A ADMINISTRATOR, UNIT TRUST OF INDIA

v.

B.M. MALANI AND ORS.

OCTOBER 11, 2007

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[S.B. SINHA AND H.S. BEDI, JJ.]

Income Tax Act, 1961—s. 226(3)—Interpretation of—Assessee defaulter of payment of income tax—UTI holding units under the C *Scheme on assessee's behalf—Income Tax Department issuing notice to UTI raising demand on account of income tax penalty by assessee—UTI selling units below par without assessee's consent and making part payment—High Court holding units to be redeemed at par—Correctness of—Held: UTI could not have transferred the amount, in* D *absence of any right of option of repurchase of units having been exercised by assessee—s. 226(3)(vi) cannot be interpreted to mean that UTI was fully authorised to dispose of the units on its own—UTI could hold the amount only when assessee had exercised his option—More so, assessee made sincere efforts to pay tax—Thus, assessee to be* E *restituted with the dividend declared on the amount.*

Respondent-assessee invested Rs. 65 lakhs in Monthly Income Plan of Unit Trust of India under Capital Gains Scheme in 1998 to seek exemption under section 54AE of the Income Tax Act, 1961. The capital invested in the scheme was protected on maturity. The F **face value of the units was Rs 10/- and the units were not to be redeemed below par. Respondent defaulted in payment of income tax. Income Tax Officer issued notice to the appellant-Unit Trust of India under section 226(3) of the Act raising a demand of Rs. 48,08,000/- from the amount held by UTI for or on account of** G **assessee, regarding the income tax penalty imposed on the respondent. Appellant calculated the unit price at the rate of Rs. 6.93 per unit and paid Rs. 43, 69,083.30 to the Department. Though the units were transferred, their value had not become due to the assessee on the date on which such notice was given. Respondent**

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filed writ petition challenging the action of the appellant in resorting to sale of the units without his consent. High Court held that the respondent was entitled to the redemption value of the units at the rate of Rs. 10/- per unit after five years. Hence the present appeals.

Appellant-UTI contended that the respondent being a defaulter and the appellant having been holding the units on its behalf, the High Court erred in passing the impugned judgment; that the units were transferable on the day on which the payments were made and keeping in view the purported tenor of the notice in terms whereof the appellant was to be treated as assessee-in-default, it had no other option but to make payment.

Dismissing the UTI's appeal and allowing assessee's appeal, the Court

HELD: 1.1 Section 226(3) of the Income Tax Act, 1961 would be applicable only when a money is due to the assessee from any person. Clause (vi) of sub-section (3) of Section 226 of the Act in categorical terms created a legal fiction to the effect that when an amount is not payable, the assessee is not required to pay any such amount or part thereof. [Paras 13 and 16] [1147-A; 1148-E]

2.1. Appellant is a statutory authority. It had floated the Capital Gains Scheme. The scheme constituted a contract between the parties. Under the Scheme the lock-in period was for five years. The repurchase was allowed only from 1st September, 2001. Indisputably, the respondent did not opt therefor. In absence of any right of option having been exercised by the respondent, the appellant, could not have transferred the amount in question. It is wholly incorrect to contend that the scheme itself provided that repurchase was allowed from 1.9.2001 even without the consent of the respondent. It was for the respondent to give his option. The Income Tax Officer could not have exercised the said option on behalf of the assessee. The stand of the Income Tax Department also was that it sought to attach the units and did not opt for the repurchase value at that point of time.

[Paras 15] [1147-B, C, D; 1148-B]

A 2.2. Respondent was a defaulter to the extent of Rs. 157.77 lacs. He sold some of the properties. A portion of sale proceeds, Rs. 65 lakhs had been invested with the appellants under the units. He filed an application for settlement before the Settlement Commissioner. He had deposited a sum of Rs.25 lacs when moving an application B for deposit of the amount. Upto October 2000, he had already paid a sum of Rs.92.04 lacs. Only a sum of Rs.48,08,000/- was due from him and with regard to the same he sought time for payment.

[Para 12] [1146-A, B, C]

C 2.3. Respondent made all sincere efforts to pay the tax. It made an offer to the Income Tax Officer to transfer the bonds at their face value at Rs.10/- per unit. Unfortunately, the Income Tax Department neither replied to the said letter nor paid and heed to his request. Respondent had invested a sum of Rs.65 lacs. Therefore, he was entitled to, at least, that amount. Government of India had already D been considering the matter of reimbursement to the holders of the units at least at the purchase rate. Thus, it not only acted hastily but also illegally. As a State, within the meaning of Article 12 of the Constitution, it was required to exercise restraint and give effect to the provisions of the contract in a reasonable manner. Appellant E being a statutory authority should have acted strictly in terms of the conditions of the contract. It was to act reasonably and fairly.

[Para 16] [1148-C, D, E]

2.4. Section 226(3)(vi) cannot be interpreted to mean that the F Unit Trust of India was fully authorised to dispose of the units on its own without any notice to the holder of the units. In a situation of this nature, having regard to sub-section (3) of Section 226 of the Act, it cannot be said that the appellant was holding the money of the respondent. The amount in question could have been held by the G appellant only when the respondent had exercised his option therefor. [Paras 18 and 19] [1148-G; 1149-A-B]

2.5. Respondent No.1 never authorised the Unit Trust of India to sell the same in the market at the lower price as respondent No.1 has stated in his letter that due to the fall in the prices in the market, H he was not able to dispose of the units. Respondent No.1 further

prayed time till May 2002 to clear the dues and was awaiting information from Respondent Nos.2 and 3 but in the meantime the petitioner sold the same in the market without any intimation to respondent No.1. Therefore, there is no error in the judgment of High Court as the respondent is entitled to be restituted. Respondent was also entitled to dividend declared during the said period viz. from the date of allotment. The High Court was not correct in not considering that aspect of the matter.

[Paras 17 and 23] [1148-F, G; 1150-E, F]

Life Insurance Corporation of India and Anr. **v.** *Gangadhar Vishwanath Ranade (dead) by Lrs.,* **[1989] 4 SCC 297, distinguished.**

Vysya Bank Ltd. **v.** *Joint Commissioner of Income Tax,* **241 ITR 178, referred to.**

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 4792 of 2007.

From the Judgment and final Order dated 27.8.2004 of the High Court of Judicature of Andhra Pradesh at Hyderabad in Writ Petition No. 23025 of 2002.

WITH

C.A. Nos. 4793-4799 of 2007.

M.L. Verma, Sanjay Kapur, Shubhra Kapur and Rajiv Kapur for the Appellant.

R.G. Padia, D.K. Singh, Pradeep Shukla, B.V. Balaram Das and S.V. Deshpande for the Respondents.

The Judgment of the Court was delivered by

S.B. SINHA, J. 1. Leave granted.

2. Interpretation of sub-section (3) of Section 226 of the Income Tax Act, 1961 (Act) is involved in these appeals which arises out of a judgment and order dated 27.8.2004 passed by the High Court of Judicature of Andhra Pradesh at Hyderabad in Writ Petition No.2305

of 2002 whereby and whereunder the writ petition filed by B.M. Malani (hereafter referred to as the respondent) was allowed in part.

3. Respondent is an assessee of income tax. He was admittedly a defaulter in payment of income-tax. He had invested an amount of 65 lacs in the Monthly Income Plan (III) offered by the Unit Trust of India under Capital Gains Scheme, the predecessor in interest of the petitioner in the year 1998 with an object to seek exemption under Section 84-E of the Act. The 'Highlights' projected for such an offer were as under :

* "A five year close ended income plan
* The plan offers three options 1) Monthly Income Option, 2) Annual Income Option & 3) Cumulative Option
* The face value of a unit is Rs.10/- and units will be sold at par.
* The Trust shall pay an assured income @ 12.50% p.a. payable monthly under monthly income option and @ 13.25% p.a. payable annually under annual income option, for all the five years of the plan.
* Under the Monthly Income Option, income distribution warrants for the period upto March 1999 will be sent along with the membership advice/unit certificate. Thereafter income warrants payable monthly will be sent in advance for every April-March period.
* Repurchase allowed from 1st September, 2001 at NAV based repurchase price under all the three options.
* Scheme shall be listed on the whole sale debt segment of the NSE within six months from the closure of subscription.
* It is guaranteed that the capital invested in the scheme will be protected on maturity i.e. units will not be redeemed below par. The Development Reserve Fund (DRF) of the Trust will guarantee this capital protection. There is no such guarantee for premature repurchases and the repurchase price in such cases will be as per prevailing NAV. There is scope for capital

appreciation as a part of investment will be in equities.

* Tax benefits under Section 80L and Sections 48 and 112 of Income Tax Act, 1961 on income distributed and capital gains from capital appreciation. Capital gains tax exemption under Section 54EA of the Income Tax Act, 1961 subject to lock-in for three years from the date of acceptance."

4. Appellant received a notice from the Income Tax Department purported to be under sub-section (3) of Section 226 of the Income Tax Act. In compliance of the demand made therein, a sum of Rs.43,69,083.30 p. was paid to the Department by the appellant wherefor, the value of the unit at the relevant time was calculated at the rate of Rs.6.93 p. per unit.

5. Respondent herein filed a writ petition questioning the said action of the appellant in resorting to sale of the said units without his consent.

6. Admittedly, although the units were transferred, their value had not become due to the assessee on the date on which such notice was given. It was held by the High Court that the respondent was entitled to the redemption value of the units at the rate of Rs.10/- per unit after five years.

7. Appellant is, thus, before us. An appeal has also been filed by the respondent contending that the dividend declared on the said amount also should have been directed to be paid by the High Court.

8. Mr. M.L. Verma, learned senior counsel appearing on behalf of the appellant, would submit that the respondent being a defaulter and the appellant having been holding the units on its behalf, the High Court committed a serious error in passing the impugned judgment. The learned counsel urged that admittedly the units were transferable on the day on which the payments were made and keeping in view the purported tenor of the notice in terms whereof the appellant was to be treated as an assessee-in-default, it had no other option but to make payment.

9. Mr. Deshpande, learned counsel appearing on behalf of the respondent, on the other hand, would support the impugned judgment.

10. Sub-section (3) of Section 226 of the Act reads as under :

"(3)(i) The Assessing Officer or Tax Recovery Officer may, at any time or from time to time, by notice in writing require any person from whom money is due or may become due to the assessee or any person who holds or may subsequently hold money for or on account of the assessee to pay to the Assessing Officer or Tax Recovery Officer either forthwith upon the money becoming due or being held or at or within the time specified in the notice (not being before the money becomes due or is held) so much of the money as is sufficient to pay the amount due by the assessee in respect of arrears or the whole of the money when it is equal to or less than that amount.

(ii) to (v)

(vi) where a person to whom a notice under this sub-section is sent objects to it by a statement on oath that the sum demanded or any part thereof is not due to the assessee or that he does not hold any money for or on account of the assessee, then nothing contained in this sub-section shall be deemed to require such person to pay any such sum or part thereof, as the case may be, but if it is discovered that such statement was false in any material particular, such person shall be personally liable to the Assessing Officer or Tax Recovery Officer to the extent of his own liability to the assessee on the date of the notice, or to the extent of the assessee's liability for any sum due under this Act, whichever is less."

11. Indisputably, a notice was issued by the Income Tax officer upon the Branch Manager of the Unit Trust of India wherein, *inter alia*, it was stated :

"A sum of Rs.48,08,000/- is due from B.M. Malani of Hyderabad on account of Income-tax penalty. You are required hereby under Section 226(3) of the Income-tax Act, 1961 to pay to me forthwith any amount due from you to or, held by you, for or on account of the said assessee upto the amount of arrears shown above.

2. I also request you to pay any money which may subsequently become due from you to him/them or which you may subsequently hold for or on account of him/them upto the amount of arrears still remaining unpaid, forthwith on the money becoming due or being held by you as aforesaid.

3. Any payment made by you in compliance with this notice is in law deemed to have been made under the authority of the said assessee and my receipt will constitute a good and sufficient discharge of your liability to the person to the extent of the amount referred in the receipt.

4. Please note that if you discharge any liability to the assessee after receipt of this notice you will be personally liable to me as Assessing Officer/Tax Recovery Officer to the extent of the liability discharged, or to the extent of the liability of the assessee for tax/ penalty interest/fine referred to in the preceding para, whichever is less.

5. Further, if you fail to make payment in pursuance of this notice, you shall be deemed to be an assessee in default in respect of the amount specified on this notice and further proceeding may be taken against you for the realisation of the amount as if it were an arrear of tax due from you in the manner provided in Section 222 to 225 of the Income Tax Act, 1961 and this notice shall have the same effect as an attachment of a debt under Section 222 of the said Act.

6. The necessary challan(s) for depositing the money to the credit of the Central Government is/are enclosed.

7. A copy of this notice is being sent to the afore-mentioned assessee."

12. Whether the action on the part of the appellant to act thereupon was valid, is the question. The scheme, the relevant provision whereof had been noticed by us hereinbefore, goes to show that the lock-in period was for a period of five years. Purchase of the units, however, was allowed from 1st September, 2001 at NAV based repurchase price. The scheme

A constituted a contract between the parties. The option of the purchase was to be exercised by the respondent. Appellant, on the basis of the said purported notice dated 8.2.2002, could not have placed itself in the shoes of the respondent. It is not in dispute that the respondent was a defaulter to the extent of Rs.157.77 lacs. He had sold some of his
B properties in 1998. A portion of the sale proceeds, namely, 65 lacs had been invested with the appellant. He had sought for exemption under Section 54AE of the Act. The amount of 65 lacs was secured under the said units with the appellants. It is not in dispute that an application for settlement was filed before the Settlement Commissioner by the
C respondent. He had deposited a sum of Rs.25 lacs when moving an application for deposit of the amount. Upto October 2000, he had already paid a sum of Rs.92.04 lacs. Only a sum of Rs.48,08,000/- were due from him. He, therefore, in his letter dated 4.2.2002 stated as under :

> "Sale of Bonds at present would result in a loss of Rs.3 per unit
D which will be about 30% loss and it would be difficult to bear such loss while the taxes are pending payment. In the event the Bonds are sought to be acquired by the Department, I shall transfer them at its face value at Rs.10/- per unit against taxes although I am voluntarily making the tax payments as per commitments.
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> In the above facts and circumstances, with a great constrains I had paid tax Rs.25.00 lakhs on 31.1.2002 as committed by me in my petition dated 26.10.2001 although I had sought time for above payment till the end of February 2002. It may also be submitted
F that I had sold my property for the purpose of payment of taxes and opted an additional tax burden of Rs.35.00 lakhs under the Settlement Commission Orders and Co-operated with the Department. In the circumstances, I request you sir to grant time for payment of balance tax till the end of May 2002 as I am given to understand after the budget is presented, the capital gains Bonds
G issued by Unit Trust of India are likely to be purchased by the Government at par @ Rs.10/- per Unit in which case I will not suffer loss on sale and the market rate for sale of such units will also go up. The department was good enough to grant time earlier for payment of tax and I have kept my commitments at all the times
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and accordingly paid the tax." A

13. Sub-section (3) of Section 226 of the Income Tax Act would be applicable only when a money is due to the assessee from any person. Was the amount due to the assessee when the notice dated 8.2.2002 was issued is the question? B

14. Appellant is a statutory authority. It had floated the scheme. It knew the terms and conditions thereof. On a plain reading of the highlights of the scheme, relevant provisions whereof have been noticed by us hereinbefore, it is evident that repurchase was allowed only from 1st September, 2001. Indisputably, the respondent did not opt therefor. In C absence of any right of option having been exercised by the respondent, the appellant, in our opinion, could not have transferred the amount in question. It is wholly incorrect to contend that the scheme itself provided that repurchase was allowed from 1.9.2001 even without the consent of the respondent. It was for the respondent to give his option. The Income D Tax Officer could not have exercised the said option on behalf of the assessee. Curiously, the Income Tax Department itself, in its counter affidavit filed before the High Court, categorically stated :

> "In reply to the averments made in para 10 of the affidavit, it is submitted that the letter addressed to the petitioner on 7.12.2001 E which was served on the same date clearly speaks about the actual demand outstanding for payment. From out of that, the petitioner paid an amount of Rs.25,00,000/- on 31.1.2002. Hence the net figure reported in the attachment proceedings is quite correct i.e. (Rs.73.08 lakhs – Rs.25.00 Lakhs). It is pertinent to mention here F that though the petitioner once again approached Settlement Commission on the levy of interest as wholly unjustified and untenable on 4.2.2002, nothing is heard from the Settlement Commission before initiating the proceedings for attachment, i.e., by way of any letter from the Settlement Commission for stay of G demand till the outcome of the Settlement Commission's Report. Secondly, though the units have been attached the UTI which when the units are there for sale ought to have obtained the consent of the petitioner before sale and as such the loss, if any on account of sale, i.e., Rs.21.31 lakhs cannot be attributed to the 2nd H

A respondent. The petition for waiver of interest filed before the Commissioner of Income Tax, V, Hyderabad has been rejected for Asst. year 1990-91, 91-92, 92-93 & 95-96 vide Commissioner of Income Tax Proc. No.CIT.V/220(2A)/1/2002-03 dated 26.11.2002.

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15. Thus, the stand of the Income Tax Department also was that it sought to attach the units and did not opt for the repurchase value at that point of time.

16. We have noticed that the respondent made all sincere efforts to C pay the tax. It made an offer to the Income Tax Officer to transfer the bonds at their face value at Rs.10/- per unit. Unfortunately, the Income Tax Department neither replied to the said letter nor paid and heed to his request. Respondent had invested a sum of Rs.65 lacs. He, therefore, was entitled to, at least, that amount. Government of India had already D been considering the matter of reimbursement to the holders of the units at least at the purchase rate. In that view of the matter, it must be held that it not only acted hastily but also illegally. As a State, within the meaning of Article 12 of the Constitution of India, it was required to exercise restraint and give effect to the provisions of the contract in a reasonable E manner. Clause (vi) of sub-section (3) of Section 226 of the Act in categorical terms created a legal fiction to the effect that when an amount is not payable, the assessee is not required to pay any such amount or part thereof. Appellant being a statutory authority should have acted strictly in terms of the conditions of the contract. It was to act reasonably and F fairly.

17. Respondent No.1 never authorised the Unit Trust of India to sell the same in the market at the lower price as respondent No.1 has stated in the letter dated 4th February, 2002 that due to the fall in the prices in the market, he was not able to dispose of the units. Respondent G No.1 further prayed time till May 2002 to clear the dues and was awaiting information from Respondent Nos.2 and 3 but in the meantime the petitioner sold the same in the market without any intimation to respondent No.1

H 18. Section 226(3)(vi) cannot be interpreted to mean that the Unit

Trust of India was fully authorised to dispose of the units on its own without any notice to the holder of the units. A

19. Reliance has been placed on *Life Insurance Corporation of India & Anr.* v. *Gangadhar Vishwanath Ranade (dead) by Lrs.*, [1989] 4 SCC 297 is misplaced. In a situation of this nature, having regard to sub-section (3) of Section 226 of the Act, it cannot be said that the appellant was holding the money of the respondent. The amount in question could have been held by the appellant only whether the respondent had exercised his option therefore. The fact situation obtaining therein was absolutely different. In that case, the paid up policies taken by the respondent. He assigned the same in favour of his wife. Assignment made was registered although notice under sub-section (3) of Section 226 was issued before the policy was matured. No statement on oath was made under clause (vi) thereof raising an objection on the basis of the registered assignment. It was in that situation opined : B C D

> "It is, therefore, obvious that the question of revocation of the notice under Clause (vii) of Sub-section (3) of Section 226 of the Income Tax Act, 1961 arose in the present case only after the L.I.C. made the requisite statement on oath under Section 226(3)(vi) of the Act in view of its consistent stand throughout that the moneys due under the policies were held by it for and on behalf of the assignee and not the defaulter. Mere information of the assignment to the I.T.O. and keeping the assignee informed of the I.T.O.'s action did not amount to discharge of the statutory obligation under Section 226(3)(vi) of the Act, by the L.I.C. The statute having expressly provided the mode of raising such an objection in the form of a statement on oath specified in Clause (vi), performance of that obligation by the notice had to be made only in that manner. This statutory obligation was performed by the L.I.C. only on 5.12.1975 as stated earlier. The personal liability arising after making the requisite statement on oath as envisaged by Clause (vi) is only "if it is discovered that such statement was false in any material particular and not otherwise." E F G

20. The said decision has no application in the facts and circumstances of the present case. H

A 21. Reliance has also been placed upon a decision of a learned Single Judge of *Karnataka High Court in Vysya Bank Ltd.* v. *Joint Commissioner of Income Tax,* [241 ITR 178]. In that case, the Bank was holding the money on behalf of the judgment-debtor. The money was lying with the bank on fixed deposit. The said fixed deposit was made on B interest. It was in that situation opined :

> "The banker becomes a debtor of the assessee in default the moment the fixed deposit receipt is obtained. Normally the payment of the fixed deposit receipt on the due dates. But on forgoing interest or paying lesser rate of interest the bankers generally permit C customers to withdraw the amount of the fixed deposits before the maturity date. The fixed deposit receipt is not a negotiable instrument but could be assigned with the concurrence of the bank in favour of other persons attachment of the amount in the fixed deposit could be made by the income-tax authorities under the D proviso to section 226(3) of the Income-tax Act."

22. The banker becomes a debtor of the assessee-in-default on maturity of the fixed deposit scheme. The fixed deposit itself could have been a subject matter of the judgment.

E 23. We, therefore, do not find any error in the judgment of the High Court as the respondent is entitled to be restituted. We are of the opinion, that the respondent was also entitled to dividend declared during the said period viz. from the date of allotment. The High Court was not correct in not considering that aspect of the matter.

F 24. For the reasons aforementioned, the appeal filed by the Administrator, Unit Trust of India is dismissed and the appeal filed by B.M. Malani is allowed with costs. Counsel's fee assessed at Rs.25,000/- (Rupees twenty five thousand only).

G N.J. CA. No. 4792 of 2007 dismissed.
and C.A. Nos. 4793-4799 of 2007 allowed.