

answered in the affirmative, i.e., in favour of the Revenue and against the assessee.

(7) The last question, i.e., question No. 8, which requires to be considered in this reference is whether on the facts and in the circumstances of the

case, the Appellate Tribunal was right in law in holding that the transaction (of contributing certain shares of limited companies as contribution of

capital of the assessee) did not yield any capital gains to the assessee and the question of quantum of capital gains did not arise ?

This question is also concluded by the judgment of the Supreme Court rendered in the case of Sunil Siddharthbhai Vs. Commissioner of Income

Tax, Ahmedabad, Gujarat, . The Supreme Court therein has held as under (headnote) :

The consideration for the transfer of the personal assets ins the right which arises or accrues to the partner during the subsistence of the

partnership to get his share of the profits from time to time and, after the dissolution of the partnership or with his retirement from the partnership,

to get the value of his share in the net partnership assets as on the date of the dissolution or retirement after deduction of liabilities and prior

charges. The credit entry made in the partner"s capital account in the books of the partnership firm does not represent the true value of the

consideration. It is a notional value only, intended to be taken into account at the time of determining the value of the partner"s share in the net

partnership assets on the date of dissolution or on his retirement, a share which will depend upon deduction of the liabilities and prior charges

existing on the date of dissolution or retirement. It is not possible to predicate beforehand what will be the position in terms of the monetary value

of a partner"s share on that date. At the time when the partner transfers his personal asset to the partnership firm, there can be no reckoning of the

liabilities and losses which the firm may suffer in the years to come. All that lies within the womb of the future. It is impossible to conceive of

evaluating the consideration acquired by the partner when he brings his personal asset into the partnership firm when neither can the date of

dissolution or retirement be envisaged nor can there be any ascertainment of liabilities and prior charges which may not have even arisen yet.

Therefore, the consideration which a partner acquires on making over his personal asset to the firm as his contribution to its capital cannot fall

within the terms of section 48. And as that provision is fundamental to the computation machinery incorporated in the scheme relating to the

determination of the charge provided in section 45, such a case must be regarded as falling outside the scope of capital gains taxation altogether.

10. Applying the principles of law propounded by the Supreme Court of India to the facts of the present case, it is clear that the transaction by

which the assessee made over certain shares of limited companies as her contribution of capital did not yield any capital gain to the assessee and,

therefore, the question of quantum of capital gain could not have been considered. The Appellate Tribunal, therefore, was right in holding that the

transaction did not yield any capital gain to the assessee and the question of quantum of capital gain could not have been considered. The

Appellant Tribunal, therefore, was right in holding that the transaction did not yield any capital gain to the assessee and the question of capital gain

did not arise. The said question is, therefore, answered in favour of the assessee and against the Revenue.

11. In view of the above discussion and our answers to the questions referred to above, the reference stands accordingly disposed of with no

order as to costs.