

Commissioner of Income Tax v. G. Narshimhan (Died) by Heirs

Civil Appeal No. 6799 of 1983

[1998] Supp. 3 SCR 532 | 1998-12-14

Whether previously assessed deemed dividends reduce accumulated profits, and whether cash and property distributed on reduction of share capital can produce capital gains after separating the dividend component.

2(22)(d) | 2(22)(e) | 2(47) | 45(1) | 194 | 256(1)

Two-judge bench | Sujata V. Manohar, J. | A.P. Misra, J.

Assessment years: 1963-64

Mixed answers; capital gain was not quantified

Previously assessed deemed dividends of Rs 64,517 reduced accumulated profits. Capital reduction nevertheless involved extinguishment of rights: separate the dividend component before computing any gain on the residue. The Tribunal still had to value the property and determine gain, if any. Retain the source-cover spelling Narshimhan and do not adopt the headnote's Companies Act year. Comprehensive later treatment and current statutory mapping remain unverified.

01 FACTS OF THE CASE

The assessee held 70 shares of Rs 1,000 each in Kasthuri Estates (Pvt.) Ltd., Madras. A court-approved reduction, effective 26 May 1962, reduced the face value to Rs 210 and produced a proportionate distribution of money and company properties. The dispute concerned AY 1963-64. The Tribunal held that no capital gains arose because there was no transfer; two questions reached the High Court under section 256(1) (physical pages 3–4/SCR 534–535).

Separately, the company had previously advanced Rs 48,250, Rs 14,667, Rs 1,400 and Rs 200 to four shareholders. These amounts, totaling Rs 64,517, had been assessed as deemed dividends. The first question concerned their deduction from accumulated profits; the second concerned the reduction-related receipt and extinguishment of share rights (physical pages 4–6/SCR 535–537).

Source: See the proposition-specific paragraph and PDF-page references below.

02 DISCUSSION BY THE HON'BLE COURT

On the first question, the Court read sections 2(22)(e) and 194 with the Companies Act restriction on the source of dividends. Once the advances were treated as deemed dividends to the extent of accumulated profits, the fiction required treating that amount as paid out of those profits. Rs 64,517 therefore reduced the company's accumulated profits; the first answer was affirmative and for the assessee (physical pages 5–6/SCR 536–537).

On the second question, Kartikeya Sarabhai supported a transfer through proportionate extinguishment of share rights despite the continued shareholding. But section 2(22)(d) first required separation of the distribution attributable to accumulated profits, whether capitalised or not, as dividend income. Only the residue was a capital receipt; capital gain could arise only after deducting the cost attributable to the extinguished interest. The Court invoked Urmila Ramesh to distinguish distributable accumulated profits from return of capital (physical pages 7–8/SCR 538–539).

The Court did not value the property or quantify a gain. Those matters were outside the referred questions and had not been addressed after the Tribunal's no-transfer conclusion. The Tribunal was to value what the assessee received and determine whether any capital gain arose (physical pages 8–9/SCR 539–540).

Source: See the proposition-specific paragraph and PDF-page references below.

03 JUDICIAL DECISION

Question 1 was answered in the affirmative for the assessee. Question 2 was answered in the negative for Revenue, with property valuation and capital-gain determination left to the Tribunal when the matter returned. The appeal was disposed of accordingly; the reporter records it as partly allowed. No quantified gain, valuation, costs direction or subsequent Tribunal result is supplied (physical pages 6 and 8–9).

Source: See the proposition-specific paragraph and PDF-page references below.

04 OUTCOME / IN WHOSE FAVOUR

In whose favour: Mixed: assessee on accumulated-profit adjustment; Revenue on rejection of the no-transfer answer

Appeal partly allowed; question 1 for assessee, question 2 for Revenue; valuation and capital gains, if any, to be determined by Tribunal

Legal characterisation decided; factual valuation and quantification remained open

No ruling that the full distribution is capital gain, or that gain necessarily equals the reduction in nominal share value.

Source: See the proposition-specific paragraph and PDF-page references below.

05 AKHB REVIEW POINT

Use a sequenced computation: first establish accumulated profits after the earlier deemed-dividend adjustment; then identify the distribution attributable to those profits; only thereafter examine the remaining receipt against the acquisition cost of the extinguished rights. Cash, property valuation and nominal share-value reduction are different inputs.

This historical reference decision does not supply the missing valuation or a final tax bill. The phrases treating deemed dividends as dividends for all purposes belong to the accumulated-profits issue actually decided; they should not be detached into a claim resolving every company-law, repayment or later statutory question. The applicable statutory version and comprehensive later treatment remain unverified.

Source: See the proposition-specific paragraph and PDF-page references below.

PROPOSITION-SPECIFIC SOURCE PARAGRAPHS AND PDF PAGES

1.

Topic: Cover spelling, bench, date, appeal identity and share facts

Source url: [Open cited source](#)

Pdf pages: 1; 3; 4

Paragraphs: Unnumbered judicial text

Source role: reported metadata and judicial text

2.

Topic: Prior deemed dividends and question 1 answer

Source url: [Open cited source](#)

Pdf pages: 4; 5; 6

Paragraphs: Unnumbered judicial text

Source role: judicial text

3.

Topic: Extinguishment, dividend-first allocation and attributable acquisition cost

Source url: [Open cited source](#)

Pdf pages: 7; 8

Paragraphs: Unnumbered judicial text

Source role: judicial text

4.

Topic: Property valuation left open and mixed disposition

Source url: [Open cited source](#)

Pdf pages: 8; 9

Paragraphs: Unnumbered judicial text

Source role: judicial text

5.

Topic: Editorial Companies Act year discrepancy

Source url: [Open cited source](#)

Pdf pages: 1; 5; 6

Paragraphs: Unnumbered judicial text

Source role: reported editorial and judicial comparison

JUDICIAL AUTHORSHIP AND SEPARATE OPINIONS

Sujata V. Manohar, J.

ACT IDENTIFIED IN THE REVIEWED SOURCE

Income-tax Act, 1961

SOURCE & VERIFICATION

[Hon'ble Supreme Court source PDF \(reported judgment\)](#)

Identified source rendition: 9 PDF pages; SHA-256

46b817f0b8810e2bad5b9705b1b8d0c868762ccc72e44e12b3c922d757131a2f. Original bytes preserved.

Complete unnumbered judicial text from physical page 3/SCR 534, paragraph beginning At all material times, through physical page 9/SCR 540, disposal of question 2 and the appeal. Preceding editorial headnote and the reporter disposition line are distinguished.

[Open cited source rendition](#)

The cover and running title spell the name G. NARSHIMHAN. The note retains Narshimhan rather than silently substituting the alternative spelling Narasimhan.; The cover headnote labels the Companies Act as 1961. The judicial discussion refers to section 205 of the Companies Act without supplying that year; the editorial year is not adopted as statutory authority.; The judicial ending answers the two questions separately and leaves valuation and gain computation to the Tribunal. The reporter's Appeal partly allowed line is not a quantified capital-gain award.; No property valuation, attributable acquisition cost, final capital-gain amount, or subsequent Tribunal determination appears in the source.

STATUTORY SCOPE

No automatic mapping to the Income-tax Act, 2025 or present-law certification. Apply the statutory text for the relevant year.

LATER TREATMENT

Source checked 2026-10-04. Comprehensive subsequent judicial and statutory treatment has not been verified. Only the expressly identified bounded comparisons have been checked. No current-law or Income-tax Act, 2025 mapping is certified.

IDENTIFIED SOURCE LINKS

[reported judgment - PDF pages: 9](#)

SHA-256: 46b817f0b8810e2bad5b9705b1b8d0c868762ccc72e44e12b3c922d757131a2f

AI DISCLOSURE

AI-assisted research checked against the identified source. Extraction, interpretation or omission errors remain possible. Source review does not mean independent approval by a practising professional. Verify every material statement against the complete original judgment.

PROFESSIONAL DISCLAIMER

General research information only; not legal or tax advice, a certified judgment or a substitute for the full order. Applicability depends on facts, assessment year, statutory version and jurisdiction. Subsequent treatment is unverified unless identified sources are expressly stated. Downloading does not create a professional engagement. Obtain case-specific advice before reliance.