THE HIGH COURT OF DELHI AT NEW DELHI

% Judgment delivered on: 24.07.2013

\+ W.P.(C) No.1272/2013

AAA PORTFOLIOS PVT. LTD & ORS. ..... Petitioners

versus

THE DEPUTY COMMISSIONER OF INCOME TAX & ORS. …. Respondents

Advocates who appeared in this case:

For the Petitioners : Mr Parag P. Tripathi, Sr. Advocate with Mr Simran Mehta, Mr R.M. Mehta, Ms Yogita Sunaria and Ms Mahima Gupta

For the Respondent : Mr Sanjeev Sabharwal and Mr Puneet Gupta for R-1.
Mr Sumit Bansal and Mr Ateev Mathur for R-2.
Mr Y.K. Kapur for R-3.

CORAM:-
HON'BLE MR JUSTICE BADAR DURREZ AHMED, ACTING CHIEF JUSTICE
HON'BLE MR JUSTICE VIBHU BAKHRU

JUDGMENT

VIBHU BAKHRU, J

1. This is a writ petition filed by the petitioners challenging the order dated 01.02.2013 passed by Respondent no.1 (hereinafter referred to as the "Assessing Officer") and the consequential notice dated 04.02.2013 issued under Section 226(3) of the Income Tax Act,1961 (hereinafter referred to as the "Act"). The petitioners are aggrieved on account of the action of the Assessing Officer in appropriating a sum of ₹95,85,30,934/- which was lying in escrow with respondent No.2 bank.

2. The petitioners held shares in respondent No.3 company, namely, Escorts Heart Institute & Research Centre Ltd. (hereinafter referred to as the "assessee company"). Petitioner Nos.1 & 2 held 1,00,000 shares each of the assessee company and the petitioner No.3 held 16,00,000 shares of the assessee company. The petitioners along with three other entities, namely Charak Ayurvedic Institute, Escorts Employees Welfare Trust and Diamond Leasing and Finance Limited who held 100 shares of the assessee company each entered into a share purchase agreement dated 25.9.2005 for sale of their shares in the assessee company to M/s Fortis Health Care Ltd. (hereinafter referred to as the "purchaser"). In all 18,00,300 shares of the assessee company which aggregated 90.01% of the issued and paid up share capital of the assessee company were agreed to be sold by the petitioners and three other entities (hereinafter collectively referred to as the "sellers"). The consideration for the sale of 18,00,300 shares of the assessee company was agreed at ₹585,00,97,485/- @ ₹3249.51 per share. As agreed under the share purchase agreement, the purchaser was required to deposit the entire consideration with the escrow agent and the sellers agreed to deposit certain documents including share transfer deeds and instructions with the escrow agents in order to consummate the transaction for sale and purchase of an aggregate of 18,00,300 equity shares of the assessee company. The shares held by petitioner No.3 were pledged with certain lenders and the escrow agent was required to release part of the consideration to the lenders in order that the petitioner No.3 could redeem the pledge and transfer unencumbered shares to the purchaser.

3. It was agreed between the sellers and the purchaser that the escrow agent would release ₹3,24,951/- each to Charak Ayurvedic Institute, Escorts Employees Welfare Trust and Diamond Leasing and Finance Limited as consideration for the sale of the 100 shares each held by them in the assessee company and out of

the balance consideration deposited by the purchaser an aggregate sum of ₹149,99,02,514/- would be withheld with the escrow agent and the remaining balance amount would be released to the petitioner No.3. The amount to be withheld by the escrow agent included a sum of ₹64,99,02,514/- which was the entire consideration payable to petitioner Nos.1 and 2 for sale of their shares in the assessee company to the purchaser.

4. The purpose for withholding the sum of ₹64,99,02,514/- from the sale consideration payable by the purchaser was on account of the income tax liability of the assessee company that was being contested. It is relevant to state that M/s Escorts Heart Institute and Research Centre, which was a charitable society was merged with another society and subsequently, the same was converted into a company incorporated under the Companies Act, namely, the assessee company. The Assessing Officer denied the exemption to the assessee company under Section 35(1)(ii) of the Act and passed an assessment order for the assessment year 2001-2002 raising a demand of ₹124.36 crores. The said demand is disputed by the assesssee company. As there were disputes pending with the Income Tax Department regarding the tax liability of the assessee company, it was agreed between the purchaser and the petitioners that a certain sum would be held back from the sale consideration by the escrow agent and would not be released to the petitioners until the income tax liability of the assessee company was finally adjudicated. In the event that the income tax liability of the assessee company exceeded the amount withheld by the escrow agent from the sale consideration, the same would not be released to the petitioners but would be returned to the purchaser. However, in the event, the tax liability of the assessee company was less than the amount withheld by the escrow agent then the amount equal to the income tax liability of the assessee company would be refunded to the purchaser and the balance would be released to the petitioners.

5. Pursuant to the share purchase agreement dated 25.09.2005, the sellers and the purchaser and respondent no. 2 entered into an Escrow Agreement dated 27.09.2005 which, *inter alia*, recorded the obligations of respondent no.2 as the escrow agent.

6. The Assessing Officer issued a notice under Section 226(3) of the Act to respondent no. 2 bank in respect to the amount held by respondent no. 2 as an escrow agent in terms of the Escrow Agreement dated 27.09.2005. The said notice was objected to and it was clarified by respondent no. 2 that it was not holding any money on account of the assessee company. The Assessing Officer sent another similar notice dated 15.02.2007 without considering the objections of the respondent no. 2 bank.

7. The Assessing Officer sent a notice dated 16.07.2008 directing the respondent no. 2/bank to remit a sum of ₹ 64,99,02,514/- which was lying in fixed deposits to the Assessing Officer by 17.07.2008.

8. The notice dated 16.07.2008 was challenged by petitioner no. 1 and 2 by filing a writ petition, being writ petition no. 5080/2008 in this Court. This Court passed an interim order dated 17.07.2008 staying the operation of the notice dated 16.07.2008 and after hearing parties, remanded the matter to the Assistant Commissioner of Income-tax to decide whether the petitioner had a *locus standi* in the matter and to pass a reasoned order after considering the submissions of the petitioners.

9. It was contended before the Assessing Officer on behalf of the petitioners that the action under Section 226(3) of the Act was in the nature of garnishee proceedings where the revenue steps into the shoes of the assessee and recovers money directly from a third party who owes money to the assessee. It was further contended that respondent no. 2 does not either hold any money on account of the

assessee company or owe any money to the assessee company and therefore, the sums held by the respondent no. 2 in escrow pursuant to the Escrow Agreement dated 27.09.2005 cannot be demanded by the revenue.

10. The respondent no. 2 bank also furnished an affidavit dated 07.12.2012 unequivocally affirming that the fixed deposit of ₹ 94,84,96,05.97/- was held by respondent no.2 in terms of the Escrow Agreement and that no part of the same was owed to or held on account of the assessee company. The relevant extract from the affidavit dated 07.12.2012 furnished by respondent no. 2 to the Assessing Officer is quoted below:-

> "4. That the Bank is holding Fixed Deposit of Rs 94,84,96,005.97 (Rupees Ninety four crores eighty four lakhs ninety six thousand five and paise ninety seven only) as 'Escrow Agent' in terms of Escrow Agreement dated 27.09.2005 executed by and between Escorts Limited, AAA Portfolio Pvt. Ltd., Big Apple Clothing Pvt. Ltd., Charak Ayurvedic Institute, Escorts Employees Welfare Trust, Diamond Leasing & Finance Ltd., Fortis Healthcare Ltd. and HDFC Bank Limited.
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> 5. That no part of the amount lying in the 'Escrow Account' is owed to or belongs to or held by the Bank or may be subsequently held by the Bank on account of M/s Escorts Heart Institute & Research Centre, Delhi".

11. The Assessing Officer after considering the submission of the petitioners passed the impugned order dated 01.02.2013. After quoting the relevant clauses from the Escrow Agreement the Assessing Officer held as under:-

> "From the above quoted excerpts of the Escrow agreement, it is amply clear that any Income Tax Demand arising on account of merger of Escort Heart Institute and Research Center Delhi with EHIRCL, Chandigarh and/or the conversation of the merged entity into a Part IX company under the Companies Act, 1956 has to be paid by the ESCROW Account. The said demand has been raised due to the withdrawal of exemption of the Escort Heart Institute and

> Research Center, Delhi as it got merged with the Chandigarh Society which was a non-charitable society. Therefore, it can be concluded without doubt that the said amount of money has been kept in the ESCROW Account for meeting Income Tax demands only. So the notice u/s 226(3) sent by the ACIT dated 10.10.2006 is very much in accordance with ESCROW Agreement and Income Tax Act."

12. Pursuant to the impugned order, the Assessing Officer sent a notice dated 04.02.2013 under Section 226(3) of the Act calling upon respondent no. 2 to forthwith pay the amount held by respondent no.2 by way of fixed deposits pursuant to the Escrow Agreement. Thereafter, respondent no. 2 paid a sum of ₹95,85,30,934/- to the Assessing Officer in compliance of the notice dated 04.02.2013.

13. The controversy in the present writ petition essentially revolves around the question whether respondent no. 2 held any money on account of the assessee company pursuant to the Escrow Agreement. While it is contended on behalf of the petitioners that the amount kept in escrow with the respondent bank belongs to petitioner no. 1 & 2 being the sale consideration receivable by them for sale of their shares to the purchaser, the impugned order holds to the contrary.

14. The other aspect that is required to be considered is whether respondent no.2 could be compelled to makeover the funds held in escrow despite an affidavit being furnished on behalf of respondent no.2 that it did not hold any sum on account of the assessee company.

15. Before proceeding further it would be relevant to examine the provisions of Section 226 of the Act. Section 226 falls within chapter XVII of the Act, which contains the machinery provisions for collection and recovery of income tax. Section 226 of the Act provides for other modes of recovery of tax due from an assessee. Section 226(3) of the Act is relevant for considering the controversy

in the present matter and the relevant clauses of Section 226 of the Act are quoted below:-

> **"226. - Other modes of recovery.**
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> xxxx xxxx xxxx xxxx xxxx
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> (3) (*i*) The Assessing Officer or Tax Recovery Officer may, at any time or from time to time, by notice in writing require any person from whom money is due or may become due to the assessee or any person who holds or may subsequently hold money for or on account of the assessee to pay to the Assessing Officer or Tax Recovery Officer either forthwith upon the money becoming due or being held or at or within the time specified in the notice (not being before the money becomes due or is held) so much of the money as is sufficient to pay the amount due by the assessee in respect of arrears or the whole of the money when it is equal to or less than that amount.
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> (*ii*) A notice under this sub-section may be issued to any person who holds or may subsequently hold any money for or on account of the assessee jointly with any other person and for the purposes of this sub-section, the shares of the joint holders in such account shall be presumed, until the contrary is proved, to be equal.
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> (*iii*) A copy of the notice shall be forwarded to the assessee at his last address known to the Assessing Officer or Tax Recovery Officer, and in the case of a joint account to all the joint holders at their last addresses known to the Assessing Officer or Tax Recovery Officer.
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> (*iv*) Save as otherwise provided in this sub-section, every person to whom a notice is issued under this sub-section shall be bound to comply with such notice, and, in particular, where any such notice is issued to a post office, banking company or an insurer, it shall not be necessary for any pass book, deposit receipt, policy or any other document to be produced for the purpose of any entry, endorsement or the like being made before payment is made, notwithstanding any rule, practice or requirement to the contrary.
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> (*v*) xxxx xxxx xxxx xxxx xxxx

(*vi*) Where a person to whom a notice under this sub-section is sent objects to it by a statement on oath that the sum demanded or any part thereof is not due to the assessee or that he does not hold any money for or on account of the assessee, then nothing contained in this sub-section shall be deemed to require such person to pay any such sum or part thereof, as the case may be, but if it is discovered that such statement was false in any material particular, such person shall be personally liable to the Assessing Officer or Tax Recovery Officer to the extent of his own liability to the assessee on the date of the notice, or to the extent of the assessee's liability for any sum due under this Act, whichever is less."

16. The provisions of Section 226(3) of the Act provide the machinery for enabling an Assessing Officer to recover the amount of income tax due from an assessee by recovering sums from any person who owes any money to the assessee or holds any money on his account. Section 226(3) of the Act confers upon an Assessing Officer a special jurisdiction to proceed directly against a person, other than an assessee, for recovery of income-tax demands due from the assessee. The power conferred under Section 226(3) of the Act is a special power that enables the Assessing Officer to reach beyond the assessee in order to appropriate amounts due to or held by third parties on account of the assessee. The proceedings under Section 226(3) of the Act are in the nature of garnishee proceedings whereby a garnishee is called upon to directly pay a debt to the creditor of a person to whom the garnishee is indebted. The Assessing Officer is similarly situated as a garnisher and is in a position to initiate action under Section 226(3) of the Act to reach out to the property of the assessee which is held by a third party or to any sum which is owed by a third party to the assessee. The Assessing Officer steps into the shoes of an assessee with respect to recovering sums owed to or held by the garnishee on account of the assessee. An Assessing Officer is not conferred with any additional rights in respect of any amount due from the garnishee other than that which are available to the assessee.

17. Section 226(3) of the Act neither confers jurisdiction nor provides a machinery for an Assessing Officer to adjudicate the indebtedness of a third party to the assessee and the provisions of section 226(3) must be confined to those cases where a third party admits to owing money or holding any money on account of the assessee or in cases where it is indisputable that the third party owes money to or holds money on account of the assessee. However, in cases where there are contentious issues raised by a third party who disputes his liability to pay any money to the assessee there is no mechanism provided or jurisdiction conferred upon the Assessing Officer to proceed further in the matter and take upon himself the mantle of adjudicating the said disputes.

18. A Division Bench of the Calcatta High Court in the case of ***Shaw Wallace and Co. Ltd. v. Union of India***: **(2003) 262 ITR 528 (Cal.)** also expressed a similar view and held as under:

> "In the facts and circumstances of the case whether the decree had been put to execution by VCVL or not is immaterial. If the decree is offered, the Tax Recovery Officer is free to proceed upon it under section 226(3) of the Act. But by reason of clause (vi) thereof the judgment debtor/garnishee has a right to object. As soon as objected, to the Tax Recovery Officer cannot proceed to recover until discovery of falsity of the objection. If the executability of the decree is challenged, the Tax Recovery Officer cannot assume jurisdiction to decide a dispute between the garnishee and the assessee. He cannot usurp the jurisdiction of the executing court. The jurisdiction of the Tax Recovery Officer is confined within the dispute between the assessee and the income tax authority. He cannot assume jurisdiction in respect of any dispute between the assessee and the garnishee nor can he embark upon an exercise to determine any such dispute unless it appears to be false on the face of it. As soon there appears to be a dispute prima facie, the objection cannot be presumed to be false. The proceedings under section 226(3) of the Act would then be subject to the determination by the appropriate forum. Until determination, the Tax Recovery Officer has no scope of discovering the falsity of the objection. When the

> garnishee does not admit or denies that he owes the debt to the assessee, the Tax Recovery Officer cannot sit in judgment over the denial and come to his own conclusion. It was so held in *Mohamedaly Sarafaly and Co. v. ITO* [1968] 68 ITR 128, 131 (Mad) and *P. K. Trading Co. v. ITO* [1970] 78 ITR 427, 433 (Cal). Once on oath the garnishee denies the liability towards the assessee, the burden of showing the statement on oath is false in any material particular would be upon the Revenue. The Revenue has to disclose material particulars that led it to a definite conclusion. Then only the payment can be imposed on the garnishee under section 226(3)(vi) of the Act. The apex court had taken such a view in *Beharilal Ramcharan v. ITO* [1981] 131 ITR 129, 137- 38. It is only when the objection is altogether false and it is so apparent and is so discovered that the Tax Recovery Officer can proceed against the garnishee under section 226(3) of the Act. It is only the part, which cannot be objected to would come within its purview."

19. It is well settled that even in cases of garnishee proceeding under Order 21 Rule 46 of the Code of Civil Procedure (hereinafter referred to as the "CPC"), the Court may pass a garnishee order enabling a judgment creditor to obtain satisfaction of his claim only in those cases which are similar in scope as to judgments on admission under Order 12 Rule 6 of the CPC. A Court cannot issue garnishee order under Order 21 Rule 46 of the CPC against a debtor of the judgment debtor who disputes his indebtedness unless an issue in this regard is struck and tried as provided under Order 21 Rule 46C of the CPC. Unlike the CPC, Section 226(3) of the Act does not have any provision similar to Order 21 Rule 46C of the CPC which confers jurisdiction on the Assessing Officer to adjudicate the question regarding indebtedness of a third party to an assessee who disputes the same. Once the third party noticee has disputed that he owes any money or holds any money on account of the assessee, the Assessing Officer would not have any jurisdiction to proceed further against the third party. This is also abundantly clear from the language of clause (vi) of Section 226(3) of the Act.

20. The Supreme Court has in the case of ***Surinder Nath Kapoor v. Union of India***: **AIR 1988 SC 1777**, observed as under:

> "15. The object of serving a notice under clause (3)(vi) of section 226 is to give the garnishee an opportunity to admit or deny his liability for the amount mentioned in the notice. Under clause (i) of section 226(3), if the garnishee objects to the notice by a statement on oath that the sum demanded or any part thereof is not due to the assessee, then the garnishee will not be required to pay any such sum or part thereof, as the case may be."

21. In the present case, respondent no. 2 bank has furnished an affidavit unequivocally affirming that no part of the amount held by respondent no. 2 in escrow is owed to or belongs to or is held by respondent no. 2 on account of the assessee company. In view of the affidavit dated 07.12.2012 furnished by the respondent no. 2 bank, the Assessing Officer had no jurisdiction to proceed further and call upon the respondent no. 2 bank to makeover the funds held by respondent no. 2 as an escrow agent pursuant to the Escrow Agreement dated 27.09.2005, to the Assessing Officer. In this view, the impugned order dated 01.02.2013 and impugned notice dated 04.02.2013 are wholly without jurisdiction and are thus liable to be set aside.

22. In view of our finding that the decision of the Assessing Officer to proceed further despite the affidavit dated 07.12.2012 furnished by respondent no. 2 bank is without jurisdiction, it is not necessary to examine the question whether the amount held by respondent no. 2 bank pursuant to the Escrow Agreement could be stated to be any money which is due or may become due to the assessee company or which is held for and on account of the assessee company. However, we have heard counsel for the parties in this regard and deem it appropriate to examine the same.

23. Indisputably the monies held by respondent no. 2 bank are a part of the consideration which has been deposited by the purchaser for purchase of the shares of the assessee company from the sellers in terms of the Share Purchase Agreement dated 25.09.2005 entered into between the sellers and the purchaser. The assessee company is not a party to the said agreement. The Share Purchase Agreement dated 25.09.2005 contains the agreed covenants with regard to the escrow arrangement as agreed between the petitioners and the purchaser. Clause 2.9 of the Share Purchase Agreement is relevant and is quoted below:-

> "2.9 The Escrow Agent, shall deal with the Heldback Amount No.2 as under:-
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> AAA and Apple agree that the amount of their respective share of the Sale Consideration being Rs. 32,49,51,257 (Rupees Thirty Two Crores Forty Nine Lakhs Fifty One Thousand Two Hundred Fifty Seven Only) each aggregating to Rs,64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) to which they are entitled under this Agreement, shall be retained by the Escrow Agent and shall be invested by the Escrow Agent in capital gains tax saving bonds in the names of AAA and Apple in equal proportions (the "Securities"). The Securities shall be kept in the custody of the Escrow Agent and shall be retained as security towards settlement of the Income Tax claim/demand of the Company subject to such Income Tax claim/demand having been finally adjudicated in law or finally settled, as the case may be. EL and the Purchaser hereby agree that the Income Tax claim/demand shall be defended by EL at its own cost in mutual consultation with the Purchaser and the Company. In the event EL is desirous of settling the Income Tax claim/demand it shall do so only with the prior written consent of the Purchaser and the Company, which consent shall not be unreasonably withheld.
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> For the purposes of this Article 2.9, Income Tax claim/demand shall mean any Income Tax and/or Capital Gain Tax claim/demand including interest and penalty thereon, if any, made on the Company on account of or in connection with the

merger of Escorts Heart Institute and Research Centre Delhi with Escorts Heart Institute and Research Centre, Chandigarh and/or the conversion of the merged entity into a Part IX Company under the Companies Act, 1956, including all legal expenses incurred by EL for defending the Income Tax claim/demand.

Provided that EL shall have right to substitute the Securities with cash or such other securities as may be acceptable to the Purchaser by depositing an amount with the Escrow Agent, equivalent to the value of total Securities including interest accrued thereon up to the date of such substitution by EL. In the event EL substitutes the Securities with either cash or such other securities, the Securities in the names of AAA and Apple shall be released by the Escrow Agent to AAA and Apple along with interest accrued thereon.

The Parties hereby agree and undertake that the Heldback Amount No.2 shall be utilized in the manner provided below:

(a) In the event the Income Tax claim/demand is equal to Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) together with all interest accrued thereon, the entire amount of Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) together with all interest accrued thereon shall be paid to the Purchaser in the first instance by EL under intimation to the Escrow Agent by EL, within two Business Days of the Company notifying EL, the Purchaser and the Escrow Agent, failing which by the Escrow Agent in favour of the Purchaser from the amount invested in securities or held in cash by the Escrow Agent as the case may be, together with all interest accrued thereon. In the event the said amount is paid directly by EL to the Purchaser the Escrow Agent, under instructions of EL, shall release to EL and/or AAA and/or Apple as the case may be, the amount (if in cash) or securities, as the case may be together with all interest accrued thereon held by the Escrow Agent.

(b) In the event the Income Tax claim/demand exceeds Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs

Two Thousand Five Hundred Fourteen Only), together with all interest accrued thereon, an amount of Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) together with all interest accrued thereon shall be paid to the Purchaser in the first instance by EL under intimation to the Escrow Agent by EL, within two Business Days of the Company notifying EL, the Purchaser and the Escrow Agent, failing which by the Escrow Agent in favour of the Purchaser from the amount invested in securities or held in cash by the Escrow Agent as the case may be, together with all interest accrued thereon. The balance amount being difference between aforesaid Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) together with all interest accrued thereon and the Income Tax claim/demand shall be borne by EL and the Purchaser in the ratio of 1/3 and 2/3 respectively.

EL hereby undertakes to pay its 1/3 share to the Purchaser within two Business Days of the Company notifying EL, the Purchaser and the Escrow Agent. In the event there is a delay in payment to Purchaser by EL of its aforesaid 1/3 share, interest @ 15% per annum on the aforesaid 1/3 share or part thereof which shall remain payable by EL to the Purchaser shall commence with effect from the expiry of two Business Days until payment to the Purchaser. In the event the said amount is paid directly by EL to the Purchaser, the Escrow Agent under instructions of EL, shall release to EL and/or AAA and/or Apple as the case may be, the amount (if in cash) or securities as the case may be together with all interest accrued thereon held by the Escrow Agent.

(c) In the event the Income Tax claim/demand is less than Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) together with all interest accrued thereon, the Income Tax claim/demand shall be paid to the Purchaser by EL in the first instance under intimation to the Escrow Agent by EL, within two Business Days of the Company notifying EL, the Purchaser and the Escrow Agent, failing which by the Escrow Agent in favour of the Purchaser from the amount invested in securities or held in cash by the Escrow Agent as the case may be, together with all

interest accrued thereon. The Escrow Agent shall pay to EL the balance amount along with interest accrued thereon available with the Escrow Agent after payment of the Income Tax claim/demand. In the event the said amount is paid directly by EL to the Purchaser the Escrow Agent, under instructions of EL, shall release to EL and/or AAA and/or Apple as the case may be, the amount (if in cash) or securities as the case may be together with all interest accrued thereon held by the Escrow Agent.

The Escrow Agent is hereby authorised jointly and/or severally by AAA**,** Apple and EL to deal with cash or the securities being Heldback Amount No.2, to give effect to the provisions of this Article 2.9.

On the Income Tax claim/demand being paid to the Purchaser in a manner as contemplated under this Article 2.9 (a), (b) and (c), EL and/or AAA and/or Apple shall stand discharged all of its obligations."

24. Pursuant to the Share Purchase Agreement dated 25.09.2005 the sellers, the purchaser and respondent no. 2 entered into an Escrow Agreement dated 27.09.2005 which, *inter alia*, recorded the obligations of respondent no.2 as the escrow agent. Clause 4.4 & clause 4.5 of the Escrow Agreement are relevant as the same relate to the sums agreed to be placed with the escrow agent with respect to the income tax liability of the assessee company. Clause 4.4 and 4.5 the Escrow Agreement are quoted below:-

"4.4 The Escrow Agent, shall deal with the Heldback Amount No.2 as under:-

(a) Parties agree that the amount under Heldback Amount No.2 comprise of respective shares of AAA and Apple in the Sale Consideration being Rs.32,49,51,257 (Rupees Thirty Two Crores Forty Nine Lakhs Fifty One Thousand Two Hundred Fifty Seven Only) each aggregating to Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only).

(b) Parties further agree that Heldback Amount No.2 shall be retained and invested on behalf of AAA and Apple by the Escrow Agent in two separate fixed deposits (the "Fixed Deposits") of Rs.32,49,51,257 (Rupees Thirty Two Crores Forty Nine Lakhs Fifty One Thousand Two Hundred Fifty Seven Only) each maintained with the Escrow Agent in the name of the Escrow Account. The Fixed Deposits shall be of a tenor of five years and one day each and would be encashable/renewable from time to time by Escrow Agent without any further approval, consent or notice from AAA, Apple, EL and/or Purchaser, as the case may be, unless Escrow Agent is in receipt of any joint instructions to the contrary from EL and Purchaser.

(c) Parties further agree that Heldback Amount No.2 in the form of Fixed Deposits shall be retained by the Escrow Agent as custodian towards settlement of the Income Tax claim/demand of the Company.

Provided that EL shall have right to substitute the Fixed Deposits with cash or such other securities (Fixed Deposits along with cash and such other substituted securities shall hereinafter be referred to as the "Securities") as may be acceptable to the Purchaser and the Escrow Agent, by depositing such Securities with the Escrow Agent, equivalent to the value of total Fixed Deposits/substituted Securities including interest accrued thereon up to the date of such substitution by EL. In the event EL substitutes the Fixed Deposits with cash or other securities, the Fixed Deposits or any balance held in respect of Heldback Amount No.2 shall be released by the Escrow Agent to AAA and Apple in the proportion of their respective shares in the Sale Consideration along with interest accrued thereon.

For the purposes of this Clause 4.4, Income Tax claim/demand shall mean any Income Tax and/or Capital Gain Tax claim/demand including interest and penalty thereon, if any, made on the Company on account of or in connection with the merger of Escorts Heart Institute and Research Centre Delhi with Escorts Heart Institute and Research Centre, Chandigarh and/or the conversion of the merged entity into a Part IX Company under the Companies Act, 1956, including all legal

expenses incurred by EL for defending the Income Tax claim/demand.

4.5 The Parties hereby agree and undertake that the Heldback Amount No.2 or any balance in respect thereof shall be disbursed either to the Sellers or the Purchaser in accordance with the manner specified below:

(a) In the event the Income Tax claim/demand is equal to Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) together with all interest accrued thereon, the entire amount of the Securities or any balance in respect thereof shall be paid to the Purchaser upon receipt of a opinion in writing by the Escrow Agent from the Purchaser obtained by the Purchaser from one amongst the following accounting firms, namely Price Waterhouse, Ernst & Young, Delloitte, Touche & Tohmatsu and KPMG certifying/stating that the demand pertains to Income Tax claim/demand.

(b) In the event the Income Tax claim/demand exceeds Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only), together with all interest accrued thereon, the entire amount of the Securities or any balance in respect thereof shall be paid to the Purchaser upon receipt of a opinion in writing by the Escrow Agent from the Purchaser, obtained by the Purchaser from one amongst the following accounting firms, namely Price Waterhouse, Ernst & Young, Delloitte, Touche & Tohmatsu and KPMG certifying/stating that the demand pertains to Income Tax claim/demand. The balance amount after payment of the Income Tax demand/claim as aforesaid shall be borne and paid by the Seller and the Purchaser in terms of the SPA.

(c) In the event the Income Tax claim/demand is crystallised in part or is less than Rs.64,99,02,514 (Rupees Sixty Four Crores Ninety Nine Lakhs Two Thousand Five Hundred Fourteen Only) together with all interest accrued thereon, the Income Tax claim/demand crystallised in part shall be paid to the Purchaser upon receipt of a opinion in writing by the Escrow Agent from the Purchaser, obtained by the Purchaser from one amongst the following accounting firms, namely Price Waterhouse, Ernst &

> Young, Delloitte, Touche & Tohmatsu and KPMG certifying/stating that the demand pertains to Income Tax claim/demand. The balance amount after disbursement of the Income Tax claim/demand to the Purchaser as specified in this paragraph shall be released by the Escrow Agent to EL and/or AAA and/or Apple as the case may be only upon receipt of joint instructions from EL and the Purchaser that there is no other Income Tax claim/demand pending and/or to be discharged."

25. A plain reading of the Share Purchase Agreement dated 25.09.2005 and the Escrow Agreement dated 27.09.2005 would indicate that the conclusion drawn by the Assessing Officer that respondent no. 2 held any money on account of the assessee company is patently erroneous. Neither the Share Purchase Agreement nor the Escrow Agreement provides for any contingency which would enable the assessee company or any other party to insist that the funds held by the respondent no. 2 bank in escrow be paid either to the assessee company or to the Income-tax Department on account of the assessee company.

26. The reason why the purchaser and the sellers agreed to keep part of the sale consideration paid by the purchaser in escrow with respondent no. 2 bank is apparent from the terms of the Share Purchase Agreement and the Escrow Agreement. The assessee company whose shares were being transacted had been converted from a society with whom a charitable society had been merged. As per the Revenue these transactions had resulted in an income-tax liability upon the assessee company which was disputed by the assessee company. In the event, the income-tax as demanded was finally adjudicated to be payable, it would have an adverse effect on the value of the shares of the assessee company which were subject matter of the transaction. Thus, in order to indemnify the purchaser against such adverse effect in the value of the shares of the assessee company being acquired by the purchaser, an amount of ₹64,99,02,514/- (referred to as "Heldback Amount no.2" in the Share Purchase Agreement and

the Escrow Agreement) was agreed to be withheld and kept in escrow with respondent no. 2 bank, from the consideration payable for purchase of the shares of the assessee company. In the event the liability of the assessee company on account of or in connection with the merger of Escorts Heart Institute and Research Centre Delhi with Escorts Heart Institute and Research Centre, Chandigarh and/or the conversion of the merged entity into a company under the Companies Act, 1956, including all legal expenses incurred by petitioner no. 3 for defending the Income Tax claim/demand, (defined as income tax claim/demand for the purposes of the Share Purchase Agreement and the Escrow Agreement) as finally adjudicated was less than the amount available with the respondent no. 2 bank, an amount equal to the income-tax liability would be paid to the purchaser and the balance would be released to the petitioners. In the event the income-tax claim/demand as finally adjudicated was greater than the amount available in escrow with the respondent no. 2 bank, the entire amount would be paid to the purchaser. The Share Purchase Agreement further recorded that in addition, petitioner no. 3 would pay 1/3rd of the deficient amount to the purchaser. It is clear from the language of the Share Purchase Agreement that under no circumstances would the money held in escrow be released either to the assessee company or to the Income-tax Department. This clearly indicates that no amount was held by respondent no. 2 on account of the assessee company.

27. There is also no reason why either the purchaser of shares of a company or the selling shareholders have any occasion to pay any part of the consideration for sale and purchase of shares of a company to the company. A company is an independent entity completely distinct from its shareholders. A transaction relating to sale and purchase of shares is a transaction inter-se the selling shareholders and purchasers and a company cannot stake claim to any part of the consideration as shares of a company are not the assets of the company but those

of its shareholders. The assessee company is neither a party to the Share Purchase Agreement or the Escrow Agreement nor can claim any sum from the parties to the Escrow Agreement. No money is due to the assessee company by respondent no.2 or is held by or may subsequently be held by Respondent no. 2 on account of the assessee company. The conclusion of the Assessing Officer that the amount of money kept with respondent no. 2 in escrow is available to the assessee for meeting its income-tax demand is thus erroneous.

28. For the reasons as stated above, we set aside the decision of Assessing Officer dated 01.02.2013 and the notice dated 04.02.2013. Consequently, the respondent no. 1 is directed to forthwith refund the amount recovered from respondent no.2 bank pursuant to the notice dated 04.02.2013.

29. Parties are left to bear their own costs.

VIBHU BAKHRU, J

BADAR DURREZ AHMED, ACJ

JULY 24, 2013
MK/rk