

Note – Judgement of Gujarat High Court reg. section 281, which deals with certain transfers to be void

This Note relates to the significance of the recent judgement of Gujarat High Court in the case of *Tax Recovery Officer Vs Industrial Fin. Corpn. of India [2012] 346 ITR 11 (Guj)*, which deals with the interpretation of the provisions of section 281 of the Income-Tax Act, 1961 (the Act), relating to “*Certain transfers to be void*”. As per the aforesaid judgement, section 281 of the Act, lays down that a charge or transfer of property during the pendency of income-tax proceedings would be void. However, under the proviso to sub-section (1) of section 281, the charge or transfer shall not be void if made (a) for adequate consideration and without notice of the pendency of such proceedings or (b) without notice of tax or other sum payable by the assessee (the transferor).

In this connection, the attention of all the clients is invited to one of my Articles under the title, “*Circular No.4 of 2011, relating to section 281, which deals with certain transfers to be void*”, which was published in *337 ITR (Jour) p.8*. In the aforesaid Article, the implications of the aforesaid Circular No.4 of 2011, issued by the Central Board of Direct Taxes (CBDT) and the provisions of section 281 of the Act, have been discussed in detail. For the sake of the perusal and guidance of the clients, the Conclusion of the aforesaid Article is reproduced as follows :

Conclusion

In the light of the discussion in the preceding paragraphs, it may be safely concluded that –

- 1. Section 281 is normally invoked by the Income-Tax Department, in order to protect the interests of the Revenue, wherever the circumstances so demand.*
- 2. Section 281 of the Income-Tax Act, 1961, does not prescribe any adjudicatory machinery for deciding any question which may arise under it.*
- 3. The Tax Recovery Officer / Income-Tax Officer has no power under section 281 to declare a transfer void.*

4. *In order to declare a transfer fraudulent under section 281, appropriate proceedings have to be taken by the Income-Tax Department before the competent civil court.*
5. *Clause (i) of the proviso to section 281(1) refers to a bona fide transfer for value, without notice of pendency of proceedings.*

In other words, the provisions of section 281 will not apply in a case where the impugned charge or transfer is made for adequate consideration or sufficient reason, without notice of the pendency of proceedings.

6. *In view of the proviso to section 281(1), if the impugned charge or transfer is covered under clause (i) of the proviso then clause (ii) of the said proviso will not come into play.*

In other words, previous permission of the Assessing Officer will not be required for the impugned charge or transfer, as contemplated under section 281(1) of the Act.

7. *Creation of a charge on an asset for raising a loan for the purposes of business of the assessee is definitely an adequate consideration or sufficient reason for such charge.*
8. *The previous permission of the Assessing Officer will not be required in a case where the impugned charge is created for raising a loan for the purposes of the business of the assessee.*

Similarly, the previous permission of the Assessing Officer will not be required in a case where the impugned transfer is made for adequate consideration.

9. *The aforesaid Circular No.4 of 2011, dated July 19, 2011, will, therefore, apply only in a case where the previous permission of the Assessing Officer is sought by the assessee and not otherwise.*

In view of the aforesaid reasons, the aforesaid circular will not apply in cases –

- (i) where the transfer of an asset is made for adequate consideration, or*
- (ii) a charge is created on an asset for raising a loan for the purposes of the business of the assessee.*

It is heartening to note that the aforesaid judgement of Gujarat High Court fully supports my aforesaid view regarding the implications of the provisions of section 281 of the Act.

In the aforesaid case, two Writ Petitions were filed before the Hon. Gujarat High Court, one by the TRO, Gandhinagar and the second by the Assistant Commissioner of Customs. The first Writ Petition, filed by the TRO, was against the action taken by M/s Industrial Finance Corporation of India (IFCI, for short) under section 13(4) of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act, for short). A prayer was made to restrain the first respondent-financial institution from parting with possession, transferring or otherwise dealing with the properties of the second respondent – Parekh Platinum Ltd (PPL, for short) – borrower company.

The question involved in the first Writ Petition was whether, in view of section 281(1) of the Act, the charge created against the property in question by mortgaging the property by the second respondent-assessee borrower in favour of the first respondent-financial institution, during the pendency of any of the proceedings under the Income-Tax Act, 1961, was void as against any claim in respect of tax and other sum payable by PPL, the respondent-assessee in favour of the petitioner-Revenue, viz the Income-Tax Department.

After a detailed discussion regarding the interpretation of the provision of section 281 of the Act, the Writ Petition filed by the Tax Recovery Officer of the Income-Tax Department was dismissed. The reason for the dismissal of the aforesaid Writ Petition was that the TRO had not disputed the fact that no notice of pendency of any income-tax proceeding was served on the financial institution (IFCI) on or before the execution of the equitable mortgage by PPL, the assessee in favour of the financial institution. While executing the agreement, the Director on behalf of the assessee (PPL), had specifically mentioned in the agreement that there were no income-tax dues and no such proceeding was pending. Therefore, the financial institution (IFCI) was entitled to protection and the *bona fide* transfer of the property having been made for valuable consideration from the assessee (PPL) and without notice of the proceedings for recovery of arrears of income-tax against the financial institution (IFCI), was saved under

clause (i) of the proviso to section 281(1) of the Act, though the transfer was hit by main part of section 281 of the Act.

From the aforesaid Article and the judgement of Gujarat High Court, it is clearly established that under clause (i) of the proviso to section 281(1) of the Act, the charge or transfer shall not be void if made (a) for adequate consideration and without notice of the pendency of the income-tax proceedings, or (b) without notice of tax or other sum payable by the assessee, viz. the transferor. It may further be noted in this regard that once the case in relation to the charge on or transfer of any assets in favour of any other person; falls within the purview of clause (i) of the proviso to section 281(1) of the Act, then clause (ii) of the said proviso will not come into play. In other words, the previous permission of the Assessing Officer will not be required in respect of the aforesaid charge or transfer.

All the clients are, accordingly, advised to make use of the contents of the aforesaid Article, as well as the judgement of the Gujarat High Court, in respect of the provisions of section 281 of the Act.

The aforesaid legal position will be useful in the following cases :

- (i) Where the transfer of an asset is made for adequate consideration, or
- (ii) A charge is created on an asset for raising a loan for the purposes of the business of the assessee.

The copy of the aforesaid Article is attached herewith, for ready reference.

Place : Pune

Date : 15.9.2012

(S.K. Tyagi)

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