

PETITIONER:
COMMISSIONER OF INCOME-TAX (CENTRAL) CALCUTTA

Vs.

RESPONDENT:
INDIA DISCOUNT CO. LTD.

DATE OF JUDGMENT:
07/08/1969

BENCH:
RAMASWAMI, V.
BENCH:
RAMASWAMI, V.
SHAH, J.C. (CJ)
GROVER, A.N.

CITATION:
1970 AIR 410 1970 SCR (1) 767
1969 SCC (2) 514

ACT:
Income-tax Act (11 of 1922), ss. 10 and 12--Shares sold with arrear dividends--Amount of arrear dividends received by purchaser--Whether taxable.

HEADNOTE:

The assessee--a dealer in shares and securities, purchased certain shares on which dividends relating to previous years were in arrears. The shares were sold with the arrear dividends. The assessee received the amount of arrear dividends and he first credited this sum to the profit and loss appropriation account and thereafter transferred the same to a reserve fund. No adjustment was made in the share purchase account on account of the receipt of the dividend. The value of the shares which represented the stock-in-trade of the assessee remained the same both in the opening and the closing stocks. The assessee claimed that the amount of arrear dividends received was not income liable to income-tax as it was merely a realisation of the capital. The Income-tax Officer rejected the contention and brought it to tax. This decision was upheld in further appeals. But, on reference, the High Court held that the amount was not liable to tax. Dismissing the appeal by the Revenue, this Court,

HELD: The consideration paid by the assessee was given not only for the shares but also for the share dividends. As the dividend had been declared long ago there was no uncertainty as to the exact amount receivable in respect of them, and so, both the purchaser and the vendor knew exactly what sum would come to the vendor by way of such dividend. The existence of a contract binding the vendors to make over to the purchaser the arrear dividends clearly implied that the price paid by the purchaser was not only for the value of the share scrips but also for the amount which was going to be realised in the form of arrear dividends by the purchaser. Such an arrangement implied that the value of the per share settled into the broker's bill was not the real value of the share scrips alone but also included the element of the arrear dividends agreed to be receivable by the purchaser. The legal position, therefore, was that the

arrear dividends were not claimable by the purchaser by virtue of his right as such purchaser and could not become his income from the shares. He was to get the same because the vendor had contracted to pass the arrear dividends on to him. They were the income of the vendors, i.e., the registered holders but they could not become the income of the purchaser. What the assessee acquired in the form of share scrip represented its stock-in-trade which consisted of the shares and the dividends potential which had to be realised. [770 D-H]

A receipt which in law cannot be regarded as income cannot become so merely because the assessee erroneously credited it to the profit and loss account. [771 C]

Commissioner of Income-tax, Bombay City I v. M/s. Shoorji Vallabhdas & Co. 46 I.T.R. 144, referred to.

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 2115 of 1968.

SupCl/69--5
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Appeal from the judgment and order dated January 6, 1965 of the Calcutta High Court in Income-tax Reference No. 145 of 1961.

B. Sen, S. A. L. Narayana Rao, R.N. Sachthey and B.D. Sharma, for the appellant.

S. Mitra and P.K. Mukherjee, for the respondent.

The Judgment of the Court was delivered by

Ramaswami, J. The respondent is a private limited company (hereinafter referred to as the assessee). The appeal relates to the assessment year 1956-57 for which the previous year is the year ending September 30, 1955. The business of the assessee was to deal with shares and securities. On September 30, 1954 the assessee purchased 11,900 shares of Kedarnath Jute Manufacturing Co. Ltd. in two lots, one at the rate of Rs. 9-8-0 per share and the other at Rs. 9-4-0 per share from one Beharilal Nathani, Share broker, for a total consideration of Rs. 1,12,575/-. When the assessee purchased the said shares a large amount of dividends was in arrear as the previous owners had not claimed the dividends declared between 1936 and 1945, although a large part of the dividends on the said shares in respect of the years 1945 to 1954 had been collected by the previous owners of the said shares. A letter addressed by Beharilal Nathani to the assessee bearing the date September 30, 1954 goes to show that the shares had been "sold with arrear dividends". It is admitted that the dividends which had been declared between the years 1936 and 1945 and were received by the assessee during the accounting period amounted to Rs. 43,925/-. The assessee first credited this sum to the profit and loss appropriation account and thereafter transferred the same to a reserve fund in the accounting year ending September 30, 1955. No adjustment was made in the share purchase account on account of the receipt of dividend. The value of the shares which represented the stock-in-trade of the assessee remained the same both in the opening and the closing stocks. Before the Income-tax Officer it was contended on behalf of the assessee that as the arrear dividends pertained to the years 1936 to 1945 the arrear dividend received by the assessee was not in the nature of income liable to income-tax as it was merely a realisation of capital. The Income-tax Officer rejected the contention of the assessee and treated the

amount of arrear dividend as the business income of the assessee liable to tax. On appeal by the assessee the Appellate Assistant Commissioner of Income-tax examined the question whether the amount of Rs. 43,925/- should be treated as dividend and should, therefore, be assessed under s. 12 of the Indian Income-tax Act, 1922 (hereinafter referred to as the Act) or whether it should be treated as

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profits and gains of business arising to the assessee and taxed under s. 10 of the Act. He, however, held that the amount could not be regarded as 'dividend' as the assessee was not the registered shareholder in the years for which the arrear dividends were declared. But he held that since the shares were purchased by the assessee with the knowledge that it would be entitled to receive the arrear dividends which represented profits arising on the acquisition of such shares, the assessee could be deemed to have entered into a scheme of profit making, an adventure in the nature of trade. 'The assessee brought a second appeal to the Appellate Tribunal but the appeal was dismissed. The Appellate Tribunal confirmed the findings by the Income-tax authorities and held that the assessee acquired the shares on which the arrear dividends were received in the course of its share-dealing business and that the sum of Rs. 43,925/- so received by the assessee formed an integral part of its income arising from business which was liable to tax. At the instance of the assessee the Appellate Tribunal stated a case to the High Court on the following question of law:

"Whether on the facts and in the circumstances of the case the sum of Rs. 43,925/- received by the assessee represented business income arising under section 10 from an adventure in the nature of trade or it was a dividend within the meaning of section 12 of the Income-tax Act ?"

After looking into the statement of case and also the application of the assessee under s. 66(1) of the Act the High Court held that the question which the Tribunal had referred did not correctly and accurately describe the stand and contention taken by the assessee throughout which was that no part of the arrear dividend received by the assessee was income at all liable to tax. The High Court thereafter addressed itself to the real issue between the parties and ultimately held that the amount of Rs. 43,925/- was not liable to tax. This appeal is brought on behalf of the Commissioner of Income-tax against the judgment of the High Court dated January 6, 1965 by a certificate granted under s. 66A(2) of the Act.

It is necessary that the question referred to by the High Court should be reframed in the following manner in order to bring out the real point in controversy between the parties:

"Whether in the facts and circumstances of the case the assessee had purchased the arrears of dividend ? If so whether the said sum of Rs. 43,925/- could at all be assessed either as dividend or as profit ?"

It is manifest that dividends declared by Kedarnath Jute Manufacturing Co., between the years 1936 and 1945 were the

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property of the persons whose names stood on the share register on the relevant dates. When a company declares dividend the same can only be paid to the person who is then

the registered holder. A purchaser of shares becomes entitled to all dividends declared since his purchase but not before. If the purchase is made on the eve of declaration of dividend but the purchaser does not get his name mutated in the records of the company in time to have the dividend-warrant issued in his own name he is entitled to call upon his vendor to make over the dividend to him if and when received. It is well settled that after a sale of the shares and so long as the purchaser does not get his name registered, the vendor is for certain purposes considered a trustee for the purchaser of the rights attaching to the shares or accruing thereon, including the voting rights. In the present case there was a contract between the assessee and the registered shareholders to sell the shares to the assessee with arrear dividends. In other words the assessee entered into the contract with the registered shareholders not only to purchase share scrips but the dividends which had been declared but not collected by him or paid over to shareholders. As the dividends had been declared long ago there was no uncertainty as to the exact amount receivable in respect of them. It is, therefore, clear that both the purchaser and the vendor knew exactly what sum of money would come to the vendor by way of such dividend. In other words the purchase consideration included the amount of the arrear dividends and as the dividends had been declared long ago, there was no uncertainty as to the exact amount receivable in respect of them. The existence of a contract binding the vendors to make over to the purchaser the arrear dividends clearly implied that the price paid by the purchaser was not only for the value of the share scrips but also for the sum of Rs. 43,925/- which was going to be realised in the form of arrear dividends by the purchaser. The High Court held upon an examination of the evidence that such an arrangement implied that the value of Rs. 9-8-0 and Rs. 9-4-0 per share as settled into the broker's bills was not the real value of the share scrips alone but also included the element of the arrear dividends agreed to be receivable by the purchaser. The legal position, therefore, is that the arrear dividends were not claimable by the purchaser by virtue of his right as such purchaser and could not become his income from the shares. He was to get the same because the vendor had contracted to pass the arrear dividends on to him. They were the income of the vendors, i.e., the registered holders but they could not become the income of the purchaser. In fact the assessee had purchased the amount of arrear dividends for a price which was included in the total consideration of Rs. 1,12,575/-. What the assessee acquired in the form of share scrip represented its stock-in-trade, which consisted of the shares and the dividends potential which had to be realised.

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In this state of facts it is manifest that the assessee paid the amount of Rs. 1,12,575/- not only for the share scrips but also for the arrear dividends which was inextricably connected with the purchase of the share scrips. In our opinion the High Court rightly held that the amount of Rs. 43,925/- was not income which could be assessed in the hands of the assessee.

It was said that the assessee had itself credited the amount of Rs. 43,925/- to the profit and loss appropriation account and thereafter transferred the same to a reserve fund in the accounting year ending September 30, 1955. No adjustment was made in the share purchase account on account of the receipt of dividend. But it is well established that

a receipt which in law cannot be regarded as income cannot become so merely because the assessee erroneously credited it to the profit and loss account. [see Commissioner of Income-tax, Bombay City I v. M/s. Shoorji Vallabhdas & Co.(1)]. The assessee's case, had all along been that the amount of arrear dividends received could not be treated as income of the assessee liable to tax for the assessment year 1956-57. As we have already shown the consideration paid by the assessee was given not only for the shares but also for share dividends amounting to Rs. 43,925/- and the amount of Rs. 1,12,575/- was paid not only for the share scrips but also for the arrear dividends. In other words there was capital purchase by the assessee. of the shares together with arrear dividends due on the shares for the years 1936 to 1945. It is therefore not possible to treat the payment of Rs. 43,925/- as income liable to tax either as profit under s. 10 of the Act or as dividend under s. 12 of the Act.

For the reasons expressed we hold that there is no merit in this appeal. It is accordingly dismissed with costs.

Y.P.

Appeal dismissed.

(1) 46 I.T.R. 144.

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