

Union Of India vs Rajeswari And Co, & Ors on 15 July, 1986

Equivalent citations: 1986 AIR 1748, 1986 SCR (3) 175, AIR 1986 SUPREME COURT 1748, 1986 UPTC 1231, 1986 21 TAX LAW REV 197, 1986 SCC (TAX) 583, 1986 2 UJ (SC) 506, (1986) 27 TAXMAN 258, (1986) LS 112, (1986) JT 161 (SC), 1986 TAXATION 82 (2) 15, (1986) 161 ITR 60, 1986 (3) SCC 426, (1986) 3 SUPREME 366, (1986) 58 CURTAXREP 102

Author: R.S. Pathak

Bench: R.S. Pathak, Sabyasachi Mukharji

PETITIONER:

UNION OF INDIA

Vs.

RESPONDENT:

RAJESWARI AND CO, & ORS.

DATE OF JUDGMENT 15/07/1986

BENCH:

PATHAK, R.S.

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PATHAK, R.S.

MUKHARJI, SABYASACHI (J)

CITATION:

1986 AIR 1748	1986 SCR (3) 175
1986 SCC (3) 426	JT 1986 161
1986 SCALE (2) 6	

ACT:

Transfer of Property Act, 1882-s. 53-Applicability of-
Proceeds arising upon transfer of assets of an assessee
company employed fully in paying off some creditors-
Transaction whether invalid and inoperative-Transfer in
favour of a person not a creditor-validity of.

Constitution of India, Art. 136-Questions of fact-
Whether could be raised before the Court.

HEADNOTE:

A public limited company, working at a loss, having
come to know of the proposal of the Department to reopen its
income-tax assessments for the previous years, disposed of

its assets to the respondent firm, with which it had a partnership business, and employed the proceeds in paying off the debts due to various creditors, with the result that nothing was left for paying off the tax arrears of the company.

A suit under s. 53 of the Transfer of Property Act, 1882 was instituted by the Union of India-appellant for a declaration that the sale deed in favour of the respondent firm was invalid, inoperative and not binding on the appellant and other creditors of the transferor company and alleging fraudulent intent to defeat legitimate claims, which was decreed by the trial court. The High Court, however, allowed the appeal holding that the appellant had failed to satisfy the provisions of s. 53 inasmuch as the evidence showed that the company had utilised the proceeds arising upon the transfer of its assets in paying off all its other creditors, and that even if the company had done so in order to avoid payment of its income tax dues no relief could be granted to the appellant.

In this appeal by special leave it was urged for the appellant that the transfer was effected in favour of a person who was not a creditor, that the assets had been undervalued and that there was evidence to show that the benefit of the sale proceeds was enjoyed by the directors

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of the company, who were also partners of the respondent firm.

Dismissing the appeal, the court,

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HELD: It is open to a debtor to prefer one or more creditors over the others in the payment of his debts, and so long as he retains no benefit in the property the mere circumstance that some creditors stand paid while others remain unpaid, does not attract the provision of s. 53 of the Transfer of Property Act. [180A-B]

Musahar Sahu and Another v. Hakim Lal and another, L.R. 43 Indian Appeals 104, In re Moroney, [1888] L.R. 21 Ir. 27, 62, Middleton v. Pollock, [1876] 2 Ch.D. 104, 108 and MA PWA MAY and another v. S.R.M.M.A. Chettyar Firm, 56 Indian Appeals 379, referred to.

In the instant case, there was no finding by the High Court in support of the contention that some of the debts discharged were owed to persons who were also directors of the company or that the consideration which passed for the sale of the assets was inadequate and that the assets had been undervalued. This Court will not permit such questions of fact to be raised unless there is material evidence which has been ignored by the High Court or the finding reached by the Court is perverse. [180B-C]

It has been found by the High Court that the sale was effected for the purpose of discharging genuine debts payable by the company and that the sale proceeds were really employed for paying off the creditors of the company.

Once it was also found that the consideration was not inadequate, it was immaterial that the transfer was effected in favour of a person who was not a creditor. [180D-E]

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 1689 Of From the Judgment and Order dated 31st August, 1972 of the Madras High Court in Appeal No. 357 of 1965.

B.B. Ahuja and Ms. A. Subhashini for the Appellant. A.T.M. Sampath and P.N. Ramalingam for the Respondents. The Judgment of the Court was delivered by PATHAK, J. This appeal by special leave arises out of a suit instituted by the appellant for a declaration that a sale-deed of immoveable properties and the transfer of moveables belonging to the respondent limited company in favour of the respondent firm are invalid, inoperative and not binding on the appellant and other creditors of the respondent limited company.

A suit was instituted by the Union of India, the appellant before us, alleging that the Krishna Oil Mills and Industries Ltd., a public limited company registered under the Indian Companies Act, 1913 was carrying on business in the manufacture and sale of tin cans and aerated water. It entered into a partnership in September 1952 with Rajeswari and Co., which was carrying on business in the pressing of cotton bales. Under the partnership agreement Rajeswari & Co. was to install a cotton baling press in the buildings of the Company and the business would be carried on under the name Rajapalayam Cotton Pressing Factory, with the profits being divided between the Company and Rajeswari & Co. in the ratio of 7 to 9 respectively. This was replaced by another agreement in 1954, but the business was carried on in the same name and the profits divided in the same shares. It was alleged that the Company incurred losses in its own business year after year and from 1954 the only income derived by it flowed from the shares held by it in the partnership business. It was alleged that the Company had in fact ceased to carry on its own business, but in computing the income of the Company from the assessment year 1956-57 to the assessment year 1959-60 the losses suffered during the previous years from the Company's own business were allowed to be carried forward and set off against its share of income from the partnership Firm. Subsequently the Income- tax authorities decided to reopen the assessment proceedings under s. 34 of the Indian Income-tax Act, 1922 and, it is said, this was communicated to the Company. The processing of the case took time and the notices under s. 34 were issued for the different assessment years on March 6, 1961 and March 7, 1961. It was alleged that meanwhile, the Company, having come to know of the proposed re-opening of its income-tax assessments, began to dispose of its moveable and immoveable assets with a view to defeat the claim of the Union of India and to place the properties beyond the reach of the creditors of the company. The assets of the company were transferred in favour of Rajeswari & Co. and the sale proceeds were employed for paying off the debts due to various creditors who, it is said, included also the close relations and friends of the Directors of the Company. In the result, there was nothing left for paying off the tax arrears of the Company.

The suit was resisted by the Company, which in its written statement, admitted that it was working

at a loss for some years and was obliged to replace its original business of seed crushing and oil extraction by a more modest business activity, and in its circumstances it entered into a partnership with Rajeswari & Co. for carrying on the business of pressing cotton bales. It denied that when disposing of its assets it was aware of the intention of the income-tax authorities to reopen its assessments. It pleaded that because of action threatened by the Registrar of Joint Stock Companies in 1959 it was compelled to consider its position and to decide in a General Body meeting in June 1960 to dispose of the assets of the company. It was also stated that the partnership agreement of 1954 between the Company and Rajeswari & Co. stipulated that Rajeswari & Co., should have first preference if the Company proposed to sell its assets. The right of pre-emption was pressed by Rajeswari & Co. and, therefore, a resolution was passed in February 1961 at another Extraordinary Meeting of the Company to sell the lands and buildings at a valuation to be fixed by expert opinion. It was asserted that the assets were sold to Rajeswari & Co. and the sale proceeds were distributed to the creditors so that all the creditors were paid off.

Rajeswari & Co. also filed a written statement in opposition to the suit and besides asserting that it had installed cotton bale presses in the buildings of the Company pursuant to the partnership agreement between them it denied any fraudulent intent in purchasing the assets of the Company. It asserted that it acted in good faith and paid value for the properties.

The trial court decreed the suit on April 27, 1965. Rajeswari & Co. appealed to the High Court of Madras, and the High Court allowed the appeal, set aside the trial court decree and dismissed the suit. The High Court held in substance that the Union of India had failed to satisfy the provisions of s. 53 of the Transfer of Property Act inasmuch as the evidence showed that the Company had utilised the sale proceeds arising upon the transfer of its assets in paying off all its other creditors, and that even if the Company had done so in order to avoid payment of its income-tax dues no relief could be granted to the Union of India.

In this appeal it is urged for the Union of India that the transfer of assets was effected in favour of a person who was not a creditor, that the assets had been under-valued and that there was evidence to show that the benefit of the sale proceeds was enjoyed by the Directors of the Company who were also partners of Rajeswari & Co.

Section 53 of the Transfer of Property Act provides that every transfer of immovable property made with intent to defeat or delay the creditors of the transferor shall be voidable at the option of any creditor so defeated or delayed. A long line of cases has held that the preference by a debtor of one creditor over the others is not ipso facto deemed fraudulent, and reference may be made to *Musahar Sahu and Another v. Hakim Lal and Another*, L.R. 43 Indian Appeals 104 where the Judicial Committee of the Privy Council quoted *Palles C.B.*, who said in *In re Moroney* [1888] L.R. 21 Ir. 27, 62:

"The right of the creditors, taken as a whole, is that all the property of the debtor should be applied in payment of demands of them or some of them, without any portion of it being parted with without consideration or reserved or retained by the debtor to their prejudice. Now it follows from this that security given by a debtor to

one creditor upon a portion of or upon all his property (although the effect of it, or even the interest of the debtor in making it, may be to defeat an expected execution of another creditor) is not a fraud within the statute; because notwithstanding such an act, the entire property remains available for the creditors or some or one of them, and as the statute gives no right to rateable distribution, the right of the creditors by such act is not invaded or affected."

The Judicial Committee explained that "the transfer which defeats or delays creditors is not an instrument which prefers one creditor to another; but an instrument which removes property from the creditors to the benefit of the debtor. The debtor must not retain a benefit for himself. He may pay one creditor and leave another unpaid: *Middleton v. Pollock*. [1876] 2 Ch. D. 104, 108. So soon as it is found that the transfer here impeached was made for adequate consideration in satisfaction of genuine debts, and without reservation of any benefit to the debtor, it follows that no ground for impeaching it lies in the fact that the plaintiff who also was a creditor was a loser by payment being made to this preferred creditor-there being in the case no question of bankruptcy." This proposition of law was re-affirmed by the Judicial Committee subsequently in *MA PWA MAY* and another v. *S.R.M.M.A Chettyar Firm*, 56 Indian Appeals 379.

It seems clear that it is open to a debtor to prefer one or more creditors over the others in the payment of his debts, and so long as he retains no benefit in the property the mere circumstance that some creditors stand paid while others remain unpaid does not attract the provisions of s. 53 of the Transfer of Property Act. It is not disputed that the debts satisfied by payment of the sale proceeds are genuine. A faint attempt was made to show that some of the debts discharged were owed to persons who were also Directors of the Company. There is no findings by the High Court in support of that contention. It was also urged that the consideration which passed for the sale of the assets was inadequate and that the assets had been undervalued. Here again there is no finding to support the submission. The questions raised are questions of fact, and this Court will not permit such questions to be raised unless there is material evidence which has been ignored by the High Court or the finding reached by the Court is perverse.

A point was sought to be made by learned counsel for the appellant that the transfer of the assets was effected in favour of *Rajeswari & Co.* which was not one of the creditors. It has been found by the High Court that the sale was effected for the purpose of discharging the debts payable by the Company. Once it is also found that the consideration was not inadequate it is immaterial, as the High Court has observed, that the transfer was effected in favour of a person who was not a creditor. It has been clearly found that the sale proceeds were employed for paying off the creditors of the Company.

It appears that in consequence of the impugned transfer effected by the Company the appellant has been unable to recover a sum of Rs.28,240 assessed as income-tax in October 1961. It rested its suit on s. 53 of the Transfer of Property Act. Having regard to the findings rendered by the High Court on the consideration of material on the record and upon an interpretation of s. 53 which that provision has uniformly received this appeal cannot be sustained.

The appeal fails and is dismissed with costs.

P.S.S.

Appeal dismissed.