

IN THE NATIONAL COMPANY LAW TRIBUNAL

BENCH AT ALLAHABAD

**CA No.389 of 2019
IN
CP(IB) No.55/ALD/2017**

IN THE MATTER OF:

**LML LIMITED (UNDER LIQUIDATION)
Through Liquidator of
LML Ltd.**

**.....APPLICANT
(Liquidator)**

V/S

OFFICE OF COMMISSIONER OF INCOME TAX, MUMBAI

..... RESPONDENT

ORDER DELIVERED ON:31.08.2020

CORAM:

Hon'ble Mr. Justice (Retd.) Rajesh Dayal Khare, Member, Judicial

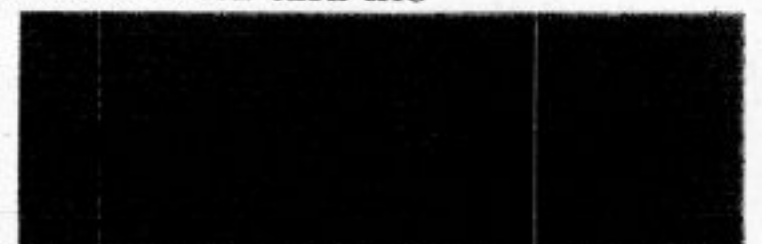
**For the Applicant: Mr. Rohan Gupta, Advocate alongwith
Ms. Monica Nanda, PCS**

For the Respondent : Mr. Gaurav Mahajan, Sr. SC for IT Department.

ORDER

Per se: Mr. Justice (Retd.) Rajesh Dayal Khare, Member (Judicial)

1. The present application has been filed under Section 60(5) of The Insolvency and Bankruptcy Code, 2016 by the liquidator seeking directions as to whether the capital gain tax is to be paid on the proceeds received from sale of assets of the corporate debtor and is to be included in the liquidation cost or to be distributed as per waterfall mechanism under Sec 53 of IBC.
2. As per the averment made in the application, various auctions were held and a sum of Rs. 113,88,40,170/- has been realised so far and the



applicant has already distributed majority of the amount realised and further he has to proceed with the distribution of the pending amounts in accordance with the waterfall mechanism prescribed under Sec 53 of the Insolvency and Bankruptcy Code, 2016. However, he is faced with the issue as to whether the capital gains tax would be attracted on sales of such assets as part of liquidation estate to be included as liquidation costs, if so, he would be required to first make provision for the capital gains and accordingly after deduction of the amount, the balance shall be distributed amongst the stakeholders.

3. Further the counsel for the liquidator has referred Sec 52 of the Code wherein a secured creditor has the option to either:
 - a) *Relinquish its security interest to the liquidation estate and receive proceeds from the sale of assets by the liquidator in the manner specified in Section 53; or*
 - b) *Realise its security interest in the manner specified in this Section.*
4. It is contended that in the present case the secured creditors have opted for proceeding under Sec 52(a) i.e. by relinquishing their security to the liquidator who proceed to sell the assets in terms of the Code and the Insolvency and Bankruptcy Board of India (Liquidation Process) Regulations, 2016.
5. Further, it is stated that a secured creditor is entitled to effect sale under the SARFAESI Act and appropriate the entire amount towards its dues, without any liability to first pay the capital gain tax. It is only upon residual liquidity that the distribution of the assets has to be made according to the other creditors. If the capital gain is first to be provided for, and then be included as liquidation cost, it would create **anomalous situation** in the secured creditor getting a lesser remittance



than what they could have realised, had they not released the security into the common corpus. Therefore, it is submitted that in case capital gains tax is treated as liquidation costs, to be defrayed at the first instance on such transactions, the secured creditors would not relinquish their security to the liquidators. Further stated that none of the provisions of the Income Tax Act, 1961 as referred by the respondent provide for distribution at all and is provided only in the waterfall mechanism provided in Sec 53 of the IBC which is as quoted :

53. (1) Notwithstanding anything to the contrary contained in any law enacted by the Parliament or any State Legislature for the time being in force, the proceeds from the sale of the liquidation assets shall be distributed in the following order of priority and within such period and in such manner as may be specified, namely :—
- (a) The insolvency resolution process costs and the liquidation costs paid in full; secured creditor in liquidation proceedings.
 - (b) The following debts which shall rank equally between and among the following:—
 - (i) workmen's dues for the period of twenty-four months preceding the liquidation commencement date; and
 - (ii) debts owed to a secured creditor in the event such secured creditor has relinquished security in the manner set out in section 52;
 - (c) wages and any unpaid dues owed to employees other than workmen for the period of twelve months preceding the liquidation commencement date;
 - (d) financial debts owed to unsecured creditors; (e) the following dues shall rank equally between and among the following:—
 - (i) any amount due to the Central Government and the State Government including the amount to be received on account of the Consolidated Fund of India and the Consolidated Fund of a State, if any, in respect of the whole or any part of the period of two years preceding the liquidation commencement date;
 - (ii) debts owed to a secured creditor for any amount unpaid following the enforcement of security interest;
 - (f) any remaining debts and dues;
 - (g) preference shareholders, if any; and



- (h) equity shareholders or partners, as the case may be.*
- (2) Any contractual arrangements between recipients under sub-section (1) with equal ranking, if disrupting the order of priority under that sub-section shall be disregarded by the liquidator.*
- (3) The fees payable to the liquidator shall be deducted proportionately from the proceeds payable to each class of recipients under sub-section (1), and the proceeds to the relevant recipient shall be distributed after such deduction.*

6. It is further contended that from the perusal of above hierarchy of the waterfall mechanism it is clear that the debts owed to a secured creditor and workmen are on higher hierarchy rather than the liability towards government dues and no provision has been pointed out nor any claim has been laid by the respondent by which state dues would get precedence over the distribution proposed to be made to the secured, unsecured financial creditor and workmen.

7. Further referring to Sec 238 of IBC and Sec 178(6) of the Income Tax Act which provides as follows:

Section 238 : Provisions of this Code to override other laws.

The provisions of this Code shall have effect, notwithstanding anything inconsistent therewith contained in any other law for the time being in force or any instrument having effect by virtue of any such law.

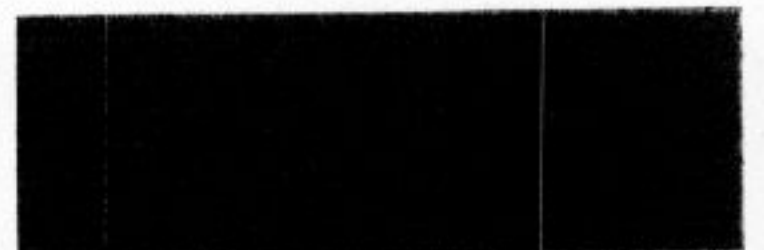
Section 178(6) of The Income- Tax Act

(6) The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other law for the time being in force.[except the provisions of the Insolvency and Bankruptcy Code, 2016].

It is argued that the provisions of IBC, 2016 would prevail over Income Tax Act, 1961 and the provisions of Income Tax Act have also been amended in view of the provisions of the Insolvency and Bankruptcy Code.



8. The counsel for the applicant in support of his arguments has relied on the judgment of Hon'ble Supreme Court in the case of **M/S Commissioner of Income Tax v. KTC Tyres India Ltd.** in which it was held that capital gain tax cannot be treated as liquidation cost. And also referred to the case of **M/S Shree Ram Lime Products Pvt. Ltd v. Gee Ispat Pvt. Ltd.** of the principal Bench, New Delhi stating that the same issue has already been decided in this matter.
9. In reply to the above, the counsel for Income Tax submitted that the amount received on sale of assets of the Corporate debtor till 30.07.2019 was realised net of TDS. Thus TDS was deducted by the purchasers of the assets of the Corporate Debtor while making payment and the sum so deducted must have been paid to the credit of the Central government. Further the counsel has refer to Sec 45 and Sec 46 of The Income Tax Act which is related to the capital gains on distribution off assets by the companies in Liquidation and how such money or assets will be chargeable to income Tax under the head Capital gain.
10. Further it was contented on behalf of Income Tax Department that the bare reading of provisions of Sec 238 of IBC it is seen that the provisions of the Code override the provisions of the Act to the extent the provisions of the Act are inconsistent with the provisions of the Code and in the present case there is no inconsistency with respect chargeability of tax on capital gains between the provision of Code and Act and provisions of Sec 45 of IT Act shall remain in operation and further stated that decision of NCLT New Delhi Bench in matter of M/S Shree Ram Lime



Products Private Limited on which the applicant relied will not be applicable to the facts of the present case.

11. After hearing the submissions of both the parties and referring to the facts of the case this Adjudicating Authority do not find favour with the arguments raised on behalf of the Income Tax and further at this juncture I would refer to the case of Hon'ble Supreme Court :


Principial Commissioner of Income Tax v. Monnet Ispat And Energy Ltd. dated 10.08.2018 in which the Hon'ble Apex Court held " Given Section 238 of The Insolvency and Bankruptcy Code, 2016, it is obvious that the Code will override anything inconsistent contained in any other enactment, including the Income Tax- Tax Act..."

12. Thus referring to this, this Adjudicating Authority is of the view that the applicability of Sec 45 and 46 of The Income Tax Act will not have an overriding effect on the water fall mechanism provided under Sec 53 of the IBC, 2016, which is a complete code in itself and thus capital gain shall not be taken into consideration as the liquidation cost.
13. Further, it is observed that Sec 178 of Income Tax Act, 1961 provides for a priority in appropriation of the amount set aside by the liquidator for clearance of tax dues but it is to consider that the liquidation of accompany could be under the provisions of different enactments. And as for liquidation under IBC, Sec 178 of IT Act stands excluded by virtue of amendment of Section 178 (6) with effect from 01.11.2016, in accordance with the provision of Sec 247 of the IBC read with Third Schedule appended there to, therefore , as the corporate debtor is in liquidation under the Code, the Income Tax Department can no longer claim a priority in respect of clearance of tax dues as provided Under



Sec 178(2) and (3) of the Income Tax Act, 1961 as also held in case of **Leo Edibles & Fats Ltd v. Income Tax Department.**

14. Further as per Sec 238 of the Code, the provision of the Code shall have an overriding effect on any other enactment and Sec 53 of the Code provides the waterfall mechanism for distribution of assets in which Sec 53(b) i.e the debt owed to the secured creditors has been given priority over government dues as reflected under Sec 53(i) and has to be dealt accordingly.
15. Therefore, the tax liability arising out of the sale of assets by the liquidator shall be distributed in accordance with the provisions of Section 53 of the Insolvency and Bankruptcy Code, 2016 and the capital gain tax shall not be treated as the liquidation cost.
16. Accordingly, CA No.389/2019 is **disposed of.**


JUSTICE RAJESH DAYAL KHARE
MEMBER (J)

Date: 31.08.2020

Swati Gupta
(LRA)