
(1982) 01 MP CK 0001

In the Madhya Pradesh High Court

Case No : Miscellaneous Civil Case No. 82 of 1979

Additional Commissioner of Income Tax

APPELLANT

Vs

Ramchand Daryanomal

RESPONDENT

Date of Decision : 05-01-1982

Acts Referred:

Income Tax Act, 1961 — Section 41(2)

Citation : (1982) ILR (MP) 831 : (1982) 138 ITR 666 : (1982) JLJ 760 : (1983) 28 MPLJ 300

Hon'ble Judges : G.P. Singh, C.J.; Faizanuddin, J

Bench : Division Bench

Advocate : B.K. Rawat, for the Appellant; B.L. Nema, for the Respondent

Judgement

G.P. Singh, C.J.

This is a reference made by the Income Tax Appellate Tribunal on a direction by the High Court u/s 256(2) of the I.T. Act, 1961. The questions of law referred are as follows :

" (1) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that the new firm had not come into existence with effect from April 27, 1966 ?

(2) Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was justified in holding that the transaction between the old firm and the new firm involving the assets of the old firm does not carry the normal elements of sale in terras of the definition of "sale" under the Sale of Goods Act ? "

The reference relates to the assessment year 1966-67 of a registered firm, M/s. Ramchand Daryanomal, which was constituted on 8th May, 1954. The firm consisted of seven partners. Two partners, namely, Daryanomal and Ammalmal, retired on 27th April, 1966, and a deed of dissolution was executed on the same date. The remaining five partners took a new partner, Thakurdas, and constituted a new firm styled as Ramchand Daryanomal by a deed of partnership which was

also executed on 27th April, 1966. In accordance with Clause (5) of the deed of dissolution of the assessee-firm the new firm took over all the assets and liabilities of the assessee-firm. The assessee-firm owned truck MPA 1101. The written down value of this truck was Rs. 4,747. The transfer value of the truck was shown as Rs. 15,000. The assessee-firm also owned a factory the written down value of which was Rs. 4,635. The transfer value of the factory was shown as Rs. 25,000. The ITO held that the assessee-firm made profits of Rs. 10,253 and Rs. 20,365 on sales of the truck and factory, respectively, to the new firm. He, therefore, added these items as income of the assessee u/s 41(2) of the Act. In the appeal by the assessee to the AAC, this addition was deleted as in his opinion there was no sale within the meaning of Section 41(2). The same view was taken by the Appellate Tribunal.

As regards the first question, there can be no doubt that when the assessee-firm was dissolved on the retirement of two partners by executing a deed of dissolution and a new firm was constituted by the remaining partners by taking a new person as partner, under the general law of partnership the firm so constituted on 27th April, 1966, was a new firm. We are not here concerned with Section 187 of the I.T. Act where, in these circumstances, it would be said that there is merely a change in the constitution of the firm because of the specific provision contained in Sub-section (2)(a) of that Section (see *Vimal and Amar Talkies Vs. Commissioner of Income Tax*,).

Coming to the main question whether the transfer of assets and liabilities of the assessee-firm to the new firm constituted sale within the meaning of Section 41(2), it has to be kept in mind that a firm is not a legal entity, under the law, different from its partners and what is called the property of the firm is the property belonging to the partners collectively and what are called the debts and liabilities of the firm are their debts and liabilities : (see *Lindley on Partnership*, 12th Edn., p. 28, quoted with approval in *Commissioner of Income Tax, Madras Vs. R.M. Chidambaram Pillai and Others*, . During the subsistence of the partnership, however, no partner can deal with any portion of the property as his own nor can he assign his interest in a specific item of the partnership property to any one. His right is to obtain such profits, if any, as part of his share from time to time and upon the dissolution of the firm to share in the assets of the firm which remain after satisfying the liabilities: (*Addanki Narayanappa and Another Vs. Bhaskara Krishtappa and Others*, . In view of these legal principles, it is difficult to hold that there was a sale when the assessee-firm was dissolved on the retirement of two partners and a new firm was constituted by the remaining five partners who took another person as partner. Five partners in both the firms were common. When two partners retired from the assessee-firm their interest in the properties of the assessee-firm ceased in consideration of what they received on settling the accounts at the time of dissolution. The five remaining partners who also became partners of the new firm could not in law sell any property to themselves and, therefore, the taking over of the assets and liabilities of the assessee-firm by the new firm did not amount to sale in the eye

of law. The truck and the factory, after the retirement of the two partners of the assessee-firm, vested in the five remaining partners who were also the partners of the new firm with one outsider. The properties of the new firm thus vested essentially in the five partners who were also partners of the assessee-firm. As sale postulates a transfer of property from one person to another, there was no sale of the truck and the factory in these circumstances. The view taken by us is supported by a decision of the Madras High Court in COMMISSIONER OF Income Tax, MADRAS-I Vs. ABDUL KHADER MOTOR AND LORRY SERVICE., . In that case the firm consisted of two persons. Thereafter, it was reconstituted by taking two more persons as partners. The buses belonging to the old firm were transferred to the new firm and the question was whether there was any sale within the meaning of Section 41(2) of the Act. The Madras High Court answered this question in the negative. The learned standing counsel relied upon Chittoor Transport Co. (Pr.) Ltd. Vs. Income Tax Officer, Chittoor, , Chittoor Motor Transport Co. (P.) Ltd. Vs. Income Tax Officer, Chittoor, and Commissioner of Income Tax, Gujarat Vs. B.M. Kharwar, , in support of his argument that we must hold that there was a sale as held by the ITO. In all the cases relied upon by the learned standing counsel, the property was transferred by a firm to a company or by a company to a firm. A company being a legal entity distinct from its shareholders, it was held in these cases that the transfers amounted to sales. These cases are clearly distinguishable and have no application to the facts of the instant case.

For the reasons given above, we answer the questions as follows :

- (1) A new firm came into existence from 27th April, 1966.
- (2) There was no sale of the truck and the factory within the meaning of Section 41(2) by the assessee-firm in favour of the new firm.

There will be no order as to costs of this reference.