

IN THE HIGH COURT OF HIMACHAL PRADESH, SHIMLA

I.T.A No. 13 of 2004.

Date of decision: 26.8.2009

Commissioner of Income Tax, Shimla

Appellant

Versus

Panchratan Hotels Pvt. Ltd, Manali

Respondent

Coram:

The Hon'ble Mr. Justice Deepak Gupta, J.

The Hon'ble Mr. Justice V.K.Ahuja, J.

Advocate(s): For the appellant: Mr. Vinay Kuthiala, Advocate

For the respondent: M/s. K.D. Sood and Sanjeev Sood, Advocates.

JUDGEMENT

Deepak Gupta, J.(Oral):- This appeal has been admitted on the following substantial questions of law:-

“(i) Whether the sale of 100% share-holding of the Respondent Company to the New Management constitutes a ‘transfer’ as envisaged by Section 2(47) of the Income Tax Act, 1961 and would amount to succession of business.

(ii) Whether in the facts and circumstances of the case, the Ld. ITAT misconstrued and misinterpreted the material on record while coming to the conclusion that the expenditure incurred by the respondent on repairs and renovations was revenue expenditure and not capital expenditure.”

2. The facts of the case are that the assessee-M/s. Hotel Panchrattan is a Private Limited Company engaged in the business of running of a hotel at Manali. All the shares of this company belonged to the Kapoor family. The management of the company also vested with members of the Kapoor family. During the assessment year 1993-94, i.e., accounting year 1992-93, 100% shareholding of the company was sold by the Kapoor family to M/s.General Sales Limited on 31.7.1992.

3. The assessee filed a return of income declaring a loss. The Assessing Officer after computing the assessment under Section 144 of the Income Tax Act,1961 determined the loss at Rs.41,45,590/-. After the Assessing Officer finalized the return, the Commissioner of Income Tax exercising his powers under Section 263 came to the conclusion that the order passed by the Assessing Officer was erroneous. According to the C.I.T, there was 100 per cent transfer of shares from the Kapoor family to M/s. General Sales Limited on

31.7.1992. Therefore, it was a case of succession of business covered under Section 170 of the Income Tax Act. It further held that the assessment for the year 1.4.1992 to 30.7.1992 was required to be made in the hands of the old company and subsequent assessment from the period 31.7.1992 to 31.3.1993 in the hands of the new company.

4. The moot question which arises for consideration is whether the transfer of the shareholding would amount to transfer of business in terms of Section 170(1) of the Income Tax Act which read as follows:-

“170 (1) Where a person carrying on any business or profession (such person hereinafter in this Section being referred to as the predecessor) has been succeeded therein by any other person (hereinafter in this section referred to as the successor) who continues to carry on that business or profession-

(a) the predecessor shall be assessed in respect of the income of the previous year in which the succession took place up to the date of succession.

(b) The successor shall be assessed in respect of the income of the previous year after the date of succession.”

5. The Apex Court in Commissioner of Income Tax, Madras v. K.H. Chambers, ITR, Volume 55, 1965 considered the import of Section 25(4) of the Income Tax Act, 1922 which corresponds to the provisions of Section 170 of the Income Tax Act, 1961. It held as follows:-

“Succession involves change of ownership; that is, the transfer goes out and the transferee comes in; it connotes that the whole business is transferred; it also implies that substantially the identity and the continuity of the business are preserved. If there is a transfer of a business, any arrangement between the transferor and the transferee in respect of some of the assets and liabilities not with a view to enable the transferor to run a part of the business transferred but to enable the transferee to run the business unhampered by the load of debts or for any other appropriate collateral purpose cannot detract from the locality of the succession.

6. The expression “succession” has acquired a somewhat artificial meaning. The tests of change of ownership, integrity, identity and continuity of a business have to be satisfied before it can be said that a person “succeeded” to the business of another.”

7. It is apparent that to fall under the ambit of Section 170, there must be a transfer of ownership.

8. Sh. Vinay Kuthiala, learned counsel for the revenue contends that in view of the definition of transfer under Section 2(47) of the Act even a transfer of shares or the right to enjoy a capital asset is a transfer and by transferring the shares, there has been a

transfer in the right to use the capital assets of the company and, therefore, the case is covered under Section 170 of the Act.

9. Even if for the sake of arguments, we accept that the transfer of shares amounts to transfer of capital assets in terms of Section 2(47), then also in our considered view, Section 170 will not apply. A bare reading of Section 170 shows that the transfer of the business should be from one assessee to another. Person under Section 2(31)(iii) of the Income Tax Act includes a company. Under Company Law, a company is a juristic person. The share holders are not the owners of the company. It is the company itself which is its own owner having its own seal and succession. Where shares are transferred, at best this would be a transfer vis-à-vis, the person who was the holder of the shares to the person to whom the shares are transferred. Therefore, individually when Mr. Kapoor has sold his share to M/s.General Sales Limited then it may amount to a transfer when considering the incomes of Mr. Kapoor or M/s.General Sales Limited. Section 170 may be attracted to both the previous and subsequent owner of the shares but cannot apply to the company itself. This is no transfer as far as the assessee, i.e., M/s. Panchratan Hotel is concerned.

10. Reliance placed by Sh.Kuthiala on the judgment of the Apex Court in Commissioner of Income Tax v. Mrs.Grace Collis and others ITR (248) 2001 is misplaced. In that case there was amalgamation of companies and the share-holders of one company got shares of the other company. The value of the shares in the transferee company was much higher and the question arose whether the assesseees, i.e., individual share-holders were liable to pay capital gains tax or not. The Apex Court held that it is a transfer within the meaning of Income Tax Act and, therefore, the share-holders were liable to pay tax. It is obvious that the question was answered in relation to the share-holders and not in respect of the company. In the present case, we are concerned with the one assessee whose entire share-holding and management was transferred by one group of people to another.

11. The company is a juristic person having its distinct legal entity separate from that of the shareholders. The change in the share-holders of the company does not change the legal identity of the company.

12. Therefore, Section 170 had no application to the facts of the case. Reliance in this behalf may be placed on the judgment of the Allahabad High Court in Commissioner of Income Tax v. Mass Products (Ind.) Ltd. ITR 221, 1996 wherein it was held as follows:

“In our opinion, the first question referred to us has to be answered in the negative and against the Department because it is settled law that a limited liability company is a distinct legal entity separate from its shareholder. Change in the shareholders of the company does not change the legal identity of the company. A limited liability company is thus different from a partnership-firm because while a company is distinct from its shareholders and directors, a partnership-firm is not different from its partners and it is not a distinct legal entity. Since the assessee is a limited liability company change in the ownership of its shares will have no effect on the legal identity of the company.”

13. We are in respectful agreement with the observation of the Allahabad High Court. In view of the above discussion, we find no merit in the appeal which is dismissed and both the questions are answered in favour of the assessee.

No order as to costs.

(Deepak Gupta)

Judge

August 26, 2009

(m) Judge

(V.K.Ahuja)