

K.R.RAMAMANI MEMORIAL NATIONAL TAXATION MOOT PROBLEM 2017-18

Substantial Questions of Law: Department is on appeal before Hon'ble Madras HC on:

1. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law that the sale consideration was diverted to the Corporation by **overriding title**.
2. Whether on the facts the Tribunal was right in holding that -
*since the expenditure in this case is only the acquisition of full ownership prior to act of transfer of property which stood diminished by reason of transfer of some interest in the property by way of mortgage, **the expenditure in question is an expenditure incurred for the purpose of transferring the full ownership rights in the property** and hence entitled to deduction u/s 48(i) of the amount paid to the TN Financial Corporation'*

Facts:

1. The assessee, Mr.V.Markiv, stood guarantee for repayment of a loan taken by a private limited company, Vulcan BPO Pvt Ltd, of which the assessee was the main promoter (99% shareholding) from the TN Financial Corporation and had also mortgaged certain property belonging to him in favour of the Corporation.
2. In exercise of its rights under the document of mortgage, the Corporation sold the property and appropriated the entire proceeds towards discharge of the loan taken by Vulcan BPO Pvt Ltd (Rs.2 cr loan which was equivalent to property sale value).
3. The Income-Tax Officer (ITO) held that the assessee should be deemed to have received the entire sale proceeds and computed capital gains on the entire sale proceeds thereon. On appeal by assessee, CIT(A) merely upheld order of the ITO
4. On appeal against CIT(A) by the assessee, the Tribunal recorded the undisputed factual position that no amount was *actually received* by the assessee, that the entire sale consideration was paid directly to the Corporation by the purchasers and it was thereafter that the mortgaged property was released.
5. The Tribunal held that the sale consideration was diverted to the Corporation by overriding title. It also upheld the alternate view that the amount settled is part of the cost u/s 48(i)
6. The Assessee relied on the cases of:
 - CIT Vs. Thressiamma Abraham **(227 ITR 802 Ker)**
 - CIT Vs. Shakuntala Kanthilal **(190 ITR 56 Bom)**
 - CIT Vs. Abrarr Alvi **(247 ITR 312 Bom)**
 - Gopinath Nath Pal and Sons Vs. DCIT **(278 ITR 240 Cal)**
 - CIT Vs. Rudra Industrial Commercial Corporation **(244 CTR 304 Kar)**
 - Addl CIT Vs. Mohanbhai Pamabhai (165 ITR 166 SC)
 - Raja Bejoy Singh Dhudhuria vs CIT **((1933) 35 BOMLR 811)**
 - Addl.CIT Vs. Glad Investments Private Limited. **(105 TTJ Delhi 393)**
7. The Department relied on the decisions of:
 - CIT Vs. Roshanbabu Mohammed Hussein Merchant **(144 taxman 720 Bom)**
 - V.S.M.R.Jagdishchandran Vs. CIT(227 ITR 240 SC)
 - CIT Vs. Atilli N.Rao (252 ITR 880 SC)
 - R.M.Arunachalam etc. vs CIT (141 CTR SC 348)
 - Ambat Echukutty Menon vs CIT (87 ITR 129 Ker)

8. **Contentions of Assessee:** The assessee distinguished the various cases relied on by the Department stating that:

- a. There are two kinds of mortgages (as clearly delineated in the case laws relied by the Department itself):
 - i. One type of mortgage is a self-created mortgage i.e. mortgage of property owned by assessee for the direct benefit of the assessee and the
 - ii. Other type of the mortgage is a mortgage on property owned by assessee but created for someone else's benefit.

This type of mortgage can either be an inherited mortgage (like a son inheriting a father's mortgaged property) (or) it can be like in the instant case a mortgage given as a guarantor for a company in which the assessee is interested in.

- b. The assessee's contention is that only for the self-created mortgage will the capital gains be assessable to tax on the entire property sale cost. This is because the assessee has gained a benefit on the mortgage directly. When the assessee is a guarantor for another who defaults and hence the assessee loses the property, it does not gain any benefit.
- c. The assessee points out that even in the cases relied by the Department, this delineation of types of mortgages and the corresponding Capital Gains application is brought out.
- d. The assessee also pointed out that in *Roshanbabu Mohammed Hussein (supra)* relied on by Dept, the HC held after discussing all the relevant decisions that there was a clear distinction between the obligation to discharge the mortgage debt created by previous owner and obligation to discharge debt by assessee itself. The same rationale can be applied to the instant case to say there is a distinction between clearing mortgage debt of a company assessee stood guarantee for vs clearing mortgage debt of the assessee itself.
- e. The assessee stresses that definition of profit is the difference between assets and liabilities between two points of time and if such a definition were adopted the difference between self-created mortgage and the instant case where the assessee stands to lose his asset and not gain anything for the same will clearly be brought out
- f. The assessee further points out that *R.M.Arunachalam (supra)* ,in fact, specifically refused to answer the question about overriding title as it was raised before the SC for the first time and that no case has dealt with this aspect except *Thresiamma Abraham (supra)*, a fact which was not appreciated in *Ambat Echukuty Menon (supra)*

9. **Contentions of the Department:**

- a. The Department relies on the above case laws and says the facts are identical to *Thresamma Abraham* case (supra) which has specifically been overturned by *Ambat Echukuty Menon* (supra) and that this issue is clearly covered in favour of the Department by *Attili N. Rao* (supra) SC.
- b. The issue is that there was a sale, capital gains has to be paid on the sale consideration minus cost of acquisition; the fact there was a mortgage and amount was paid to release it etc is a secondary event and is of no consequence to the capital gains point of taxation and quantum thereof.