K.P. Varghese *v.* Income-tax Officer

SUPREME COURT OF INDIA

SEPTEMBER 4, 1981

P.N. BHAGWATI AND E.S. VENKATARAMIAH, JJ.

Counsels appeared

M.M. Abdul Kadher, S.K. Mehta, E.M.S. Anam, P.N. Puri and N.K. Dua for the Appellants.
S.T. Desai and A. Subhashini for the Respondent.

JUDGMENT

BHAGWATI, J: The principal question that arises for determination in this appeal by certificate is whether understatement of consideration in a transfer of property is a necessary condition for attracting the applicability of section 52(2) of the Income-tax Act, 1961 (hereinafter referred as "the Act") or it is enough for the revenue to show that the fair market value of the property as on the date of the transfer exceeds the full value of the consideration declared by the assessee in respect of the transfer by an amount of not less than 15 per cent of the value so declared. The facts giving rise to the appeal are not very material but since they form the backdrop against which the question arises for consideration, we may briefly state them.

2. The assessee was the owner of a house situated in Ernakulam, which he had purchased in 1958 for the price of Rs. 16,500. On 25-12-1965 the assessee sold the house for the same price of Rs. 16,500 to his daughter-in-law and five of his children. The assessment of the assessee for the assessment year 1966-67 for which the relevant accounting year was the calendar year 1965 was thereafter completed in the normal course and in this assessment, no amount was included by way of capital gains in respect of the transfer of the house since the house was sold by the assessee at the same price at which it was purchased and no capital gains accrued or arose to him as a result of the transfer. On 4-4-1968, however, the ITO issued a notice under section 148 of the Act seeking to reopen the assessment of the assessee for the assessment year 1966-67 and requiring the assessee to submit a return of income within thirty days of the service of the notice. The notice did not state what was the income alleged to have escaped assessment but by his subsequent letter dated 4-3-1969 the ITO intimated to the assessee that he proposed to fix the fair market value of the house sold by the assessee on 25-12-1965 at Rs. 65,000 as against the consideration of Rs. 16,500 for which the house was sold and assess the difference of Rs. 48,500 as capital gains in the hands of the assessee. The assessee raised objections against the reassessment proposed to be made by the ITO but the objections were overruled and an order of reassessment was

passed by the ITO including the sum of Rs. "48,500 as capital gains and bringing it to tax. Though the sale of the house by the assessee was in favour of his daughter-in-law and five of his children who were persons directly connected with him, the ITO could not invoke the aid of section 52(1) for bringing the sum of Rs. 48,500 to tax, because there was admittedly no understatement of consideration in respect of the transfer of the house and it was not possible to say that the transfer was effected by the assessee with the object of avoidance or reduction of his liability under section 45 of the Act. The ITO, therefore, rested his decision to assess the sum of Rs. 48,500 to tax on sub-section (2) of section 52 and taking the view that this sub-section did not require as a condition precedent that there should be understatement of consideration in respect of the transfer and it was enough to attract the applicability of the sub-section if the fair market value of the property as on the date of the transfer exceeded the full value of the consideration declared by the assessee by an amount of not less than 15 per cent of the value so declared, which was indisputably the position in the present case, the ITO assessed the sum of Rs. 48,500 to tax as capital gains. The assessee thereupon preferred a writ petition in the Kerala High Court challenging the validity of the order of reassessment insofar as it brought the sum of Rs. 48,500 to tax relying on section 52(2).

3. The writ petition came up for hearing before Isaac, J. sitting as a Single Judge of the High Court and after hearing both parties, the learned Judge came to the conclusion that understatement of consideration in respect of the transfer was a necessary condition for attracting the applicability of section 52(2) and since in the present case there was admittedly no understatement of consideration and it was a perfectly *bonafide* transaction, section 52(2) had no application and the sum of Rs. 48,500 could not be brought to tax as capital gains under that provision. The revenue appealed against this decision to a Division Bench of the High Court and having regard to the importance and complexity of the question involved, the Division Bench referred the appeal to a Full , Bench of three Judges. The Full Bench heard the appeal but there was a division of opinion, two Judges taking one view and the third Judge taking another. While Raghvan, CJ. agreed substantially with the view taken by Isaac, J., Gopal Nambiar, J. and Vishwanath Iyer, J. took a different view and held that in order to bring a case within section 52(2), it is not at all necessary that there should be understatement of consideration in respect of the transfer and once it is found that the fair market value of the property as on the date of the transfer exceeds the full value of the consideration declared by the assessee in respect of the transfer by an amount of not less than 15 per cent of the value so declared, section 52(2) is straightaway attracted and the fair market value of the property as on the date of the transfer is liable to be taken as the full value of the consideration for the transfer. The writ petition was accordingly dismissed and the order of reassessment sustained by the majority decision reached by the Full Bench. Hence, the present appeal by the assessee with certificate obtained from the High Court.

4. It will be noticed from the above statement of facts that the principal question arising for determination in this appeal turns on the true interpretation of section 52(2). But in order to arrive at its proper interpretation, it is necessary to refer to some other provisions of the Act as well. Section 2(24) of the Act defines the word "income". The definition is inclusive and covers "capital gains" chargeable under section 45. Section 4 is the charging section and it provides that income-tax shall be charged in respect of the total income of the previous year of every person. Section 5 of the Act defines the scope of

"total income" by providing that the total income of the previous year of a person who is resident shall include all income from whatever source derived which is received or is deemed to be received in India in such year by him or on his behalf or accrues or arises or is deemed to accrue or arise to him in India during such year or accrues or arises to him outside India during such year. Section 14 of the Act enumerates the heads of income under which income shall, for the purposes of charge of income-tax and computation of total income, be classified and they include "capital gains". Section 45 provides that any profits or gains arising from the transfer of a capital asset effected in the previous year shall be chargeable to income-tax under the head "Capital gains" and shall be deemed to be the income of the previous year in which the transfer took place. The mode of computation of capital gains is laid down in section 48 of the Act which provides that the income chargeable under the head "Capital gains" shall be computed by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset, two amounts, namely, (*i*) expenditure incurred wholly and exclusively in connection with such transfer; and (*ii*) the cost of acquisition of the capital asset and the cost of any improvement thereto. Then follows section 52 which is the material section requiring to be construed in the present appeal. That section consists of two sub-sections and runs as follows:

> "(1)Where the person who acquires a capital asset from an assessee is directly or indirectly connected with the assessee and the Income-tax Officer has reason to believe that the transfer was effected with the object of avoidance or reduction of the liability of the assessee under section 45, the full value of the consideration for the transfer) shall, with the previous approval of the Inspecting Assistant Commis-sioner, be taken to be the fair market value of the capital asset on the date of the transfer.
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> (2)Without prejudice to the provisions of subsection (1), if in the opinion of the Income-tax Officer the fair market value of a capital asset transferred by an assessee as on the date of the transfer exceeds the full value of the consideration declared by the assessee in respect of the transfer of such capita] asset by an amount of not less than fifteen per cent of the value so declared, the full value of the consideration for such capital asset shall, with the previous approval of the Inspecting Assistant Commissioner, be taken to be its fair market value on the date of its transfer:"

There is a marginal note to section 52 which reads: "Consideration for transfer in cases of under-statement". It may be pointed out that originally when the Act came to be enacted, section 52 consisted of only one provision which is now numbered as sub-section (1) and it was by section 13 of the Finance-Act, 1964 that sub-section (2) was added in that section with effect from 1-4-1964.

5. Now on these provisions the question arises what is the true interpretation of section 52(2). The argument of the revenue was and this argument found favour with the majority Judges of the Full Bench that on a plain natural construction of the language of section 52(2), the only condition for attracting the applicability of that provision is that the fair market value of the capital asset transferred by the assessee as on the date of the transfer exceeds the full value of the consideration' declared by the assessee in respect of the transfer by an amount of not less than 15 per cent of the value so declared. Once the ITO is satisfied that this condition exists, he can proceed to invoke the provision in section 52(2) and take the fair market value of the capital asset transferred by the

assessee as on the date of the transfer as representing the full value of the consideration for the transfer of the capital asset and compute the capital gains on that basis. No more is necessary to be proved, contended the revenue, To introduce any further condition such as understatement of consideration in respect of the transfer would be to read into the statutory provision something which is not there : indeed it would amount to rewriting the section. This argument was based on a strictly literal reading of section 52(2) but we do not think such a construction can be accepted. It ignores several vital considerations which must always be borne in mind when we are interpreting a statutory provision. The task of interpretation of a statutory enactment is not a mechanical task. It is more than a mere reading of mathematical formulae because few words possess the precision of mathematical symbols. It is an attempt to discover the intent of the Legislature from the language used by it and it must always be remembered that language is at best an imperfect instrument for the expression of human thought and as pointed out by Lord Denning, it would be idle to expect every statutory provision to be "drafted with divine prescience and perfect clarity." We can do no better than repeat the famous words of Judge Learned Hand when he said: "...it is true that the words used, even in their literal sense, are the primary and ordinarily the most reliable source of interpreting the meaning of any writing : be it a statute, a contract or anything else. But it is one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary ; but to remember that statutes always have some purpose or object to accomplish, whose sympathetic and imaginative discovery is the surest guide to their meaning". We must not adopt a strictly literal interpretation of section 52(2) but we must construe its language having regard to the object and purpose which the -Legislature had in view in enacting that provision and in the context of the setting in which it occurs. We cannot ignore the context and the collocation of the provisions in which section 52(2) appears, because, as pointed out by Judge Learned Hand in most felicitous language,"... the meaning of a sentence may be more than that of the separate words, as a melody is more than the notes, and no degree of particularly can ever obviate recourse to the setting in which all appear, and which all collectively create". Keeping these observations in mind we may now approach the construction of section 52(2).

6. The primary objection against the literal construction of section 52(2) is that it leads to manifestly unreasonable and absurd conesquences. It is true that the consequences of a suggested construction cannot alter the meaning of a statutory provision but it can certainly help to fix its meaning. It is a well-recognised rule of construction that a statutory provision must be so construed, if possible, that absurdity and mischief may be avoided. There are many situations where the construction suggested on behalf of the revenue would lead to a wholly unreasonable result which could never have been intended by the Legislature. Take, for example, a case where A agrees to sell his property to B for a certain price and before the sale is completed pursuant to the agreement and it is quite well known that sometimes the completion of the sale may take place even a couple of years after the date of the agreement—the market price shoots up with the result that the market price prevailing on the date of the sale exceeds the agreed price at which the property is sold by more than 15 per cent of such agreed price. This is not at all an uncommon case in an economy of rising prices and in fact we would find in a large number of cases where the sale is completed more than a year or two after the date of the agreement that the market price prevailing on the date of the sale is very much more than

the price at which the property is sold under the agreement. Can it be contended with any degree of fairness and justice that in such cases, where there is clearly no understatement of consideration in respect of the transfer and the transaction is perfectly honest and *bona fide* and, in fact, in fulfilment of a contractual obligation, the asses-see who has sold the property should be liable to pay tax on capital gains which have not accrued or arisen to him. It would indeed be most harsh and inequitable to tax the assessee on income which has neither arisen to him nor is received by him, merely because he has carried out the contractual obligation undertaken by him. It is difficult to conceive of any rational reason why the Legislature should have thought it fit to impose liability to tax on an assessee who is bound by law to carry out his contractual obligation to sell the property at the agreed price and honestly carries out such contractual obligation. It would indeed be strange if obedience to the law should attract the levy of tax on income which has neither arisen to the assessee nor has been received by him. If we may take another illustration, let us consider a case where A sells his property to B with a stipulation that after sometime, which may be a couple of years or more, he shall resell the property to A for the same price. Could it be contended in such a case that when B transfers the property to A for the same price at which he originally purchased it, he should be liable to pay tax on the basis as if he has received the market value of the property as on the date of resale, if, in the mean-while, the market price has shot up and exceeds the agreed price by more than 15 per cent. Many other similar situations can be contemplated where it would be absurd and unreasonable to apply section 52(2) according to its strict literal construction. We must, therefore, eschew literalness in the interpretation of section 52(2) and try to arrive at an interpretation which avoids this absurdity and mischief and makes the provision rational and sensible, unless of course, our hands are tied and we cannot find any escape from the tyranny of the literal interpretation. It is now a well-settled rule of construction that where the plain literal interpretation of a statutory provision produces a manifestly absurd and unjust result which could never have been intended by the Legislature, the Court may modify the language used by the Legislature or even 'do some violence" to it, so as to achieve the obvious intention of the Legislature and produce a rational construction—*Luke* v. *Inland Revenue Commissioner* [1963] AC 557. The Court may also in such a case read into the statutory provision a condition which, though not expressed, is implicit as constituting the basic assumption underlying the statutory provision. We think that, having regard to this well-recognised rule of interpretation, a fair and reasonable construction of section 52(2) would be to read into it a condition that it would apply only where the consideration for the transfer is understated or in other words, the assessee has actually received a larger consideration for the transfer than what is declared in the instrument of transfer and it would have no application in case of a *bonafide* transaction where the full value of the consideration for the transfer is correctly declared by the assessee. There are several important considerations which incline us to accept this construction of section 52(2).

7. The first consideration to which we must refer is the object and purpose of the enactment of section 52(2). Prior to the introduction of sub-section (2), section 52 consisted only of what is now sub-section (1). This sub-section provides that where an assessee transfers a capital asset and in respect of the transfer two conditions are satisfied, namely, (*i*) the transferee is a person directly or indirectly connected with the assessee, and (*ii*) the ITO has reason to believe that the transfer was effected with the

object of avoidance or reduction of the liability of the assessee to tax on capital gains, the fair market value of the capital asset on the date of the transfer shall be taken to be the full value of consideration for the transfer and the. assessee shall be taxed on capital gains on that basis. The second condition obviously involves understatement of the consideration in respect of the transfer because it is only by showing the consideration for the transfer at a lesser figure than that actually received that the assessee can achieve the-object of avoiding or reducing his liability to tax on capital gains. And that is why the marginal note to section 52 reads : "Consideration for the transfer in cases of under-statement". But, it must be noticed that for the purpose of bringing a case within sub-section (1), it is not enough merely to show understatement of consideration but it must be further shown that the object of the understatement was to avoid or reduce the liability of the assessee to tax on capital gains. Now, it is necessary to bear in mind that when capital gains are computed by invoking sub-section (1), it is not any fictional accrual or receipt of income which is brought to tax. Sub-section (1) does not deem income to accrue or to be received which in fact never accrued or was never received. It seeks to bring within the net of taxation only that income which has accrued or is received by the assessee as a result of the transfer of the capital asset. But since the actual consideration received by the assessee is not declared or disclosed and in most of the cases, if not all, it would not be possible for the ITO to determine precisely what is actual consideration received ' by the assessee or in other words how much more consideration is received by the assessee than that declared by him, sub-section (1) provides that the fair market value of the property as on the date of the transfer shall be taken to be the full value of the consideration for the transfer which has accrued to or is received by the assessee. Once it is found that the consideration in respect of the transfer is understated and the conditions specified in sub-section (1) are fulfiled, the ITO will not be called upon to prove the precise extent of the undervaluation or in other words, the actual extent of the concealment and the full value of the consideration received for the transfer shall be computed in the manner provided in sub-section (1). The net effect of this provision is as if a statutory best judgment assessment of the actual consideration received by the assessee is made, in the absence of reliable materials.

8. But the scope of sub-section (1) of section 52 is extremely restricted because it applies only where the transferee is a person directly or indirectly connected with the assessee and the object of the understatement is to avoid or reduce the income-tax liability of the assessee to tax on capital gains. There may be cases where the consideration for the transfer is shown at a lesser figure than that actually received by the assessee but the transferee is not a person directly or indirectly connected with the assessee or the object of understatement of the consideration is unconnected with tax on capital gains. Such cases would not be within the reach of sub-section (1) and the assessee, though dishonest, would escape the rigour of the provision enacted in that subsection. Parliament, therefore, enacted subsection (2) with a view to extending the coverage of the provision in sub-section (1) to other cases of understatement of consideration. This becomes clear if we have regard to the object and purpose of the introduction of sub-section (2) as appearing from *travaux preparatoire* relating to the enactment of that provision. It is a sound rule of construction of a statute firmly established in England as far back as 1584 when *Heydon's* case [1584] 3 Co. Rep. 7 a was decided that "... for the sure and true interpretation of all statutes in general ... four things are to be discerned and

considered: (1) What was the common law before the making of the Act, (2) What was the mischief, and defect for which the common law did not provide, (3) What remedy the Parliament hath resolved and appointed to cure the disease of the Commonwealth. And (4) The true reason of the remedy ; and then the office of all the Judges is always to make such construction as shall suppress the mischief, and advance the remedy'". In *In re. Mayfair Property Co.* LR [1898] 2 Ch. 28, Lindley, MR in 1898 found the rule "as necessary now as it was when Lord Coke reported *Heydon's* case". The rule was reaffirmed by Earl of Halsbury in *Eastman Photographic Material Co.* v. *Comptroller General of Patents, Designs & Trade Marks* [1898] AC 571 in the following words:

> "My Lords, it appears to me that to construe the statute in question, it is not only legitimate but highly convenient to refer both to the former Act and to the ascertained evils to which the former Act had given rise, and to the later Act which provided the remedy. These three being compared I cannot doubt the conclusion."

This rule being a rule of construction has been repeatably applied in India in interpreting statutory provisions. It would, therefore, be legitimate in interpreting sub-section (2) to consider what was the mischief and defect for which section 52 as it then stood did not provide and which was sought to be remedied by the enactment of sub-section (2) or in other words, what was the object and purpose of enacting that sub-section. Now in this connection the speech made by the Finance Minister while moving the amendment introducing subsection (2) is extremely relevant, as it throws considerable light on the object and purpose of the enactment of sub-section (2). The Finance Minister explained the reason for introducing sub-section (2) in the following words:

> "Today, particularly every transaction of the sale of property is for a much lower figure than what is actually received. The deed of registration mentions a particular amount; the actual money that passes is considerably more. It is to deal with these classes of sales that this amendment has been drafted. It does not aim at perfectly *bonafide* transactions ... but essentially relates to the day-to-day occurrences that are happening before our eyes in regard to the transfer of property. I think, this is one of the key sections that should help us to defeat the free play of unaccounted money and cheating of the Government."

Now it is true that the speeches made by the Members of the Legislature on the floor of the House when a Bill for enacting a statutory provision is being debated are inadmissible for the purpose of interpreting the statutory provision but the speech made by the mover of the Bill explaining the reason for the introduction of the Bill can certainly be referred to for the purpose of ascertaining the mischief sought to be remedied by the legislation and the object and purpose for which the legislation is enacted. This is an accord with the recent trend in juristic thought not only in western countries but also in India that interpretation of a statute being an exercise in the ascertainment of meaning, everything which is logically relevant should be admissible. In fact there are at least three decisions of this Court, one in *Sole Trustee, Loka Shikshana Trust* v. *CIT* [1975] 101ITR 234, the other in *Indian Chamber of Commerce* v. *CIT* [1975] 101 ITR 796 and the third in *Addl. CIT* v. *Swat Art Silk Cloth Manufacturers Association* [1980] 121 ITR 1, where the speech made by the Finance Minister, while introducing the exclusionary clause in section 2(*15*) of the Act, was relied upon by the Court for the purpose of ascertaining what was the reason for introducing that clause. The speech made by the Finance Minister, while

moving the amendment introducing sub-section (2), clearly states what were the circumstances in which sub-section (2) came to be passed, what was the mischief for which section 52 as it then stood did not provide and which was sought to be remedied by the enactment of sub-section (2) and why the enactment of sub-section (2) was found necessary. It is apparent from the speech of the Finance Minister that sub-section (2) was enacted for the purpose of reaching those cases where there was understatement of consideration in respect of the transfer or to put it differently, the actual consideration received for the transfer was "considerably more" than that declared or shown by the assessee, but which were not covered by sub-section (1) because the transferee was not directly or indirectly connected with the assessee. The object and purpose of sub-section (2), as explicated from the speech of the Finance Minister, was not to strike at honest and *bona fide* transactions where the consideration for the transfer was correctly disclosed by the assessee but to bring within the net of taxation those transactions where the consideration in respect of the transfer was shown at a lesser figure than that actually received by the assessee, so that they do not escape the charge of tax on capital gains by understatement of the consideration. This was real object and purpose of the enactment of sub-section (2) and the interpretation of this sub-section must fall in line with the advancement of that object and purpose. We must, therefore, accept as the underlying assumption of sub-section (2) that there is understatement of consideration in respect of the transfer and sub-section (2) applies only where the actual consideration received by the assessee is not disclosed and the consideration declared in respect of the transfer is shown at a lesser figure than that actually received.

9. This interpretation of sub-section (2) is strongly supported by the marginal note to section 52 which reads "Consideration for transfer in cases of under-statement". It is undoubtedly true that the marginal note to a section cannot be referred to for the purpose of construing the section but it can certainly be relied upon as indicating the drift of the section or, to use the words of Collins MR in *Bushel* v. *Hammond* [1904] 2 KB 563, to show what the section is dealing with. It cannot control the interpretation of the words of a section particularly when the language of the section is clear and unambiguous but, being part of the statute, it *prima facie* furnishes some clue as to the meaning and purpose of the section— *Bengal Immunity Co. Ltd.* v. *State of Bihar* [1955] 2 SCR 603. The marginal note to section 52, as it now stands, was originally a marginal note only to what is presently subsection (1) and significantly enough, this marginal note remain unchanged even after the introduction of sub-section (2) suggesting clearly that it was meant by Parliament to apply to both sub-sections of section 52 and it must, therefore, be taken as indicating that, like sub-section (1), sub-section (2) is also intended to deal with cases where there is understatement of the consideration in respect of the transfer.

10. But apart from these considerations, the placement of sub-section (2) in section 52 does indicate in some small measure that Parliament intended that sub-section to apply only to cases where the consideration in respect of the transfer is understated by the assessee. It is not altogether without significance that the provision in sub-section (2) was enacted by Parliament not as a separate section, but as part of section 52 which, as it originally stood, dealt only with cases of understatement of consideration. If Parliament intended subsection (2) to cover all cases where the condition of 15 per cent difference is satisfied, irrespective whether there is understatement of consideration or not, it is reasonable to assume that Parliament would have enacted that provision as a separate

section and not pitch-forked it into section 52 with a total stranger under an inappropriate marginal note. Moreover there is inherent evidence in sub-section (2) which suggests that the thrust of that sub-section is directed against cases of understatement of consideration. The crucial and important words in sub-section (2) are: "the full value of the consideration declared by the assessee". The word "declared" is very eloquent and revealing. It clearly indicates that the focus of sub-section (2) is on the consideration declared or disclosed by the assessee as distinguished from the consideration actually received by him and it contemplates a case where the consideration received by the assessee in respect of the transfer is not truly declared or disclosed by him but is shown at a different figure. This of course is a very small factor and by itself of little consequence but along with the other factors which we have discussed above, it assumes same significance as throwing light on the true intent of sub-section (2).

11. There is also one other circumstance which strongly reinforces the view we are taking in regard to the construction of sub-section (2). Soon after the introduction of sub-section (2), the CBDT, in exercise of the power conferred under section 119 of the Act, issued a circular dated 7-7-1964 explaining the scope and object of sub-section (2) in the following words:

> "Section 13 of the Finance Act has introduced a new sub-section (2) in section 52 of the Income-tax Act with a view to countering evasion of tax on capital gains through the device of an understatement of the full value of the consideration received or receivable on the transfer of a capital asset.
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> The provision existing in section 52 of the Income-tax Act before the amendment [which has now been renumbered as sub-section (1)] enables the computation of capital gains arising on transfer of a capital asset with reference to its fair market value as on the date of its transfer, ignoring the amount of the consideration shown by the assessee, only if the following two conditions are satisfied:
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> (*a*)the transferee is a person who is directly or indirectly connected with assessee, and
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> (*b*)the Income-tax Officer has reason to believe that the transfer was effected with object of avoidance or reduction of the liability of assessee to tax on capital gains.
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> In view of these conditions, this provision has a limited operation and does not apply to other cases where the tax liability on capital gains arising on transfer of capital assets between parties not connected with each other, is sought to be avoided or reduced by an understatement of the consideration paid for the transfer of the asset."

The circular also drew the attention of the income-tax authorities to the assurance given by the Finance Minister in his speech that subsection (2) was not aimed at perfectly honest and *bonafide* transactions where the consideration in respect of the transfer was correctly disclosed or declared by the assessee, but was intended to deal only with cases where the consideration for the transfer was understated by the assessee and was shown at a lesser figure than that actually received by him. It appears that despite this circular, the income-tax authorities in several cases levied tax by invoking the provision in sub-section (2) even in cases where the transaction was perfectly honest and *bonafide* and there was no under-statement of the consideration. This was quite contrary to the

instructions issued in the circular which was binding on the tax department and the CBDT was, therefore, construed to issue another circular on 14-1-1974 whereby the CBDT, after reiterating the assurance given by the Finance Minister in the course of his speech, pointed out:

> "It has come to the notice of the Board that in some cases the Income-tax Officers have invoked the provisions of section 52(2) even when the transactions were *bona fide.* In this context references is invited to the decision of the Supreme Court in *Navnit Lal C. Jhaveri* v. *K.K. Sen* (56 ITR 198) and *Eilerman Lines Ltd.* v. *Commissioner of Income-tax, West Bengal* (82 ITR 913) wherein it was held that the circular issued by the Board would be binding on all officers and persons employed in the execution of the Income-tax Act. Thus, the Income-tax Officers are bound to follow the instructions issued by the Board."

and instructed the ITO that "while completing the assessments they should keep in mind the assurance given by the Minister of Finance and the provi-sions of section 52(2) of the Income-tax Act may not be invoked in cases of *bona fide* transactions". These two circulars of the CBDT are, as we shall presently point out, binding on the tax department in administering or executing the provisions enacted in subsection (2), but quite apart from their binding character, they are clearly in the nature of *contemporanea expositio* furnishing legitimate aid in the construction of sub-section (2). The rule of construction by reference to *contemporanea expositio* is a well-established rule for interpreting a statute by reference to the exposition it has received from contemporary authority, though it must give way where the language of the statute is plain and unambiguous. This rule has been succinctly and felicitously expressed in Crawford on Statutory Construction (1940 edn.) where it is stated in paragraph 219 that "administrative construction (*i.e.,* contemporaneous construction placed by administrative or executive officers charged with executing a statute) generally should be clearly wrong before it is overturned; such a construction, commonly referred to as practical construction, although non-controlling, is nevertheless entitled to considerable weight; it is highly persuasive." The validity of this rule was also recognised in *Baleshwar Bagarti* v. *Bhagirathi Dass* ILR 35 Cal. 701 where Mookerjee, J. stated the rule in these terms:

> "It is a well-settled principle of interpretation that courts is construing a statute will give much weight to the interpretation put upon it, at the time of its enactment and since, by those whose duty it has been to construe, execute and apply it."

And this statement of the rule was quoted with approval by this Court in *Deshbandhu Gupta & Co.* v. *Delhi Stock Exchange Association Ltd.* [1979] 4 SCC 565. It is clear from these two circulars that the CBDT, which is the highest authority entrusted with the execution of the provisions of the Act, understood subsection (2) as limited to cases were the consideration for the transfer has been understated by the assessee and this must be regarded as a strong circumstance supporting the construction which we are placing on that sub-section.

12. But the construction which is commending itself to us does not rest merely on the principle of *contemporanea expositio.* The two circulars of the CBDT to which we have just referred are legally binding on the revenue and this binding character attaches to the two circulars even if they be found not in accordance with the correct interpretation of sub-section (2) and they depart or deviate from such construction. It is now well-settled as

a result of two decisions of this Court, one in *Navnit Lal C. Jhaveri* v. *K.K. Sen, AAC* [1965] 56 ITR 198 and the other in *Ellerman Lines Ltd.* v. *CIT* [1971] 82 ITR 913, that circulars issued by the CBDT under section 119 of the Act are binding on all officers and persons employed in the execution of the Act even if they deviate from the provisions of the Act. The question which arose in *Navnit Lal C Jhaveri's* case (*supra*) was in regard to the constitutional validity of sections 2(6A)(*e*) and 12(1B) which were introduced in the Indian Income-tax Act, 1922 (hereinafter referred to as "the 1922 Act") by the Finance Act, 1955 with effect from 1-4-1955. These two sections provided that any payment made by a closely-held company to its shareholder by way of advance or loan to the extent to which the company possesses accumulated profit shall be treated as dividend taxable under the Act and this would include any loan or advance made in any previous year relevant to any assessment year prior to the assessment year 1955-56, if such loan or advance remained outstanding on the first day of the previous year relevant to the assessment year 1955-56. The constitutional validity of these two sections was assailed on the ground that they imposed unreasonable restrictions on the fundamental right of the assessee under article 19(1)(*f*) and (*g*) of the Constitution by taxing outstanding loans or advances of past years as dividend. The revenue, however, relied on a circular issued by the CBR under section 5(8) of the 1922 Act which corresponded to section 119 of the 1961 Act and this circular provided that if any such outstanding loans of advances of past years were repaid on or before 30-6-1955, they would not be taken into account in determining the tax liability of the shareholders to whom such loans or advances were given. This circular was clearly contrary to the plain language of section 2(6A)(*e*) and section 12(1B) of the-4922 Act, but even so this Court held that it was binding on the revenue and since "past transactions which would normally have attracted the stringent provisions of section 12(1B) as it was introduced in 1955, were substantially granted exemption from the operation" of the said provisions by making it clear to all the companies and their shareholders that if the past loans were genuinely refunded to the companies they would not be taken into account under section 12(1B)", sections 2(6A)(*e*) and 12(1B) of the 1922 Act did not suffer from the vice of unconstitutionality. This decision was followed in *Ellerman Lines*'case (*supra*) where referring to another circular issued by the CBR under section 5(8) of the 1922 Act on which reliance was placed on behalf of the assessee, this Court observed:

> "Now, coming to the question as to the effect of instructions issued under section 5(8) of the Act, this Court observed in *Navnit Lal C. Jhaveri* v . *K.K. Sen, AAC* [1965] 66 ITR 198, 203:

'It is clear that a circular of the kind which was issued by the Board would be binding on all officers and persons employed in the execution of the Act under section 5(8) of the Act. This circular pointed out to all the officers that it was likely that some of the companies might have advanced loans to their shareholders as a result of genuine transactions of loans, and the idea was not to affect such transactions and not to bring them within the mischief of the new provision.'

The directions given in that circular clearly deviated from the provisions of the Act, yet this Court held that the circular was binding on the Income-tax Officer." (p. 921)

The two circulars of the CBDT referred to above must, therefore, be held to be binding on the revenue in the administration or imple-mentation of sub-section (2) and this

sub-section must be read as applicable only to cases where there is understatement of the consideration in respect of the transfer.

13. Thus, it is not enough to attract the applicability of sub-section (2) that the fair market value of the capital asset transferred by the assessee as on the date of the transfer exceeds the full value of the consideration declared in respect of the transfer by not less than 15 per cent of the value so declared, but it is furthermore necessary that the full value of the consideration in respect of the transfer is understated or, in other words, shown at a lesser figure than that actually received by the assessee. Sub-section (2) has no application in case of an honest and *bonafide* transaction where the consideration in respect of the transfer has been correctly declared or disclosed by the assessee, even if the condition of 15 per cent difference between the fair market value of the capital asset as on the date of the transfer and die full value of the consideration declared by the assessee is satisfied. If, therefore, the revenue seeks to bring a case within sub-section (2), it must show not only that the fair market value of the capital asset as on the date of the transfer exceeds the full value of the consideration declared by the assessee by not less than 15 per cent of the value so declared, but also that the consideration has been understated and the assessee has actually received more than what is declared by him. There are two distinct conditions which have to be satisfied before sub-section (2) can be invoked by the revenue and the burden of showing that these two conditions are satisfied rests on the revenue. It is for the revenue to show that each of these two conditions is satisfied and the revenue cannot claim to have discharged this burden which lies upon it, by merely establishing that the fair market value of the capital asset as on the date of the transfer exceeds by 15 per cent or more the full value of the consideration declared in respect of the transfer and the first condition is therefore satisfied. The revenue must go further and prove that the second condition is also satisfied. Merely by showing that the first condition is satisfied, the revenue cannot ask the Court to presume that the second condition too is fulfilled, because even in a case where the first condition of 15 per cent difference is satisfied, the transaction may be a perfectly honest and *bona fide* transaction and there may be no understatement of the consideration. The fulfilment of the second condition has, therefore, to be established independently of the first condition and merely because the first condition is satisfied, no inference can necessarily follow that the second condition is also fulfilled. Each condition has got to be viewed and established independently before sub-section (2) can be invoked and the burden of doing so is clearly on the revenue. It is a well-settled rule of law that the onus of establishing that the conditions of taxability are fulfilled is always on the revenue and the second condition being as much a condition of taxability as the first, the burden lies on the revenue *to* show that there is understatement of the consideration and the second condition is fulfilled. Moreover, to throw the burden of showing that there is no under statement of the consideration on the assessee would be to cast an almost impossible burden upon him to establish a negative, namely, that he did not receive any consideration beyond that declared by him.

14. But the question then arises why has Parliament introduced the first condition as a prerequisite for the applicability of sub-section (2)? Why has Parliament provided that in order to attract the applicability of sub-section (2), the fair market value of the capital asset as on the date of the transfer should exceed by 15 per cent or more the full of the consideration for the transfer declared by the assessee? The answer is obvious. The

object of imposing the condition of difference of 15 per cent or more between the fair market value of the capital asset and the consideration declared in respect of the transfer clearly is to save the assessee from the rigour of sub-section (2) in marginal cases where difference in subjective valuation by different individuals may result in an apparent disparity between the fair market value and the declared consideration. It is a well-known fact borne out by practical experience that the determination of fair market value of a capital asset is generally a matter of estimate based to some extent) on guess work and despite the utmost *bona fides,* the estimate of the fair market value is bound to vary from individual to individual. It is obvious that if the restrictive condition of difference of 15 per cent or more between the fair market value of the capital asset as on the date of the transfer and the consideration declared in respect of the transfer were not provided in sub-section (2), many marginal cases would, having regard to the possibility of difference of opinion in subjective assessment of the fair market value, fall within the mischief of that sub-section and the statutory measure enacted in that sub-section for determining the consideration actually received by the assessee would be applicable in all its rigour in such cases. This condition of 15 per cent or more difference is merely intended to be a safeguard against undue hardship which would be occasioned to the assessee if the inflexible rule of the thumb enacted in sub-section (2) were applied in marginal cases and it has nothing to do with the question of burden of proof, for the burden of establishing that there is understatement of the consideration in respect of the transfer always rests on the revenue. The postulate underlying sub-section (2) is that the difference between one honest valuation and another may range up to 15 per cent and that constitutes the class of marginal cases which are taken out of the purview of subsection (2) in order to avoid hardship to the assessee.

15. It is, therefore, clear that sub-section (2) cannot be invoked by the revenue unless there is understatement of the consideration in respect of the transfer and the burden of showing that there is such understatement is on the revenue. Once it is established by the revenue that the consideration for the transfer has been understated or, to put it differently, the consideration actually received by the assessee is more than what is declared or disclosed by him, sub-section (2) is immediately attracted, subject, of course, to the fulfilment of the condition of 15 per cent or more difference, and the revenue is then not required to show what is the precise extent of the understatement or, in other words, what is the consideration actually received by the assessee. That would in most cases be difficult, if not impossible, to show and hence sub-section (2) relieves the revenue of all burden of proof regarding the extent of understatement of concealment and provides a statutory measure of the consideration received in respect of the transfer. It does not create any fictional receipt. It does not deem as receipt something which is not in fact received. It merely provides a statutory best judgment assessment of the consideration actually received by the assessee and brings to tax capital gains on the footing that the fair market value of the capital asset represents the actual consideration untruly declared or disclosed by him. This approach in construction of sub-section (2) falls in line with the scheme of the provisions relating to tax on capital gains. It may be noted that section 52 is not a charging section but is a computation section. It has to be read along with section 48 which provides the mode of computation and under which the starting point of computation is "the full value of the consideration received or accruing". What in fact never accrued or was never received cannot be computed as capital gains under section

48, Therefore, sub-section (2) cannot be construed as bringing within the computation of capital gains an amount which, by no stretch of imagination, can be said to have accrued to the assessee or been received by him and it must be confined to cases where the actual consideration received for the transfer is understated and since in such cases it is very difficult, if not impossible, to determine and prove the exact quantum of the suppressed consideration, subsection (2) provides the statutory measure for determining the consideration actually received by the assessee and permits the revenue to take the fair market value of the capital asset as the full value of the consideration received in respect of the transfer.

16. This construction which we are placing on sub-section (2) also marches in step with the Gift-tax Act. If a capital asset is transferred for a consideration below its market value, the difference between the market value and the full value of the consideration received in respect of the transfer would amount to a gift liable to tax under the Gift-tax Act, but if the construction of sub-section (2) contended for on behalf of the revenue were accepted, such difference would also be liable to be added as part of capital gains taxable under the provisions of the Act. This would be an anomalous result which could never contemplated by the Legislature, since the Income-tax Act and the Gift-tax Act are parts of an integrated scheme of taxation and the same amount which is chargeable as gift could not be intended to be charged also as capital gains.

17. Moreover, if sub-section (2) is literally cons trued as applying even to cases where the full value of the consideration in respect of the transfer is correctly declared or disclosed by the assessee and there is no understatement of the consideration, it would result in an amount being taxed which has neither accrued to the assessee nor been received by him and which from no view point can be rationally considered as capital gains or any other type of income. It is a well-settled rule of interpretation that the Court should as far as possible avoid that construction which attributes irrationality to the Legislature. Besides, under entry 82 in List I of the Seventh Schedule to the Constitution, which deals with "Taxes on income other than agricultural income" and under which the Income-tax Act, has been enacted, Parliament cannot "choose to tax as income an item which in no rational sense can be regarded as a citizen's income or even receipt. Sub-section (2) would, therefore, on the construction of the revenue, go outside the legislative power of Parliament and it would not be possible to justify it even as an incidental or ancillary provision or a provision intended to prevent evasion of tax. Sub-section (2) would also be violative of the fundamental right of the assessee under article 19(1)(*f*)—which fundamental right was in existence at the time when sub-section (2) came to be enacted—since, on the construction canvassed on behalf of the revenue, the effect of sub-section (2) would be to penalise the assessee for transferring his capital asset for a consideration lesser by 15 per cent or more than the fair market value and that would constitute unreasonable restriction on the fundamental right of the assessee to dispose of his capital asset at the price of his choice. The Court must obviously prefer a construction which renders the statutory provision constitutionally valid rather than that which makes it void.

18. We must, therefore, hold that sub-section (2) of section 52 can be invoked only where the consideration for the transfer has been understated by the assessee or, in other words, the consideration actually received by the assessee is more than what is declared or disclosed by him and the burden of proving such understatement or concealment is on

the revenue. This burden may be discharged by the revenue by establishing facts and circumstances from which a reasonable inference can be drawn that the assessee has not correctly declared or disclosed the consideration received by him and there is understatement or concealment of consideration in respect of the transfer. Sub-section (2) has no application in case of an honest and *bona fide* transaction where the consideration received by the assessee has been correctly declared or disclosed by him, and there is no concealment or suppression of the consideration. We find that, in the present case, it was not the contention of the revenue that the property was sold by the assessee to his daughter-in-law and five of his children for a consideration which was more than the sum of Rs. 16,500 shown to be the consideration for the property in the instrument of transfer and there was understatement or concealment of the consideration in respect of the transfer. It was common ground between the parties and that was a finding of fact reached by the income-tax authorities that the transfer of the property by the assessee was a perfectly honest and *bona fide* transaction where the full value of the consideration received by the assessee was correctly disclosed at the figure of Rs. 16,500. Therefore, on the construction placed by us, sub-section (2) had no application to the present case and the ITO could have no reason to believe that any part of the income of the assessee had escaped assessment so as to justify the issue of a notice under section 148. The order of reassessment made by the ITO pursuant to the notice issued under section 148 was accordingly without jurisdiction and the majority judges of the Full Bench were in error in refusing to quash it.

19. We accordingly allow the appeal, set aside the order passed by the Full Bench and restore the order of Isaac, J., allowing the writ petition and quashing the order of reassessment made by the ITO. The revenue will pay the costs of the assessee throughout.