A PERSONAL TRIBUTE TO A TRULY BRILLIANT JUDGE – LATE CHIEF JUSTICE(RETD.) SAROSH HOMI KAPADIA.

In my brief tenure as a lawyer which continues to subsist I, as any other lawyer, have read and re-read judgments and binding precedents either for a matter which is ready for hearing, or for the purpose of writing an article, or just to make time worthwhile. But there are a few tax judgments which I specially took note of, not for their length and breadth, neither for their rhetoric and if I may say so neither for their over simplicity, but for the style, choice of words, and the ultimate decision reached in the process, which process to my mind was simply par excellence. I doubt with a heavy heart that we may ever have such a judge who has literally given us a fresh look at the way the law is to be laid down and interpreted. This judge is none other than late Chief Justice of India(retd.) Sarosh Homi Kapadia.

I have not had the good fortune of meeting, or appearing in Court before Mr. Kapadia, and the real inspiration for this tribute is borne out of reading his various judgments. I decided that I must do my best to make some of the judgments well known in the public domain and that would amount to a token of personal satisfaction.

Late Justice(retd.) S.H. Kapadia was born on September 29, 1947 and went on to become the 38th Chief Justice of India. He graduated from Government Law College, Mumbai which is the oldest law college in Asia. Mr. Kapadia started his career as a class IV employee. He later became a law clerk in a lawyer's office in Mumbai. He joined Gagrat & Co., a law firm, as a clerk and later went on to work with Feroze Damania who was a highly respected "firebrand" labour

lawyer. He later joined as an advocate in the Bombay High Court on 10 September 1974.[1]

Mr. Kapadia was appointed as an additional judge of the Bombay High Court on 8 October 1991 and on 23 March 1993 he was appointed as a permanent judge. On 5 August 2003 he became the Chief Justice of the Uttarakhand High Court. On 18 December 2003 he was appointed as a judge of the Supreme Court. On 12 May 2010 he was sworn in as the Chief Justice of India by the then President Pratibha Patil. He retired on 29 September 2012. During his tenure as Chief Justice he was the Chairman of the General Council of the Gujarat National Law University and the Visitor of the National Law School of India University.[2] Mr. Kapadia sadly passed away on 4th January, 2016 at the age of 68.

In 2016, a book titled Interpretation of Taxing Statues-Frequently Asked Questions was released on the completion of both 50 years of the ITAT Bar Association and 40 years of the All India Federation of Tax Practitioners. The book was dedicated to the fond memory of Late Justice S.H Kapadia. Many renowned and distinguished persons in the field of tax penned messages and paid tributes to Mr. Kapadia.

In this Article, I will be closely examining the law laid down in the judgments of late Mr. S.H. Kapadia and I recommend that the readers of this Article also read the full text of these judgments.

1. *Reopening of assessments: Can it be done on a mere change of opinion?*

[1] https://en.wikipedia.org/wiki/S._H._Kapadia
[2] https://en.wikipedia.org/wiki/S._H._Kapadia

- In CIT vs. M/s. Kelvinator of India Limited[3], the short question involved in the appeals before the Supreme Court was, whether the concept of change of opinion stood obliterated w.e.f 1st April, 1989 i.e after substitution of Section 147 of the Income Tax Act, 1961 by the Direct Tax Laws(Amendment) Act, 1987? In other words, did the Department have power to reopen assessments on a mere change of opinion?

- The judgment answers the above question in the briefest terms possible(barely 2-3 pages). The analysis is excellent and it showcases the brilliant mindset of the judge. It speaks louder than words:
- Mr. Kapadia notes that the power to reassess prior to the Direct Tax Laws (Amendment) Act, 1987(and till 1st April, 1989)were hedged with two conditions precedent to the exercise of that power. However, after the Amending Act, 1989, w.e.f 1st April, 1989 there is only one condition which subsists i.e whether the Assessing Officer has reason to believe income has escaped assessment. Therefore, the power post 1st April, 1989 was much wider to reassess(in the absence of any condition precedent for the exercise of the power).

  Thus, the Assessing Officer has power to 'reassess' under Section 147 not the power to 'review'. If the concept of change of opinion as was contended by the Department is removed, it would amount to giving arbitrary powers to the Department to reopen assessment proceedings already concluded since in the garb of reassessment, review would take place. Thus, the concept of 'change of opinion' is an in-built test to check abuse of power by the Assessing Officer.

[3] (Civil Appeal 2009-11/2003 decided on January 18, 2010)

Therefore, post 1st April, 1989, there must be some tangible material to show income has escaped assessment. The reasons must have a live link with the formation of the belief.

- Mr. Kapadia notes that vide the Direct Tax Laws(Amendment) Act, 1987 the words reason to be believe was removed and the word opinion was substituted but due to various representations from Companies, the said expression reason to believe was re-introduced on the ground of the arbitrariness associated with the words change of opinion, by the Amending Act of 1989.
- The appeals were dismissed as meritless.

2. *Is the loss which has accrued on dividend stripping transactions liable to be disallowed in view of Section 94(7) of the Act? Is there any expenditure incurred with respect to exempt income in such dividend stripping transactions?*

- In CIT vs. Walfort Share & Stock Brokers (P.) Ltd.[4], the question before the Supreme Court was whether losses arising on dividend stripping transactions was disallowable when such transaction(in view of the Assessing Officer) was not a business transaction? The facts of the case in brief are that the assessee invested in a Mutual Fund which advertised that tax free dividend income of 40% could be earned if assessee invested in its units on or before 24-3-2000. The assessee-respondent purchased units on that very date and was entitled to a dividend. The NAV of the units fell as a result of the dividend payout to the assessee, and the assessee then sold the units at a capital loss and claimed to set off the loss against its income thereby reducing its overall tax liability. The Revenue was aggrieved with the fact that the assessee claimed dividend income as exempt

[4] [2010] 326 ITR 1 (SC)

under Section 10(33) of the Act and at the same time claimed a set off of losses which in its view was impermissible. Mr. Kapadia noted the following:

(i) The Assessment Year was 2000-2001. Section 94(7) of the Act which provides for disallowance of losses in precisely such situations was not retrospective owing to the fact that a large number of assesses in the past had undertaken such dividend stripping transactions. Section 14A and Section 94(7) of the Act both were introduced by the Finance Act, 2001 and although Section 14A was made retrospective, if the same treatment was afforded to Section 94(7), it would amount to a reversal of a large number of transactions already finalised. Hence, keeping in mind the intention of the law giver, the provision was held to be prospective thereby not affecting the transaction undertaken by the assessee in the present case.

(ii) An assessee may devise a plan for payment of tax and as long as such plan is within the four corners of the law, the assessee cannot be held liable to pay income tax when the only allegation is that such a transaction is a 'colourable device'.

(iii) A return of investment is not expenditure within the meaning of Section 14A of the Act and cannot be disallowed.

Keeping in mind the above, the Court upheld the decision of the Bombay High Court and dismissed the appeals of the Revenue.

3. *When is a sale of assets a slump sale or an itemised sale of assets?*

In *Premier Automobiles Ltd. vs. ITO & Ors.*[5], the Bombay High Court dealt with a case of whether a transaction of hiving off an undertaking constituted a slump sale or an itemised sale of assets.

[5] [2003] 264 ITR 193(Bom)

The Assessment Year in question was 1995-1996. At that point of time, there was no provision in the Act dealing with slump sale but the concept had evolved through judge made law. The facts in brief were that the assessee company PAL was in the business of manufacturing cars and had hived off its Kalyan undertaking to a joint venture company(KMCL renamed PPL) set up by PAL and another foreign company(AP) interested in doing business with the assessee company, i.e PAL. The entire undertaking had been hived off for a consideration of 210 crores plus net current assets through various agreements namely an MOU, Supplemental MOU, Slump Sale Agreement. The Assessing Officer treated the transaction as a sale of itemised assets and apportioned the sale price of each asset against the consideration receivable by the assessee from the transferee JV company. The Bombay High Court speaking through Justice Kapadia has given detailed reasons why the said transaction was a slump sale and not a sale of itemised assets where the sale price of each asset could be apportioned with the total consideration. The findings are as follows:

(i) The decisive test is whether the hiving off has resulted in continuity of business. Also, whether the assets that have been transferred are the entire business or individual assets. In the present case, the entire undertaking had been transferred and therefore, this requirement is satisfied.

(ii) Whether the transfer of the undertaking was for a lump sum price? If not, then the transaction cannot be regarded as a slump sale. The sale has to be for a lump sum price.

(iii) In the present case, there was a schedule of assets, a register of fixed assets. Not only land and building but the entire undertaking was transferred including licences, quotas etc. Therefore, the transaction met the requirement of a slump sale.

(iv) It cannot be said that no liabilities were transferred. Whilst examining whether liabilities have been transferred one has to take into account commercial principles. For example, just because the paint shop(being under construction) and being a liability was not transferred does not mean that it ceases to be a liability which has been transferred. There was an option with the assessee company to discharge the said liability with the contractor after the construction had been carried out and receive the full amount of consideration or transfer the liability beforehand and receive a lesser consideration. Either way, it amounts to the same thing and amounts to a transfer of liability. Another example is that the assessee company has to obtain an NOC from its lenders before it assigns its loans. This results in additional interest being charged by the lenders. PPL/KMCL agreed to reimburse PAL towards this additional interest, therefore, it cannot be said that there was no transfer of liabilities.

(v) It cannot be said that no plant and machinery was transferred and this finding of the Tribunal is erroneous since without such transfer of machinery there could not be a turnover of approx. 177 Crores. Hence, even this finding goes to show that the entire undertaking was transferred for a lump sum price.

(vi) Another erroneous finding is that since the entire land was not transferred, there was no slump sale. The piece of land on which the Kalyan factory was situated was transferred entirely and the remaining portion of the land consisted of a road and wall. Hence, it cannot be said that the 'entire' land has not been transferred since the assessee company has transferred its whole entitlement.

(vii) Even the finding that there were no separate accounts for the Kalyan business is errorneous. General ledgers have been produced for FY 1994-1995 showing sale of cars.

(viii) The entire Kalyan business has been sold as a going concern and this constitutes a slump sale.

These are the findings of the learned judge, to name a few, in this erudite judgment, which is a leading authority on cases of slump sale even today. It has been followed in a recent judgment of the Supreme Court in Equinox Solutions[6] where the principle that if an entire undertaking is transferred, it will constitute a slump sale of long term capital assets was upheld(*Exception: short term capital assets: See proviso to Section 50B*).

4. *Is capital gains tax to be paid when a transaction takes place between three foreign companies only because the company whose shares are to be transferred holds shares of a company located in India?*

In Vodafone International Holdings BV vs. Union of India and Anr.[7], the issue before the Supreme Court was whether the transfer of shares of a foreign company located in the Cayman islands(company 'A')-holding 67% shareholding in company 'D', undertaken by two foreign companies, one as vendor also located in the Cayman islands('B') and another as the purchaser being an offshore company('C') would invite capital gains tax for the reason that company A held underlying Indian assets of company D, a company located in India? Thus, whether the amount received by company B as vendor of the share sale was income such that company C had to deduct TDS from the amount paid to company B?

[6] CIT vs. Equinox Solution Pvt. Ltd. Civil Appeal 4399 of 2007 decided on 18.4.2017
[7] 2012 6 SCC 613

The stand of the Revenue was that since company A had underlying assets(shareholding) of a company located in India(company D), the transfer of its(company A's) share capital must be deemed to be transfer of company D's shares which has assets located in India OR that the only intent of company C was to acquire 67% stake in company D through the transfer of company A's shares.

The following was noted by Justice Kapadia:

i) The Revenue must adopt the look at principle, i.e to examine a transaction holistically and not with a dissecting approach. Thus, when shares are sold lock stock and barrel, the transaction cannot be broken up into individual components or be dissected.
ii) The parent company may have control over the subsidiary but there is a difference between actual dominant control and persuasive control of the subsidiary. It is only the former which can warrant further examination into the bona fides of the transaction i.e whether the transaction is a genuine or sham transaction.
iii) The real purpose behind the acquisition of the share capital of company A by company C was the acquisition of the business of downstream companies including that of company D of which company A held 67% share capital.
iv) The sale was purely a share sale and not a sale of assets, a sale may be in a variety of forms and a share sale is not the same as an asset sale and hence tax consequences will vary.
v) One of the chief elements of Section 9 is that the capital asset which is transferred must be situated in India, failing which the capital gain cannot accrue in India. Section 9 is divided into four situations when tax can said to accrue in India and neither of them are dependent on each other such that one and another must be satisfied in order to attract tax, but are separate. The last element i.e 'capital asset situate

in India' was introduced to plug the loophole of income not accruing in India.

vi) The group of companies have in the past paid over 20,000 crore rupees of tax and it cannot be said that the group structure was a tax avoidance set up or scheme designed to evade payment of tax.

The appeals were allowed.

5. *Is capital gains tax liable to be paid on additional compensation received even though the amount of additional compensation was challenged in appeal?*

In CIT vs. Ghanshyam[8], the Assessment Year was 1999-2000. The Supreme Court was faced with the issue of chargeability of capital gains tax on enhanced compensation/additional compensation received pursuant to compulsory acquisition of land when such enhanced compensation as ordered by the Reference Court was under challenge in appeal before the High Court by the State authority which had granted the compensation.

The assessee did not offer to tax the enhanced compensation since the amount it averred was under dispute in appeal before the High Court. Mr. Kapadia noted the following:

(i) The purpose behind introduction of Section 45(5) of the Act was precisely to meet the situation where compensation is awarded in various stages by various appellate authorities. Thus, enhanced compensation is to be taxed only in the year of receipt whereas the

[8] [2009] 315 ITR 1(SC)

compensation originally awarded is to be taxed in the previous year when the transfer took place(or was first received).

(ii) On a perusal of Section 23(1A), 23(2), 28, and 34 of the Land Acquisition Act, 1894 it is amply clear that though interest is different from compensation, the interest under Sections 23(1A) and 28 and solatium under Section 23(2) is an accretion to the compensation and hence part of the compensation chargeable to tax under Section 45(5) of the Act. However, Section 34 is only for delay in making payment of compensation and cannot form part of the compensation, therefore, cannot be included in the total income. Thus, the amount mentioned under Section 23(1A) of the 1894 Act, i.e interest awarded @12% on the market value of land from the date of notification till date of possession or date of award whichever is earlier, Section 23(2), i.e an award of solatium @30% on the market value of land and Section 28, i.e interest @ 9% on excess payment directed by a court or tribunal when the amount awarded by the collector is not sufficient form part of Section 45(5) and are to be taxed as enhanced compensation in the previous year when these amounts are received.

(iii) Therefore, on a perusal of Section 45(5) read with sections 23(1A), 23(2) and 28, the enhanced compensation is to be taxed in the year of receipt and the amount was admittedly received by the assessee in FY 1999-2000. The conclusion is further fortified by the fact that if the compensation is reduced by the appellate authority, provision is made under Section 155(6) of the Act to direct modification of the assessment order by stating the reduced compensation only as the full value of consideration. Hence, the enhanced compensation is to be taxed in the year 1999-2000 when it was received.

6. *Does interest under Section 244A of the Act have to be paid mandatorily when the principal tax to be refunded is TDS?*

   In CIT vs. H.E.G Ltd.[9], Justice Kapadia noted that the issue in the case was not of granting interest on interest, but whether the assessee was entitled to interest under Section 244A of the Act for delay in refunding TDS deposited with the Department and refunded after a delay of 57 months. The Department contended that the words 'amount due' occuring in Section 244A of the Act would not include the interest component. However, Justice Kapadia saw no merit in the contention and for obvious reasons, inasmuch as when tax is liable to be refunded, interest is liable to paid on the principal amount of tax for delay in the payment of the tax. Justice Kapadia noted that the interest became an integral part of the principal and was liable to be refunded. The very intendment of the legislature in enacting Section 244A was to grant interest for delayed refunds and this was upheld by Justice Kapadia in the present case. Thus, the Department was to refund the principal amount of TDS along with interest to be calculated as per Section 244A of the Act.

INDIRECT TAXATION

1. In Electronics Corporation of India vs. Union of India[10], Mr. Kapadia held that *inter se* disputes to be decided by a High Power Committee later known as a Committee on Disputes between the entities of the State as decided to be constituted by the orders in ONGC vs. Collector of Central Excise was no longer good law as the said Committee had outlived its purpose inasmuch as though the object

[9] (2010) 15 SCC 349
[10] [2011] 30 STT 472 (SC)

of forming the Committee was laudable(i.e there must be a conciliation mechanism through a committee to decide disputes between the entities of the States), the Committee could no longer subsist when the stakes were enormous and there was loss of revenue.

2. In AIFTP vs. Union of India[11], Mr. Kapadia upheld the constitutional validity of service tax on Chartered Accountants and Cost Accountants and the legislative competence of Parliament to impose service tax under Article 246(1) of the Constitution of India.

OTHER NOTABLE TAX JUDGMENTS

1. In CIT vs. Smifs Securities Ltd.[12], Mr. Kapadia upheld the claim of depreciation on goodwill as an intangible asset by applying the rule of *ejusdem generis* to Explanation 3 to Section 32 of the Act as it stood for Assessment Year 2003-2004.
2. In CIT vs. Ponni Sugars & Chemicals Ltd.[13], Mr. Kapadia upheld the 'purpose test' in relation to subsidies. Whether a subsidy is on revenue or capital account was to be decided by looking at the purpose/object for which the subsidy was given. In this case, the subsidy was given for repayment of term loans, hence it was on capital account. The source of the subsidy and its utilisation were factors that were irrelevant.
3. In T.R.F Ltd. vs. CIT[14], Justice Kapadia noted that it was sufficient that the bad debt was written off as irrecoverable in the

[11] [2007] 9 VST 126 (SC)
[12] [2012] 348 ITR 302 (SC)
[13] [2008] 306 ITR 392 (SC)
[14] [2010] 323 ITR 397 (SC)

books of account of the assessee and it was not necessary for the assessee to prove that the debt was in fact irrecoverable.

CONCLUSION

I have elaborated on a few notable judgments delivered by late Justice(retd.) S.H Kapadia and even while reading the judgments for the purpose of elaboration, one aspect is clear that the enormity of hard work coupled with presence of mind of the learned judge is outstanding. The eye for detail and the comprehensiveness of the judgments is unique. It has been a great pleasure in preparing this tribute to a truly brilliant judge one who is no more but cannot be forgotten.