
(1975) 01 MAD CK 0047

In the Madras High Court

Case No : Tax Case No. 104 of 1969 (Reference No. 20 of 1969)

A.L.A. Firm

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 10-01-1975

Acts Referred:

Income Tax Act, 1961 — Section 119, 139(2), 147, 169

Citation : (1976) 102 ITR 622

Hon'ble Judges : V. Sethuraman, J; V. Ramaswami, J

Bench : Division Bench

Advocate : K. Srinivasan and K.C. Rajappa, for the Appellant; V. Balasubrahmanyam and J. Jayaraman, for the Respondent

Judgement

Sethuraman, J.—The assessee was a partnership firm consisting of four partners. The firm constituted under a deed of March 26, 1960, was carrying on money-lending business in Malaya and in the course of such business acquired house properties, estates and gardens there. It was also dealing in properties by way of purchase and sale. The profit and loss of these transactions of purchase and sale of estates was being reflected in the Income Tax assessment.

2. The firm maintained its accounts for the Tamil year. We are now concerned with the year that commenced on 13th April, 1960. The firm closed its accounts on 13th March, 1961, as it was claimed that it was dissolved on that date. Along with the return, a profit and loss account, balance-sheet and profit and loss adjustment account were filed. In the profit and loss account the net profit transferred to the partner's accounts was shown at \$72,196"47. This sum was arrived at by crediting, to the profit and loss account, the difference on revaluation of estates and gardens and house properties on dissolution of the firm on 13th March, 1961. The difference on revaluation of estates and gardens and house properties on dissolution of the firm was written back with the result that the adjusted profit for purposes of Income Tax was shown as \$4,604"88. It was also stated before the Income Tax Officer that out of the four partners,

Ramana-than Chettiar formed one group, and the other partners, another group, and that the two groups were carrying on business separately with the assets and liabilities that fell to their shares on the dissolution of the firm. These statements were furnished along with the return on 10th April, 1962. On the same day the Income Tax Officer issued a notice u/s 23(2), Indian Income Tax Act, 1922, posting the hearing for the same day. He completed the assessment on the same day by adding back a sum of Rs. 2,083 representing municipal tax paid in respect of the properties in Malaya. According to the Income Tax Officer, this amount was not admissible as a deduction in arriving at the proper income. He did not issue any assessment order as such, but made a note in the order sheet as under:

"Audit assessment--Lakshmanan appears. Return filed--I.T. 86 acknowledged in list of books--Scrutinised--Order dictated ".

3. In the course of the assessment for 1962-63, for which a notice u/s 139(2) was issued, the assessee filed a nil return with a letter stating that the firm was dissolved on March 13, 1961, and that the firm was not in existence for the relevant year. The Income Tax Officer found that the statement of the assessee was correct, that the profit as per the accounts for the year ended March 13, 1961, was \$ 72,196.47 adjusted in the accounts of the respective partners and that a sum of \$ 101,248.25 being the difference on revaluation of house and gardens on dissolution of the firm had been written back in the statement for the year ended on March 13, 1961. He took the view that the difference on revaluation of assets on the dissolution of the firm, viz., \$ 101,248.25 had escaped assessment in the assessment year 1961-62. He, therefore, took proceedings u/s 147(b) of the Income Tax Act, 1961. Before starting the proceedings he wrote a letter on September 3, 1963, to the assessee referring to the sum of \$ 101,248 being the difference in revaluation of the estates, etc., and to the decision in G. R. Ramachari and Co. Vs. Commissioner of Income Tax, Madras, . He required the auditor to furnish the basis for the valuation and also file his objections, if any, to the amount being taken for assessment.

4. The auditor in his reply stated that the case referred to by the Income Tax Officer had no application and that no loss or profit on a revaluation of assets could be assessed. He referred in this connection to a circular of the Board of Revenue dated June 21, 1956. It was submitted that, under the terms of the circular, surplus was only assessable to capital gains and that there was no capital gains to be assessed as the price prevailing on January 1, 1954, was the same as at the time of the dissolution.

5. It is after this correspondence that the Income Tax Officer took proceedings u/s 148 read with Section 147(b) of the Act on 24th May, 1965. The assessee filed a return in response to this notice, but claimed that the excess by revaluation of assets on dissolution on March 13, 1961, was not assessable to Income Tax either as revenue profits or capital gains, as they had been distributed in specie on dissolution of the partnership. It was also submitted that the reassessment

proceedings were only due to change of opinion and that no reassessment could be done for giving effect to a change of opinion. The Income Tax Officer rejected these submissions and brought to tax the aforesaid sum of \$ 101,248 along with the other amounts which were already assessed under the original assessment.

6. The assessee contested the reassessment before the Appellate Assistant Commissioner without success. Thereafter, the assessee appealed to the Appellate Tribunal. Several contentions were taken before it. The Tribunal held that the proceedings u/s 147(b) had been validly taken and that the surplus of \$101,248 was rightly brought to tax.

7. At the instance of the assessee, the following three questions have been referred for the opinion of this court:

"(1) Whether, on the facts and circumstances of the case, the reassessment made on the assessee-firm for the assessment year 1961-62 u/s 147 of the Income Tax Act is valid in law ?

(2) Whether, on the facts and circumstances of the case, the assessment of the sum of \$ 301,248 as revenue profit of the assessee-firm chargeable to tax for the assessment year 1961-62 is justified in law ?

(3) Whether, on the facts and circumstances of the case, the Appellate Tribunal is right in law in sustaining the assessment of the sum \$ 101,248 after having found that the departmental officers are bound by the circular of the Central Board of Revenue ?"

8. On the first question, the submission on behalf of the assessee was that it is now well-settled that the Income Tax Officer cannot take valid reassessment proceedings on a mere change of opinion and that in the present case all the materials had already been placed before the Income Tax Officer and had been scrutinised by him. If after scrutiny the Income Tax Officer did not think it proper to tax the sum \$ 101,248 it was submitted that there was no power to reopen the assessment merely because the earlier conclusion was considered to be erroneous.

9. For the Commissioner of Income Tax, the learned counsel submitted that this was a case in which the Income Tax Officer had not at all adverted to the statements regarding the sum of \$ 101,248 and that he had applied his mind only to the rest of the income that was shown in the return. The adjustments made to the returned income were only with reference to those items which had been shown in the return. It was pointed out that when such a large sum was involved, it would be too much to expect the Income Tax Officer to have completely kept silent over the said amount without any discussion.

10. The original statement as filed before the Income Tax Officer on 10th April, 1962, was placed before us by the counsel for the Commissioner. The profit and loss adjustment account for the purpose of Income Tax contains the following narration :

"Difference on revaluation of houses and gardens on dissolution of firm written back (not assessable either as revenue or capital gains on the basis of value as on 1-1-54)-- \$ 101,248.25."

11. The words given above in brackets are found to be overtyped. The suggestion during the arguments was that one cannot be sure as to whether the words within the brackets were actually in the statements as filed before the Income Tax Officer so as to draw his attention to the assessability or otherwise of this amount. For our present purpose, we do not think it necessary to go into this aspect. We would proceed on the basis that the statement with the overtyping was there before the Income Tax Officer at the time when he made the original assessment. Even on that footing the point that arises is whether the reassessment proceedings are valid. It is now well-settled that the Income Tax Officer cannot take up the proceedings for reassessment of an income merely because there was a change of opinion. The decision of the Supreme Court in Commissioner of Income Tax, West Bengal II Vs. Dinesh Chandra H. Shah and Others,) is clear on this point. In that case the assessee, who was assessed at Calcutta, had disclosed in his return his share income from a firm in Madras. In completing the assessment the Income Tax Officer failed to include the assessee's share from the Madras firm. His successor took action u/s 34(1)(b) of the Indian Income Tax Act, 1922, to include the said share of profits. In the appeal against the reassessment, the Income Tax Officer sought to justify the reopening of the assessment merely on the ground of change of opinion. The Supreme Court held that the power to reassess was not available in the said circumstances. At page 371 it was observed as follows:

"In our judgment it is wholly unnecessary to go into the question whether an inadvertent omission can justify the reopening of the assessment on its subsequent discovery by the Income Tax Officer."

12. But the point here is whether there was any opinion formed in the original assessment, which was sought to be changed so as to reassess the same income. This point may be considered in the light of two decisions of this court. The first is Salem Provident Fund Society Ltd. Vs. Commissioner of Income Tax, Madras, . In that case the Income Tax Officer, instead of deducting a certain amount from the deficiency as shown in the actuarial valuation of the provident fund society, added a sum of Rs. 77,165. The result was that, instead of bringing to tax a sum of Rs. 13,686, he arrived at a deficiency of Rs. 1,68,016 for the assessment year 1947-48. There was a similar mistake for the assessment year 1948-49. Subsequently, after these mistakes were discovered, the Income Tax Officer took up proceedings u/s 34(1 Kb) of the Indian Income Tax Act of 1922. The contention urged on behalf of the assessee was that all these statements on the basis of which the reassessment proceedings were taken, were already on record and that in such a case there was no " information " which would justify the reassessment. The following passage at pages 564 and 565 brings out the ratio of this decision :

"We are unable to accept the extreme proposition, that nothing that can be found in the record of the assessment, which itself would show escape of assessment or under assessment, can be viewed as information which led to the belief that there has been escape from assessment or under-assessment. Suppose a mistake in the original order of assessment is not discovered by the Income Tax Officer himself on further scrutiny but it is brought to his notice by another assessee or even by a subordinate or a superior officer, that would appear to be information disclosed to the Income Tax Officer, If the mistake itself is not extraneous to the record and the informant gathered the information from the record, the immediate source of information to the Income Tax Officer in such circumstances is in one sense extraneous to the record. It is difficult to accept the position that while what is seen by another in the record is "information" what is seen by the Income Tax Officer himself is not information to him. In the latter case he just informs himself. It will be information in his possession within the meaning of Section 34. In such cases of obvious mistakes apparent on the face of the record of assessment that record itself can be a source of information, if that information leads to a discovery or belief that there has been an escape of assessment or under-assessment."

13. The High Court upheld the reassessment.

14. A similar problem arose in Commissioner of Income Tax, Madras Vs. Rathinasabapathy Mudaliar (Deceased), . In that case there was a partition between a Hindu father and his sons, one of whom was a minor. The business was carried on by a partnership after the partition and the minor had been admitted to the benefits of the partnership. The father also was a partner. The Income Tax Officer registered the firm. The father had not included in his return the income of the minor son from the firm as required by Section 16(3) of the Act of 1922. The minor son submitted a separate return and was assessed on this income. Subsequently, the Income Tax Officer discovered his error in not assessing the father thereon and started reassessment proceedings. The question before this court was whether there was "information" within the meaning of Section 34(1)(b) of the Indian Income Tax Act of 1922. At page 211 the learned judges observed as follows:

" Whether the information was received from an extraneous source or the Income Tax Officer informed himself was immaterial for the purpose of Section 34(1)(b).....the information relevant to Section 34(1)(b) may be derived from the record of the assessment itself....."

15. At page 212, it was again observed as follows:

"Even assuming that there was no omission or failure on the part of the assessee, the information that any part of the income had escaped assessment was clearly received subsequent to the assessment. That that information was gathered from the records of the original assessment itself does not make it any the less the information which led the Income Tax Officer to believe that the

income had escaped assessment."

16. The Supreme Court has considered this problem in a sales tax case in *Anandji Haridas and Co. (P.) Ltd. Vs. S.P. Kushare, S.T.O. Nagpur and Others*, . The provision under consideration of the Supreme Court was in pari materiel. At page 336 the passage that we have already extracted from the decision of this court in *Salem Provident Fund Society Ltd. v. Commissioner of Income Tax* was reproduced with approval.

17. The result of these decisions is that the statute does not require that the information must be extraneous to the record. It is enough if the material, on the basis of which the reassessment proceedings are sought to be initiated, came to the notice of the Income Tax Officer subsequent to the original assessment. If the Income Tax Officer had considered and formed an opinion on the said material in the original assessment itself, then he would be powerless to start the proceedings for the reassessment. Where, however, the Income Tax Officer had not considered the material and subsequently come by the material from the record itself, then such a case would fall within the scope of Section 147(b) of the Act. The same view has also been taken in the judgment dated 1st October, 1974, in T.C. No. 84 of 1969 (*S. Srinivasan (Deceased) (by legal representatives) Vs. Commissioner of Income Tax*,), to which one of us was a party. We are satisfied, after considering the materials on record and the relevant decisions that the Tribunal came to the correct conclusion, when it said in paragraph 23 of its order that the Income Tax Officer had acted mechanically in accepting the return without bringing his mind to play upon the entry in the statement with reference to the distribution of the assets. There is no evidence of any enquiry having been made with reference to this aspect. The amount involved is sufficiently large, so that if the Income Tax Officer was aware of the existence of this entry, he would have discussed it. At that stage the Income Tax Officer does not also appear to have been aware of the decision of this court in *G. R. Ramachari & Co. v. Commissioner of Income Tax* to which we shall refer presently. Thus, taking into account all these factors, we are satisfied that there was information which came to the notice of the Income Tax Officer subsequent to the original assessment. In the course of the reassessment proceedings, the Income Tax Officer had called for the particulars of the valuation of the estate, etc. The absence of any such query at the original stage would clearly go to show that the Income Tax Officer had not at all applied his mind to this aspect. The reassessment proceedings are validly taken.

18. This takes us to the second question. The problem that has to be considered here is whether \$ 101,248 is assessable at all. We have already pointed out that this sum represents the difference on revaluation of houses and gardens on dissolution of the firm on March 13, 1961. There was some controversy before us raised by the counsel for the Commissioner as to whether the dissolution of the firm took place on March 13, 1961, or only on April 1, 1961. This controversy was not raised before the Tribunal nor at any earlier stage. The case has so far

proceeded on the basis that the dissolution took place on March 13, 1961. We would, therefore, proceed on the same footing. This is not the stage at which any dispute about the facts can be raised.

19. The problem that arises is as to how the stock-in-trade of a firm, which is dissolved, is to be valued at the time of the termination of the firm's business. The learned counsel for the assessee submitted that when the firm is dissolved, whatever assets are possessed by the firm are impressed with the character of the properties of the firm and had shed their character as stock-in-trade. In other words, the submission was that as soon as the dissolution was agreed upon, there was a transformation of the entire properties of the firm into capital assets so that even the stock-in-trade would partake of the character of the capital assets. From this proposition, it was sought to be contended that any distribution of the properties at the time of the dissolution of the firm, may be on the basis of some valuation, did not give rise to any assessable income. For the Commissioner of Income Tax the submission was that the stage of dissolution commenced only after the stage of the termination of the business of the firm and that at the stage of termination of the business of the firm, the profits of the firm had to be ascertained and brought to tax. It was contended that in the case of stock-in-trade the clear pronouncement of the court was that it had to be valued at the market rates at the time of the dissolution. We now consider this aspect.

20. In *N. Muhammad Ussain Sahib and Another Vs. S.N. Abdul Gaffoor Sahib and Others*, the question as to how the stock-in-trade had to be valued arose in a civil litigation between the parties in a suit for dissolution of partnership and for taking of accounts. The problem was whether the book value of assets alone should be taken for assessing profit and loss of the partnership or whether the market value of the assets should be considered in arriving at the profits. In that case the distinction between the stock-in-trade and other assets was not the subject of consideration. At page 82 the distinction between the object of the annual settlement of accounts and the settlement of accounts at a time when a partner retired was pointed out. As regards the annual settlement of accounts, it was observed as follows:

"The object of the annual settlement is only for the definite purpose of assessing the profits at the end of the year and so long as the partnership is continued, it does not make any difference to the partners even if notional value is taken as the value of the assets. The asset at that book value continues to belong to the firm and whatever fluctuations there may be in the value of that asset, the benefit or the loss of it would accrue to the firm. "

21. As regards the dissolution, it was pointed out:

" But the situation is totally different when the firm is dissolved or when a partner retires. The settlement of his account must be not on a notional basis but on a real basis, that is, every asset of the partnership should be converted into

money and the account of each partner settled on that basis.....The assets have to be valued, of course, on the basis of the market value on the date of the dissolution..... "

22. The Supreme Court also in a civil case in *Addanki Narayanappa and Another Vs. Bhaskara Krishtappa and Others*, considered the question as to whether registration of the deed allotting immovable properties on dissolution of the firm was necessary. In the course of the said decision, the rights of a partner during the subsistence of the partnership and after dissolution have been considered at page 64 as follows :

"his right during the subsistence of the partnership is to get his share of profits from time to time as may be agreed upon among the partners and after the dissolution of the partnership or with his retirement from partnership of the value of his share in the net partnership assets as on the date of dissolution or retirement after deduction of liabilities and prior charges."

23. We are in the present case concerned with the rights of a partner during the subsistence of the partnership, that is, on March 13, 1971. On that date the profits of the firm have to be ascertained by valuing the stock-in-trade properly. The dissolution will follow thereafter.

24. The question as to how the stock has to be valued arose for consideration of this court in *G.R. Ramachari & Co. v. Commissioner of Income Tax*. In that case there were two partners by name Ramachari and Anantharam. Ramachari filed a suit for taking of accounts of the business which had its office at Madurai and branches in Bombay and Nagpur. The firm was declared to be dissolved. According to the decree, the valuation of the closing stock had to be at the market rates. The firm in its return admitted an income on the basis of the stocks being valued at book figures. The Income Tax Officer added in the assessment of the firm the amount representing the difference between the book figures and the market value of the stock-in-trade at the time of the dissolution. The question as to whether this addition was proper and valid came before this court. After considering the decisions cited, it was observed that there was no authority directly in point dealing with the question of the value of the stock-in-trade at the time of the dissolution of the firm. At page 146 the contention of the assessee that in the event of dissolution what remained on hand as stock-in-trade lost its character and became capital assets was rejected. The relevant passage runs as follows :

" It is obvious that when a business ceases, all its stock-in-trade has to be disposed of and brought into account in order to balance the books. The goods on hand do not lose the character of stock-in-trade, and this proposition put forward by the assessee has no authority to sustain it."

25. This point as to whether the entire assets are metamorphosed into capital on the dissolution of a firm is concluded by an earlier decision of the Privy Council in *Commissioner of Income Tax v. Muthukaruppan Chettiar*, [1935] 3 ITR 208 . In

that case, the question was whether the interest received by a partner on the dissolution of the firm was a capital receipt. The Privy Council held that what the partner received was income and not capital. The analogy of the distribution of assets on liquidation of a company being applicable to the distribution of the profits on dissolution of a firm was rejected. Thus, the contention that the stock-in-trade got transformed into capital assets is not tenable.

26. The Supreme Court's decision in *Commissioner of Income Tax v. Madurai Mills Co. Ltd.* [1973] 89 ITR 43 does not in any way run counter to the above view of the Privy Council. The Supreme Court held that there was no sale when a company in liquidation distributed its assets. The reference to the cases where the firm on dissolution distributed its assets in this connection does not mean that the analogy of a dissolved firm and distribution of assets has to be applied to other spheres involving the consequences that whatever was possessed by the firm at the time of the dissolution became capital assets. We hold that the stock-in-trade does not cease to be stock-in-trade on the dissolution of a firm.

27. On the point of valuation of stock-in-trade at the time of dissolution of a firm, the following passage occurs at page 149 in *Ramachari's* case :

".....in order to arrive at the correct picture of the trading results of the partnership on the date when it ceases to function, the valuation of the stock-on-hand should be made on the basis of the prevailing market price."

28. The result of this decision is that in the present case the stock-in-trade, viz., the estates, gardens and houses in Malaya, had to be valued at their market value.

29. The learned counsel for the assessee submitted that this decision is erroneous. His first point was that the assessee had a right to value the stock at cost or market value whichever was lower and that this right could not be taken away merely because the parties decided to discontinue the business or dissolve the firm. As pointed out by the counsel for the Commissioner, the option to value the stock at cost or market value, whichever was lower, is available to the assessee during the subsistence of the business. But we are concerned with the point of time at which the business is sought to be discontinued. At the point of termination of the business, the point is whether the assessee has still the option of valuing the stock at cost or market rate, whichever was lower. No doubt, in a case where the stock values had fallen down, the assessee would adopt the market value so that there is no likelihood of objection on the part of the assessee to the market value being adopted in such a case. With reference to the stock-in-trade at the time of the termination of the business, the problem is thus likely to arise only in cases where the market value of the stock-in-trade is higher than the cost. There is no authority to support the proposition of the assessee that the option to value the stock-in-trade at the cost or the market value, whichever is lower, is available to it even at the point of termination of the business. The decision of the Bench of this court is against this contention and

we do not think that there is any merit in the submission to the contrary.

30. The learned counsel for the assessee next submitted that this decision is inconsistent with the later decisions of the Supreme Court, so that it cannot be treated as good law at present. The counsel drew our attention to two decisions of the Supreme Court as supporting him. The first case is Commissioner of Income Tax, Madhya Pradesh Vs. Dewas Cine Corporation, . There the partnership consisted of two persons each of whom brought a cinema theatre into the firm at the time of its formation. This firm was dissolved and it was agreed between the partners that the theatres should be returned to the original owners. In the books of account maintained by the partnership, the theatres were shown to have been returned to the partners at the original price at which they were brought into the firm. The Income Tax Officer applied the proviso to Section 10(2)(vii) of the Act of 1922, under which where the amount for which any building, plant or machinery is sold exceeds the written down value, so much of the excess as does not exceed the difference between the original cost and the written down value is to be deemed to be profits of the previous year in which the sale took place. The Income Tax Officer proceeded on the footing that there was a sale at the time when the firm was dissolved and the theatres were returned to the original owner. The Supreme Court negated this view and held that there was no sale on the facts. The distinction between the case before the Supreme Court and that in Ramachari & Co. is obvious. The Supreme Court had no occasion to deal with the problem as to how the stock-in-trade had to be valued at the time of dissolution of the firm. The problem before the Supreme Court was a wholly different one, viz., as to whether there was a sale. We are not now concerned with any such question. The theatres were not stock-in-trade there. The question here arises before or at the time of dissolution and before the Supreme Court it arose after or in consequence of it.

31. The next decision which was cited is Commissioner of Income Tax, U.P. Vs. Sh. Bankey Lal Vaidya (Dead) by Lawyers, . That was also a case where the assets of the firm including goodwill, machinery, furniture, etc., were valued at the time of the dissolution at Rs. 2,50,000 and taken over by one of the two partners. The assessee in that case was paid one-half of the said value. The Income Tax Officer considered that a sum of Rs. 70,000 out of the amount received by the assessee was liable to be taxed as capital gains. The Supreme Court considered the question as to whether on the facts there was a sale of the assets of the partnership to a partner at the time of the dissolution of the firm. It was held that there was no such sale. The liability to capital gains would have arisen only when there was a sale. It was held that there was no sale. Here also the problem before the Supreme Court was a different one and whatever we have said earlier applies here also.

32. The learned counsel for the assessee referred us to a decision in Commissioner of Income Tax Vs. Janab N. Hyath Batcha Sahib, . In that case the assessee, who was individually carrying on business in forest contracts,

converted the business into one of partnership with another. He brought into the firm three lorries at a valuation of Rs. 15,000. The Income Tax Officer sought to tax the difference between the said sum of Rs. 15,000 and the written down value of the lorries as shown in the individual assessment file in the hands of the partner. The attempt to tax the said amount was by application of the proviso to Section 10(2)(vii) of the Indian Income Tax Act, 1922. After considering the cases cited, it was observed at page 532 as follows :

".....when A, as an individual, hands over his property to A and B, constituting a firm of partnership, there is no transfer of property involved. In any event, there is no such transfer of property so as to constitute a sale of goods....."

33. We do not see how this decision has any application to the facts herein. As indicated earlier, we are not concerned with the question whether there was a sale at all. We are concerned with the assessment of the firm up to the point of dissolution and the valuation of the stock-in-trade as on that date. We may in this connection point out that a case similar to the one cited above arose in the Supreme Court in Commissioner of Income Tax, West Bengal Vs. Hind Construction Ltd., . In that case the assessee was interested in a joint venture for purchase and sale of machinery. The unsold machinery remaining after the venture was closed was divided. The assessee received machinery of the value of about Rs. 2,00,000. In the account books the assessee wrote up the value to Rs. 4,00,000. When a partnership was formed, the assessee transferred that machinery at a value exceeding Rs. 6,00,000. The question was whether the assessee was liable to be assessed on the basis of which the machinery was revalued. The Supreme Court held that neither when the assessee wrote up the value of the machinery in its books nor when it handed over its machinery to the partnership was there a sale. It was held that the assessee had not derived any income. As the question of stock valuation at the time of the termination of the business was not in issue in that case, there is no scope for applying the principle laid down therein.

34. The view that: we have taken appears to us to be supported also by a decision of the Gujarat High Court in Commissioner of Income Tax, Gujarat Vs. Keshavlal Chandulal, . In that case there was a firm of 7 partners. The business of the firm was the purchase of open plots of land, construction of buildings thereon and the sale of the buildings. At the time of the dissolution the firm was left with 28 shops. These shops were distributed among the partners in three groups at a total value of Rs. 89,000, resulting in the surplus of Rs. 4,831, which was shown as a profit. The Income Tax Officer, however, sought to revalue the stock-in-trade at a higher figure and bring to tax a larger income than the sum of Rs. 4,831. The question before the Gujarat High Court was whether such an assessment was proper. Ultimately, the court held that the transfer of shops at the figure as agreed to between the parties had to be taken as such, "and that the higher valuation as made by the Income Tax Officer was not proper. In that case one of the contentions was whether there was a commercial transaction at

the time of the distribution of the shops. At page 131, in dealing with these aspects, it was observed as follows :

"There can, therefore, be no doubt that distribution of assets is part of the transaction of dissolution and is a business transaction entered into by the partners who, until then, were jointly carrying on the business. In our view, what applies to dissolution of a partnership must equally apply to a transaction entered into by businessmen when they decide to discontinue the business and make up accounts and distribute its assets and liabilities amongst themselves."

35. We would apply the above passage with reference to stock-in-trade. We are, however, not to be understood as holding that the above passage applied with reference to assets other than the stock-in-trade.

36. It is now well settled by the decision of the Supreme Court in *The Commissioner of Income Tax, Madras Vs. A. Krishnaswami Mudaliar and Others*, that whichever method of book-keeping is adopted in the case of a trading venture for computing the true profits of the year, the stock-in-trade must be taken into account. The learned counsel for the assessee submitted that under the system of accounting adopted by the assessee the valuation of the stock-in-trade was never done. In other words, no trading account is prepared. The result of this method of accounting is that the stock-in-trade is taken at cost both at the commencement and at the end of the relevant year. If there was any sale of the properties, then to that extent either the profit or the loss is accounted for in the profit and loss account. That is how in this particular case, as mentioned earlier, there has been an assessment of the profit and an allowance of the loss in some of the earlier years. Therefore, the fact that the assessee did not prepare a trading account does not mean that the principles of stock valuation did not apply to this case. The stock has to be valued whatever be the method of accounting, and, as observed earlier, at the time of the dissolution of the firm, the stock has to be valued at the market price. It was not stated before us that the sum of \$ 101,248, which was arrived at, represented anything other than the market value of the stock-in-trade. It would follow that it was properly brought to tax.

37. We have now to consider the third question. The assessee relied on a circular dated 21st June, 1956, issued by the Central Board and submitted before the Tribunal that in the case of properties acquired by Indian businessmen in the course of money-lending business prior to 1st September, 1939, the surplus arising from the sale would be in the nature of capital gains. The submission on behalf of the assessee was that the Income Tax Officer ought to have acted in accordance with the terms of this circular. The Tribunal held that the circular was in the form of a letter and that it was not known under what provisions of the Income Tax Act it had been issued. It is not clear whether the actual circular was before it. It was also held that, in any case, if the assessee felt that its case came under the terms of the letter, it had to seek its remedy elsewhere.

38. Before us, the learned counsel for the assessee submitted that the Income Tax Officer ought to have followed the circular and that the Tribunal should have set aside the assessment so as to enable the Income Tax Officer to have applied the circular. For the Commissioner the submission was that the circular had no binding force as far as the appellate Authorities are concerned and that the Tribunal rightly rejected the assessee's plea for application of the circular.

39. The problem of the binding nature of circulars has come up for decision of courts on more than one occasion. In *Navnitlal C. Javeri Vs. K.K. Sen*, Appellate Assistant Commissioner of Income Tax, "D" Range, Bombay, the Supreme Court dealt with the circular issued at the time when Section 2(6A)(e) of the Act of 1922 was enacted in 1955. That provision was enacted so as to bring to tax the loans outstanding against the accounts of shareholders where the company had accumulated profits. In other words, the provision was designed to bring to tax as dividends any amount which had been drawn as a loan by a shareholder and which was outstanding in his account to the extent of the accumulated profits available in the hands of the company. At the time of the introduction of this provision, the Hon'ble Minister gave an assurance that outstanding loans and advances which were otherwise liable to be taxed as dividends in the assessment year 1955-56, would not be subjected to tax if it was shown that they had been genuinely refunded to the respective companies before the 30th June, 1955. To this effect a circular was issued on 10th May, 1955. Before the Supreme Court the question was regarding the validity of the said provisions and not of the circular. In the course of the judgment, reference was made to the circular issued in pursuance of the assurance of the Minister concerned and it was pointed out at page 203 as follows :

"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 u/s 5(8) of the Act of 1922."

40. This decision was applied in *Ellerman Lines Ltd. Vs. Commissioner of Income Tax, West Bengal, Calcutta*,) by the Supreme Court. In that case the question arose out of the assessment of a British shipping company. In the case of the British shipping companies there was a circular of the Central Board dated February 10, 1942, permitting them to elect to be assessed on the basis of the "ratio certificates" granted by the U. K. authorities and enabling them to get investment allowance corresponding to development rebate. This circular was considered by the Supreme Court as laying down the manner of applying Rule 33. But the validity of the circular was not specifically in issue.

41. But this problem as to whether circulars of this kind can bind the judicial discretion of the authorities concerned has been the subject of specific consideration in several other decisions. In *B. Rajagopala Naidu Vs. State Transport Appellate Tribunal and Others*, the matter arose under the Motor Vehicles Act. Section 43-A of the Act conferred power on the Government to issue orders. The validity of the order issued by the Government of Madras on

April 28, 1956, in exercise of the powers u/s 43-A was challenged before the Supreme Court. The Supreme Court held at page 1579 as follows :

"In interpreting Section 43-A, we think it would be legitimate to assume that the legislature intended to respect the basic and elementary postulate of the rule of law, that in exercising their authority and in discharging their quasi-judicial function the Tribunals constituted under the Act must be left absolutely free to deal with the matter according to their best judgment."

42. It was also pointed out that the field covered by Section 43-A was administrative and did not include the area which was the subject-matter of the exercise of quasi-judicial authority by the relevant Tribunals. It was held that the law itself could regulate the exercise of judicial powers. But what the law and the provisions of law might legitimately do could not be permitted to be done by administrative or executive orders.

43. The same question of the force of the circulars of the Central Board arose for consideration under the Wealth-tax Act. The provision under the Wealth-tax Act, viz., Section 13, is identical with Section 119 of the Income Tax Act, 1961. The Supreme Court held in *Sirpur Paper Mills Ltd. Vs. The Commissioner of Wealth Tax, Hyderabad*, that the orders, instructions and directions of the Central Board might control the exercise of the power of the officers of the department in matters administrative but not quasi-judicial and that the section did not imply that the Board might give any directions or instructions to the Wealth-tax Officers or to the Commissioner in the exercise of his quasi-judicial functions. In that case the Commissioner had sought instructions from the Board as to how certain revision application filed before him should be decided. The Supreme Court set aside the orders of the Commissioner on appeal under Article 136 of the Constitution and directed him to hear the revision applications and dispose of them according to law and uninfluenced by any instructions or directions given by the Board. In *J. K. SYNTHETICS LTD. AND OTHERS Vs. CENTRAL BOARD OF DIRECT TAXES AND OTHERS.*, the Supreme Court again considered the question of the applicability of the circular of the Central Board of Direct Taxes in the matter of construction of Section 80J of the Income Tax Act. The Supreme Court held that the Central Board was not competent to give directions regarding the exercise of any judicial power by its subordinate authorities. Thus, the above three cases establish that the judicial power of the Income Tax Officer cannot be controlled by any circular that may be issued. The circulars that are contemplated by Section 119 are only in regard to administrative aspects and cannot extend to the judicial aspects of the administration of the Act. The decisions of the Supreme Court in *Navnit Lal C. Javeri v. K. K. Sen, Appellate Assistant Commissioner of Income Tax and Ellerman Lines Ltd. v. Commissioner of Income Tax* must be considered to be the exceptional ones. In one case there was an instruction in accordance with the assurance given by the Minister concerned to Parliament. In such a case, it is possible to take the view that Parliament would not have passed the relevant statute unless the particular

aspect on which the assurance was given was embodied in the statute itself. In the other case of *Ellerman Lines Ltd. v. Commissioner of Income Tax* the circular was in connection with the assessment of shipping companies under a particular rule. There is nothing inconsistent with the provisions of the Act or the rules or fettering the discretion of the authorities in the circular that was issued. The circular was intended to govern a difficult branch, viz., the assessment of shipping companies. Save in such exceptional cases it would not be proper to countenance the view that the circulars issued by the Central Board will fetter the judicial discretion of the authorities administering the Act. If such contentions were to be accepted, then it would be easy for the administrative authorities to put out of commission the entire hierarchy of tribunals and courts by issuing circulars. This would not have been contemplated by the legislature and that is why the Supreme Court has restricted the applicability of such circulars to administrative matters. We would, therefore, hold that the circular, as such, has no binding force with reference to the assessment now before us. We may make it clear that we do not accept the view of the Tribunal that the departmental officers are bound by such circulars of the Board of Revenue with reference to quasi-judicial matters.

44. In the result, questions Nos. 1 to 3 are answered in the affirmative and in favour of the revenue. The Commissioner will have his costs. Counsel's fee, Rs. 250.