

(1998) 10 MP CK 0029

In the Madhya Pradesh High Court

Case No : Miscellaneous Petition No. 1126 of 1988 13th October, 1998

ANIL KUMAR SATISH KUMAR NAHTA

APPELLANT

Vs

INSPECTING ASSISTANT COMMISSIONER OF INCOME TAX

RESPONDENT

Date of Decision : 13-10-1998

Acts Referred:

Constitution of India, 1950 — Article 226

Income Tax Act, 1961 — Section 143, 147, 148, 187, 188

Citation : (1999) 152 CTR 516

Hon'ble Judges : S.K. Kulshrestha, J

Bench : Division Bench

Judgement

S.K. KULSHRESTHA, J.

This petition challenges the notice Annexure F.2 issued under s. 148 of the IT Act, 1961, and seeks an order that the proceedings under s. 147/148 for the asst. yr. 1981-82 be declared illegal, void and without jurisdiction.

2. The petitioner-firm carries on the business of silver and silver ornaments at Seoni. For the asst. yr. 1981-82, relevant to the accounting year ending on Diwali, 1980, the petitioner filed a return of income of Rs. 54,000 and an assessment was made on a total income of Rs. 55,730 vide order dt. 7th Oct., 1987, in accordance with the provisions of s. 143(3) of the IT Act, 1961 (hereinafter referred to as "the Act").

3. The original petitioner-firm consisted of three partners viz., Santosh Chand, son of Labhchand Nahata, Prakash Chand Nahata, son of Indrachand Nahata and Ajay Kumar, son of Pukhraj Nahata. On 7th Nov., 1980, the last date of the accounting year ending on Diwali, 1980, Santosh Chand retired from the firm and the petitioner firm was continued with the remaining two partners in the subsequent assessment years and was registered as a firm by the respondent No. 1. According to the petitioner, although there was a deed of dissolution of the firm, it was clearly stated that the continuing two partners had taken over the running business of the partnership firm with all the assets and liabilities

including the share payable to the retiring partner. The petitioners have filed the deed of dissolution, which is Annexure "D". A new deed of partnership was also executed by the continuing partners, of which a copy has been filed as Annexure "B". A letter dt. 7th Feb., 1985, was issued by the respondent No. 3, the ITO, Seoni, to the effect that for the asst. yr. 1981-82, it was found that the stock of silver on the last date of the accounting year had been valued by the firm at the rate of Rs. 1,255.70 per kg. whereas the market rate of silver, as on that date, was Rs. 2,727 per kg. It was stated that as the firm was dissolved from the asst. yr. 1981-82, the closing stock should have been valued at the market rate and it was proposed to initiate action under the Act to bring to tax the income by adopting the market rate of silver, as on Diwali, 1980. The petitioner firm was, therefore, called upon to submit its objections, if any. The petitioner submitted written objections pointing out that the petitioner had valued the closing stock at the average rate of opening stock and purchases, which worked out to Rs. 1,255.70 per kg., as per the practice uniformly followed by the petitioner. It was also pointed out that while making the assessment, the valuation had been checked and accepted by the ITO. The petitioner has submitted that without considering the objections, the respondent No. 3 issued a notice under s. 148 of the Act and the petitioners, therefore, filed the return repeating the income as shown in the return earlier filed on which an assessment had already been made. The petitioners also pointed out that no ground for proceedings under s. 147 of the Act. However, since the respondent No. 3 has proceeded with the matter in accordance with s. 147, the petitioners have filed this petition challenging the said proceedings.

4. The respondents have not filed any return, but Shri V.K. Tankha, Advocate, has appeared and opposed the petition.

5. Learned counsel for the petitioners has contended that the respondent No. 3 has fallen into a patent error in treating the firm to have been dissolved while it was only a case of change in the constitution of the firm and in fact, assessment had been made in accordance with s. 187 of the Act and the method of valuation of the stock consistently followed by the petitioners had been accepted. Under these circumstances, the learned counsel has contended, the respondent No. 3 could not have treated it to be a case of dissolution of the firm and initiated proceedings for valuation of the stock at the market rate. Learned counsel has also pointed out that it was not a case where any condition for initiating proceedings under s. 147 wasted as there had been no omission or failure on the part of the assessee to make a return or to disclose fully all material facts necessary for the assessment. Learned counsel has also contended that it was also not a case that any information had been received by the respondent No. 3 that income chargeable to tax had escaped assessment. Learned counsel for the respondents has refuted the contentions of the petitioner company on the ground that all these points can be raised before the AO and since, as per the petitioners, these grounds have already been raised by the petitioner company before him, the matter should be left to be considered by him only.

6. Learned counsel for the petitioner has referred to a Full Bench decision of this Court in Girdharilal Nannelal and Sukhlal Jhamaklal Vs. Commissioner of Income Tax, in support of his contention that if a firm is dissolved and succeeded by another firm which has, as its partners, one or more partners of the original firm, the case will be one covered by s. 187 of the IT Act as it would be merely a change in the constitution of the firm. Reference has also been made to a decision of a Division Bench of this Court in Vimal and Amar Talkies Vs. Commissioner of Income Tax, , in which it was held that where a partner in the old firm was also a partner in the new firm, it was a case of change in the constitution of the firm and not a case of succession of one firm by another firm and, therefore, only a single assessment could be made by applying the provisions of s. 187 of the Act.

7. Learned counsel for the respondents has referred to a decision of the Punjab & Haryana High Court in State Bank of Patiala Vs. Central Board of Direct Taxes and Others, and to another decision of the said Court in Smt Sunena Garg vs. Asst CIT (1995) 213 Itr 96 in support of his contention that firstly the ground fully existed for reopening the assessment under s. 147 and even if it is assumed that there was no dissolution of the firm comprising three partners, this point can be urged before the AO and remedy as per the machinery provided under the Act can be availed.

8. It is clear from the perusal of the communication Annexure "F" dt. 7th Feb., 1985 that the ground on which the action was sought to be initiated was that because the firm was dissolved from the asst. yr. 1981-82, the closing stock should have been valued at the market rate and not as per the method consistently followed by the dissolved firm. The notice under s. 148 is also issued to the firm dissolved firm through its partner Santosh Chand Nahata. Therefore, the question that falls for consideration is whether in the facts and circumstances of the case, there was, in fact, a dissolution of the firm or its succession by another firm and the case was not covered by s. 187 of the Act. In Vinal & Amar Talkies vs. CIT (supra), it was held that the perusal of ss. 187, 188 and 189 of the Act would go to show that the perusal of ss. 187, 188 and 189 of the Act would go to show that when the case is merely of a change in the constitution of the firm, the assessment is to be made under s. 187 on the firm as constituted at the time of making the assessment. The relevant observations contained in the said decision appearing at p. 664 read as follows:

"It is a well-settled principle of interpretation that words used by the legislature are not readily to be accepted as surplusage. The scheme of the sections appears to be that if a firm discontinues business or is dissolved without being succeeded by another firm, the case would be covered by s. 189. If a firm is dissolved and succeeded by another firm which has as its partners one or more partners of the old firm, the case will be one covered by s. 187, as it would be merely a change in the constitution of the firm as defined in sub-s. (2) thereof. If a firm is dissolved and is succeeded by another firm and none of the partners of the old

firm is a partner in the new firm, the case would be covered by s. 188. The omission of the words "or that a firm has been newly constituted" as they occurred in s. 26(1) of the 1922 Act from s. 187 is not indicative of any contrary intention because of the comprehensive definition enacted in the latter of the expression "a change in the constitution of the firm" and also because of the presence of the words "and the case is not one covered by s. 187, as they occur in s. 188. As the scheme of ss. 187, 188 and 189 is clear and there is no ambiguity in them, recourse to the provisions of the Partnership Act cannot be taken for construing them. In this view of the matter, the Tribunal, in our opinion, was right in applying s. 187 and not s. 188 to the facts of the instant case for the reason that Smt. Manubai who was a partner in the old firm was also a partner in the new firm and it was thus a case of the change in the partnership and not a case of succession of one firm by another falling under s.188. "

9. The above Division Bench decision was considered by the Full Bench in *Girdharilal Mannelal vs. CIT* (supra) and it was observed as follows :

"Sec. 188 of the IT Act, 1961, provides for cases of succession of one firm by another and excludes from its ambit the cases covered by s. 187 by using the words "and the case is not one covered by s. 187. These words used in s. 188 go to indicate that a situation which would be ordinarily one of succession under the general law, can also be within the ambit of s. 187 and, therefore, a case of that kind is excluded from the ambit of s. 188. Unless the legislature had included within the ambit of s. 187 a case which would ordinarily be one of succession, so as to fall under s. 188, there was no occasion to use the words 1 and the case is not one covered by s. 187" in s. 188. This is another reason to support the construction we have made of s. 187(2)(a). In our opinion, these are

some of the strong reasons to support the construction made by us of the expression "change in the constitution or a firm" occurring in s. 187.

In view of the above conclusion reached by us and our concurrence with the construction made by a Division Bench of this Court in *Vimal and Amar Talkies Vs. Commissioner of Income Tax*, , it is sufficient to quote, a portion of that decision. It was held therein, as under (p. 664) :

"The difficulty arises when a dissolved firm is succeeded by another firm, in which some of the partners of the old firm are members. Such a case would also be prima facie covered by the expression "a change in the constitution of the firm" as defined in cl. (a) of sub-s. (2) of s. 187."

10. In the present case, it is not disputed that the firm was earlier constituted of were partners of which one retired and the entire business rights and liabilities were taken over by the remaining two partners and although a deed of dissolution as also a deed of partnership had been executed, the firm was, in fact, continued by the two partners and, therefore, it was a case of change in the constitution of the firm duly covered by the provisions of s. 187 of the Act. The firm did not conceal any material and all the documents were made available at

the time of the assessment nor could it be said to be a case where the information was received by the AO subsequently to constitute foundation for a belief that the income chargeable to tax had escaped assessment in the said year. Even the ground on which the assessment was proposed under s. 147 of the Act viz. that it was a case of dissolution and the dissolved firm should have valued its closing stock at the market rate and not as per the method consistently followed by the firm, was not available in view of the law settled by the Full Bench in the aforesaid decision and there was no ground for proceeding under that section.

11. The objection of the learned counsel for the respondents is that even in such cases, it is open to the petitioner to raise objection before the AO and the pursue the remedy provided under the Act against any fresh assessment. Learned counsel has referred to the decision of the Punjab & Haryana High Court in *State Bank of Patiala vs. CWT* (supra), but in that case, the assessee had changed the system of accounting without disclosing the change in the method of accounting and it was held that it was not a case where the assessee had disclosed all material facts truly. It was against the backdrop of these facts that the notice of reassessment was not quashed. In the present case, the notice has been issued on the ground that the firm stood dissolved, meaning thereby that it was not a case of change in the constitution of the firm and this ground was non-existent. Thus, the very foundation on which the notice proceeds being non-existent, the notice cannot be sustained. Learned counsel for the Department has also referred to the decision in *Smt. Sunena Garg vs. Asstt. CIT* (supra), in which the petitioner was relegated to the remedy available under the statute to raise the disputed questions of facts on merits as well as on the question of jurisdiction. The claims of the petitioner were based on the ground that in subsequent years, the petitioners were allowed deduction on account of guarantee commission which was sought to be added to the income by issuing a notice under s. 148 of the Act. It is clear that in the said judgment, the facts were disputed, but in the present case where it is clear that the jurisdiction has been invoked on the basis of a non-existent ground, no further enquiry is necessary under the provisions of the Act and the petitioner

is, therefore, entitled to relief in proceedings under Art. 226 of the Constitution of India.

12. Learned counsel for the petitioner has also referred to the decision of this Court in *H.H. Maharaja Martand Singh Ju Deo vs. WTO & Anr.* (1997) 141 CTR (MP) 228, in which, where the assessee had disclosed the entire material in the return, which had been accepted in the yearly assessment and there was no material available with the WTO to form an opinion or to believe that any wealth chargeable to tax had escaped assessment, it was held that conditions for issuing notice under s. 17 of the WT Act did not exist and the notice was quashed. In the present case also, nothing has been brought on record by the respondents to indicate that there existed any ground or material for initiating proceedings

under s. 147 of the Act and the impugned notice and the proceeding correspondence indicate that the income is sought to be taxed on the non-existent ground that there was dissolution of the firm. while the case was covered by s. 187, it being only a change in the constitution of the firm.

13. Accordingly, this petition is allowed. The notice under s. 148 of the Act (Annexure F-2) is quashed and consequently, proceedings under s. 147 for the asst. yr. 1981~82 are also quashed. Parties are, however, left to bear their own costs.