

(2002) 08 MAD CK 0196**Madras High Court****Case No:** Tax Case No. 134 of 1989 27 August 2002 A.Y. 1976-77

Neelamalai Agro Industries Ltd.

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision: Aug. 27, 2002**Citation:** (2002) 178 CTR 167**Hon'ble Judges:** R. Jayasimha Babu, J; K. Raviraja Pandian, J**Bench:** Full Bench**Advocate:** R. Meenakshi Sundaram, for the Assessee T.C.A. Ramanujam, for the Revenue, for the Appellant;**Judgement**

@JUDGMENTTAG-ORDER

R. Jayasimha Babu, J.

The question referred to us at the instance of the assessee is whether on the facts and in the circumstances of the case, the assessment of the sum of Rs. 4,45,305 as capital gains liable to tax arising out of the compensation amount received under the insurance policy on account of damage to the assessee's Sutton Tea factory building by fire is valid in law. The assessment year is 1976-77.

2. The assessee is engaged in the business of growing and manufacturing tea. It had two factories, one situated in Sutton Estate and another in Katary Estate. On 23-6-1975, there was a fire accident in which the factory buildings and machinery installed in Sutton Tea factory premises were destroyed, the assets had been insured with two insurance companies who settled the assessee's claim for compensation in terms of the fire policy. The company received a sum of Rs. 16,84,225 as compensation, of which, a sum of Rs. 8,00,000 represented compensation for damage suffered by the buildings and the rest represented compensation for damage to the plant and machinery.

3. The assessing officer deemed the receipt of those amounts from the insurance companies as consideration for the extinguishment of the rights of the assessee in those capital assets and regarded it as a "transfer", as that term is defined in section 2(47) of the Income Tax Act. Consequently, he brought to tax a sum of Rs. 5,72,762 u/s 41(2) and Rs. 4,45,305 u/s 45 of the Act. The liability for capital gain was restricted to the "transfer" of the building, as the amount received for the loss of plant and machinery did not justify a calculation u/s 45 of the Act.

4. Appeal by the assessee to the Commissioner (Appeals) did not bear any fruit. The Commissioner (Appeals) found that the surveyor's report has stated conclusively that the building was a total wreck. He also held that as some of the machineries had been salvaged, there was no transfer of those machineries, the same having been shifted to the assessee's Katar Estate. The Commissioner (Appeals) took the view that on the destruction of the building, there was total extinguishment of the rights of the assessee in the building, and that, such extinguishment amounted to "transfer".

5. The assessee having carried the matter further to the Tribunal, the Tribunal relying upon one of its earlier orders in the case of another assessee affirmed the order of the Commissioner (Appeals).

6. That the building was completely destroyed in the fire is undisputed. The capital asset thus was not in existence when the assessee received compensation. The asset was not available, for being owned, used or enjoyed by any one.

7. "Capital asset" is defined in section 2(14) of the Act. It is defined as meaning property of any kind held by an assessee whether or not connected with his business or profession. The definition of "transfer" in section 2(47) of the Act as it stood at the commencement of the year 1976-77 read thus :

"transfer", in relation to a capital asset, includes.

- (i) the sale, exchange or relinquishment of the asset;
- (ii) the extinguishment of any rights therein; or
- (iii) the compulsory acquisition thereof under any law.

The modes of transfer mentioned in this definition are : sale, exchange, compulsory acquisition, relinquishment of the asset, and extinguishment of any rights in the capital asset. The definition is an inclusive definition, and modes of transfer other than those referred to in the definition are also capable of being included in this definition. All the modes mentioned in the definition appear to have one thing in common viz., that the capital asset would continue to exist after the transfer by any one of those modes.

8. "Capital gains" is dealt with in Chapter IV of the Act in sections 45 to 55A. Section 45 of the Act refers to profits or gains arising from the transfer of a capital asset.

The section which brings the capital gains to charge of tax is section 45. What is to be taxed is the profit or the gain arising from the "transfer of a capital asset". This also implies the continued availability of the asset even after the transfer. The extent of the gain is to be ascertained with reference to the cost of acquisition of the asset. The continued availability of the asset even after the transfer, though not stated in so many words, is clearly implicit in the definition of "transfer", as also in the charging section.

9. When a thing is destroyed by fire or when a ship sinks into the sea, the capital asset is no longer available for being owned, used or enjoyed by anyone including the assessee. With the destruction of the asset, the rights of the assessee in that asset also would be destroyed. The destruction of such rights in an asset consequent upon the assets ceasing to exist is a situation which is not contemplated either in the definition of "transfer", or in the charging section.

10. The Supreme Court in the case of Vania Silk Mills (P) Ltd. Vs. Commissioner of Income Tax, Ahmedabad [OVERRULED], dealt with a case where the assessee's machineries had been destroyed in a fire and for which it had received the amount payable by the insurer who had insured those machineries against the risk of fire. The court in that case held thus :

"When an asset is destroyed there is no question of transferring it to others, The destruction or loss of the asset, no doubt, brings about the destruction of the right of the owner or possessor of the asset, in it. But it is not on account of transfer, it is on account of the disappearance of the asset. The extinguishment of right in the asset on account of extinguishment of the asset itself is not a transfer of the right but its destruction. By no stretch of imagination can the destruction of the right on account of the destruction of the asset be equated with the extinguishment of right on account of its transfer."

Thus, the court held that the destruction of the asset which, as a consequence brings about the extinguishment of rights in that asset, cannot be equated with the extinguishment of rights of the assessee on the transfer of the asset.

11. This court in the case of Agnes Corera Vs. Commissioner of Income Tax, dealt with a case where the boat owned by the assessee and which had been insured against loss, sank in the sea. The court held that the amount received by the assessee from the insurer who had insured the boat against such loss was not taxable by treating part of the amount received from the insurer as capital gain. While doing so, the court relied upon the observation of the Apex Court in the case of Vania Silk Mills (P) Ltd. (supra) that :

"whatever the mode by which the transfer was brought about, the existence of the asset during the process of transfer was a precondition. Unless the asset existed in fact, there could not be a transfer of it."

12. Learned counsel for the revenue, however, contended that the law declared by the Apex Court in the case of Vania Silk Mills (P) Ltd. (supra) is no longer good law, and that that decision has been both expressly and implidely been overruled by a three Judge Bench in the case of Commissioner of Income Tax, Cochin Vs. Mrs. Grace Collis and Others . In the case of Collis (supra), the court was concerned with the question as to whether there is a transfer of the shares when the amalgamation of the company whose shares are held by the assessee is ordered by the court with another company. The court held that the rights of the assessee in the capital asset viz., the shares in the amalgamating company stood extinguished upon the amalgamation of the amalgamating company with the amalgamated company and that :

"There was, therefore, a transfer of the shares in the amalgamating company within the meaning of section 2(47). It was, therefore, a transaction to which section 47(vii) applied and, consequently, the cost to the assessees of the acquisition of the shares of the amalgamated company had to be determined in accordance with the provision of section 49(2), that is to say, the cost was deemed to be the cost of the acquisition by the assessees on their shares in the amalgamating company. "

13. On the amalgamation of one company with another, the assets and liabilities of the amalgamating company are taken over by the amalgamated company. Those assets and liabilities do not cease to exist when amalgamation takes place. They continue to exist. The ownership of those assets stand transferred to the amalgamated company.

14. The rights of the shareholder in the shares held by him or her in the amalgamating company which had owned the assets, are replaced by the rights given to such shareholders in the shares of the amalgamated company which takes over the assets and liabilities of the amalgamating company. Shares in the amalgamated company are allotted to the shareholder of the amalgamating company, as the consideration for the transfer of the assets of the amalgamating company, the ratio being determined with reference to the value of the respective shares which is dependent upon the value of the assets and prospects of the company. Despite the extinguishment of the rights in the shares of the amalgamating company on its dissolution, the assets which gave value to those shares prior to amalgamation continue to exist, now under the ownership of the amalgamated company, and may provide added value to the shares of that company.

15. The extinguishment of rights in the capital asset referred to in the definition of "transfer" in section 2(47) of the Act, therefore, would clearly apply to a case where the rights in the shares in the amalgamating company are extinguished on amalgamation to be replaced by shares in the amalgamated company, which after amalgamation is the owner of the assets transferred to it as a consequence of the amalgamation, and which will thereafter have the ownership, use and benefit of

those assets.

16. The case of amalgamation of companies and the extinguishment of the rights of the shareholder in the amalgamating company is in noway comparable to the destruction of the assets which as a consequence brings about the extinguishment of the rights of the assessee-owner in such assets.

17. In the case of Collis (supra), at p. 330 of the reports, the court noticed the submission made by counsel for the revenue thus :

"Learned counsel for the revenue submitted that having held that the payment in settlement of the insurance claim was not in consideration of the transfer to the insurer of the damaged machinery and that therefore, there was no transfer within the meaning of section 45, it was unnecessary for this court in Vania Silk Mills (P) Ltd. Vs. Commissioner of Income Tax, Ahmedabad [OVERRULED], to go on to consider the definition in section 2(47) and the meaning to be attached to the expression "extinguishment of any rights therein". In his submission the decision in Vania Silk (P) Ltd."s case (supra) was to this extent obiter dicta".

It is only to the extent of that obiter dicta, that the decision rendered in the case of Collis (supra) can be said to be at variance with the decision rendered in the case of Vania Silk Mills (P) Ltd. (supra). In the case of Collis (supra), the court considered the terms "extinguishment of any rights therein" and the definition of "transfer" in section 2(47) of the Act. The court did not approve limiting the effect of the words "extinguishment of any rights therein" in the definition of "transfer" in section 2(47) of the Income Tax Act, to extinguishment on account of transfers. The court held :

"As we read it, therefore, the expression does include the extinguishment of rights in a capital asset independent of and otherwise than on account of transfer."

18. In the case of Collis (supra), the court did not have occasion to go into the question as to whether the destruction of a capital asset which as a consequence brings about the extinguishment of the rights of the assessee-owner in such asset, would amount to transfer. The court did not hold that Vania Silk Millis (P) Ltd. (supra) was wrongly decided, or that the definition of "transfer" in section 2(47), particularly, the use of the words "extinguishment of any rights therein" would cover cases of destruction of the capital asset. Cases such as the destruction of the capital asset in a fire, or it's complete loss as in the case of sinking of a vessel in the sea, cannot be regarded as having been brought within the fold of definition of "transfer" in section 2(47), by reason of what has been said and laid down in the case of Collis (supra).

19. It is well settled that the words and expression used in a judgment are not to be read as statutory provisions. Situations which did not arise for consideration and were, in fact, not considered are not to be regarded as having been considered. It is significant that the argument advanced for the revenue before the court in the case of Collis (supra) was not that the case of Vania Silk Mills (P) Ltd. (supra) was wrongly

decided. On the other hand, the argument before the court was that though that decision on facts was correct, certain observations which were not necessary for the case and which the revenue considered to be erroneous had been made, and were required to be overruled.

20. The law laid down in *Vania Silk Mills (P) Ltd.* (supra) that extinguishment of rights in a capital asset as a necessary consequence of destruction of the asset does not amount to transfer, has not been overruled by the Apex Court in the case of *Collis* (supra).

21. Our answer to the question referred is, therefore, in the negative, in favour of the assessee, and against the revenue.

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