

Income tax department cannot claim any priority in payment from liquidated estate under IBC

Summary – The High Court of Andhra Pradesh and Telangana in a recent case of Leo Edibles & Fats Ltd., (the Assessee) held that Income-tax department cannot claim any priority in payment from liquidation estate merely because it had issued attachment order much prior to initiation of liquidation proceedings under Insolvency and Bankruptcy Code

Facts

- The petitioner company stated that pursuant to the order passed by the National Company Law Tribunal, the fifth respondent was appointed as a liquidator to liquidate company VNR under the provisions of the code. The assets of the said company were pooled to form a liquidated estate and all such assets were sought to be sold by e-auction. A notice was published in newspapers, notifying the e-auction sale date. The petitioner company was the highest bidder for the commercial/residential building, along with land. The Earnest Money Deposit and 25 per cent of the bid amount being paid, the sale letter was issued. The petitioner company received letter calling upon it to deposit the balance sale consideration within fifteen days. At this stage, it came to know that the property purchased by it was subjected to attachment by the first respondent Tax Recovery Officer pursuant to the recovery proceedings initiated by the Income-tax Department against VNR, the company in liquidation. The Sub-Registrar, the fourth respondent, refused to entertain any request for registration in relation to the subject property until and unless the attachment order of the first respondent was lifted. Hence, the present writ petition was filed.
- The petitioner company filed application in the writ petition seeking an interim order directing the first respondent to recall the attachment and directing the fourth respondent to register the sale of the property by the fifth respondent in its favour. It also filed application seeking a direction to the fifth respondent not to insist upon the petitioner company for paying the balance sale consideration till the sale deed was registered in its favour.

Held

- The Income-tax Department does not enjoy the status of a secured creditor, on par with a secured creditor covered by a mortgage or other security interest, who can avail the provisions of section 52. At best, it can only claim a charge under the attachment order, in terms of section 281 of the Act of 1961.
- In *Ananta Mills Ltd. (In Liquidation) v. City Deputy Collector* [\[1972\] 42 Comp. Cas 476 \(Guj.\)](#) attachment *simpliciter* of the properties of a company, which was subsequently ordered to be wound up, without any further action being taken would be of no consequence or effect against the Official Liquidator and the property could be disposed of by the Official Liquidator, wholly ignoring the attachment.

- It may be noticed that in so far as an assessee company in liquidation is concerned, section 178 of the Act of 1961 provides for a priority in appropriation of the amounts set aside by the liquidator for clearance of the tax dues. However, it may be noted that liquidation of a company could be under the provisions of different enactments. In so far as liquidation of a company under the Code is concerned, section 178 of the Act of 1961 stands excluded by virtue of the amendment of section 178(6) with effect from 1-11-2016, in accordance with the provisions of section 247 read with the Third Schedule appended thereto. Therefore, in the event an assessee company is in liquidation under the Code, the Income-tax Department can no longer claim a priority in respect of clearance of tax dues of the said company, as provided under sections 178(2) and (3) of the Act of 1961. In the context of liquidation of an assessee company under the provisions of the Code, the Income-tax Department, not being a secured creditor, must necessarily take recourse to distribution of the liquidation assets as per section 53 of the Code. Section 53(1) provides the order of priority for such distribution and 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 in respect of the whole or any part of the period of two years preceding the liquidation commencement date comes fifth in the order of priority under Clause (e) thereof.
- Significantly, article 266 of the Constitution provides that all revenues received by the Government of India, all loans raised by that Government by the issue of treasury bills, loans or ways and means advances and all moneys received by that Government in repayment of loans shall form one consolidated fund to be entitled 'the Consolidated Fund of India', and all revenues received by the Government of a State, all loans raised by that Government by the issue of treasury bills, loans or ways and means advances and all moneys received by that Government in repayment of loans shall form one consolidated fund to be entitled 'the Consolidated Fund of the State'. It may be noted that this article begins with the phrase 'Subject to the provisions of article 267 and to the provisions of this Chapter with respect to the assignment of the whole or part of the net proceeds of certain taxes and duties to States, all revenues received by the Government of India shall form the Consolidated Fund of India'.
- It is therefore clear that tax dues, being an input to the Consolidated Fund of India and of the States, clearly come within the ambit of section 53(1)(e). If the Legislature, in its wisdom, assigned the fifth position in the order of priority to such dues, it is not for this Court to delve into or be little the rationale underlying the same.
- Section 178(6) of the Act of 1961 starts with a *non obstante* clause but by virtue of the amendment made thereto, *vide* section 247, exclusion of the said provision in so far as liquidation proceedings under the Code are concerned forms an exception to section 178(6) of the Act of 1961. The provisions of sections 220 and 222 of the Act of 1961 do not start with any *non obstante* clause and therefore, they would necessarily be subject to the overriding effect of the Code, by virtue of section 238 thereof.

- On the above analysis, this Court holds that the first respondent cannot claim any priority merely because of the fact that the order of attachment dated 27-10-2016 issued by him was long prior to the initiation of liquidation proceedings under the Code against VNR Infrastructures Limited, Hyderabad. It may be noted that section 36(3)(b) indicates in no uncertain terms that the liquidation estate assets may or may not be in possession of the corporate debtor, including but not limited to encumbered assets. Therefore, even if the order of attachment constitutes an encumbrance on the property, it still does not have the effect of taking it out of the purview of section 36(3)(b). The said order of attachment therefore cannot be taken to be a bar for completion of the sale effected by the fifth respondent under the provisions of the Code. The first respondent necessarily has to submit the claim of the Income-tax Department to the fifth respondent for consideration as and when the distribution of the assets, in terms of section 53(1) is taken up.
- The writ petition is accordingly allowed declaring the legal position as aforesaid. The fourth respondent shall entertain and register the sale transaction effected by the fifth respondent in favour of the petitioner company, if not already done. The first respondent is at liberty to submit its claim before the fifth respondent, who shall duly consider the same in accordance with the priorities stipulated under section 53(1).