
(1992) 01 SC CK 0061
In the Supreme Court Of India
Case No : 402 Of 1977

Commissioner of Income Tax

APPELLANT

Vs

Amritlal Nihalchand

RESPONDENT

Date of Decision : 21-01-1992

Acts Referred:

Income Tax Act, 1961 — Section 187, 188

Citation : (1992) 106 CTR 369 : (1992) 196 ITR 346

Hon'ble Judges : V. Ramaswami, J;S. Ranganathan, J;S. Mohan, J

Bench : Full Bench

Final Decision : dismissed

Judgement

B.J. Divan, C.J.—In this case, at the instance of the assessee, the following two questions have been referred to us for our opinion :

(1) Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that there was a change in the Constitution of the firm within the meaning of the said expression u/s 187 of the income tax Act, 1961, and, accordingly, the provisions of Section 188 were not applicable ?

(2) Whether, on the facts and in the circumstances of the case, the decision reached by the Tribunal, namely, that the income for the two periods November 3, 1967, to January 22, 1968, and January 23, 1968, to October 21, 1968, was required to be clubbed and assessed as a whole for the assessment year 1969-70 was correct in law ?

2. The facts leading to this reference are as follows. The relevant assessment year is 1969-70, the corresponding previous year being Samvat year 2024, that is, November 3, 1967, to October 21, 1968. The assessee firm is a registered partnership firm and it deals in cloth. For the assessment year 1969-70, the firm had filed two returns of income for two periods falling within Samvat year 2024 relevant to the assessment year 1969-70. The first return was for the period from November 3, 1967, to January 22, 1968, showing an income of Rs. 24,147.

The second return was for the period January 23, 1968, to October 21, 1968, showing a total income of Rs. 70,251. In this case, the original deed of partnership was executed on June 24, 1963, and, under this deed, the partnership was said to have come into existence with effect from April 15, 1963. The firm was carrying on business in the name of Messrs. Amritlal Nihalchand. It had two partners, Raichand Chunilal Daxini and Chaturdas Nihalchand Tanna. In this original partnership which is also referred to as "the old firm", two minors, Amritlal Nihalchand Tanna and Pratapbhai Sagalchand Chandan, were admitted to the benefits of the partnership. Amritlal Nihalchand Tanna attained majority on June 23, 1968. It is the case of the assessee that, with effect from January 22, 1968, the old firm was dissolved and the business of the old firm was taken over by another firm of the same name, namely, Messrs. Amritlal Nihalchand. The new firm also took over all the debts and liabilities together with the stock and tenancy rights of the old firm. In the old firm, the shares of the partners were :

Raichand Chunilal 25%

Chaturdas Nihalchand Tanna 22-1/2%

Amritlal Nihalchand Tanna 15% share in the benefits of the partnership

Pratapbhai Sagalchand 37-1/2% share, he also being a minor.

3. In the new partnership firm which came into existence, Raichand Chunilal retained his original share of 25%, Chaturdas Nihalchand got 7.5 per cent. share instead of 22-1/2 per cent., Amritlal Nihalchand got 20 per cent. share as a partner, Pratapbhai Sagalchand retained his benefits of the partnership to the extent of 37-1/2 per cent. and another minor, Mahesh Kumar Prabhudas, with a share in the benefits of the partnership to the extent of 10 per cent. was admitted to the benefits of the partnership. It appears that a new deed of partnership was executed on January 24, 1968, by the three adult partners of the new firm, namely, Raichand Chunilal Daxini, Chaturdas Nihalchand Tanna and Amritlal Nihalchand Tanna and the partnership deed stated that the old partnership firm was dissolved by the partners with effect from the end of January 22, 1968," and the new firm was constituted with effect from January 23, 1968. In the recital clause in the new partnership deed in terms, it was mentioned that, with effect from January 22, 1968, the old partnership business was closed, the old partnership firm was dissolved and brought to an end and all its rights, liabilities, stock, tenancy rights and the right to use the name of the firm had been taken over by the new firm in which there were three adult partners and the partnership deed of January 24, 1968, mentioned that the new firm had commenced business with effect from January 23, 1968. Under these circumstances, the firm filed two returns for the two separate periods, namely, from the commencement of the Samvat year, that is, November 3, 1967, to January 22, 1968, so far as the old firm was concerned and the other return being for the period January 23, 1968, to October 21, 1968, for the period in which the new firm had functioned as a business entity. It may also be

mentioned that intimations that the old firm was dissolved and the new firm had been brought into existence were sent to the Registrar of Firms functioning under the Indian Partnership Act and also to the income tax Officer. Along with the returns, an application in Form No. 12 for declaration regarding the continuance of the firm as well as an application for registration under Form No. 11 had been sent. The income tax Officer was of the view that the new firm had taken over the business of the old firm as a going concern and even though the income tax liabilities of the old firm were payable by the partners of the old firm, the tax payable by that firm was actually debited to the profit and loss account of the new firm. On these facts, he held that this was merely a case of a mere change in the Constitution of the firm and not a dissolution of the previous firm and he made a single assessment clubbing the income of the two periods together in the hands of the new firm. He also passed an order u/s 185 of the income tax Act, 1961, granting registration to the new firm for the assessment year 1969-70.

4. Against the decision of the income tax Officer, the assessee took the matter in appeal and the Appellate Assistant Commissioner accepted the contention of the assessee regarding the dissolution of the old firm and held that the income tax Officer had erred in clubbing the income for both the periods together and directed the income tax Officer to make separate assessments in respect of these two periods.

5. Against the decision of the Appellate Assistant Commissioner, the matter was taken in appeal before the income tax Appellate Tribunal by the Revenue. On behalf of the Revenue, it was contended that this was a case of a mere change in the Constitution as contemplated by Section 187. In the alternative, it was urged that even if it was assumed that this was a case of succession, it would be governed by Section 187 of the Act and not by Section 188. The Revenue contended before the Tribunal that the decision of the Bombay High Court in *Bhausia Ganusa Pawar and Co. Vs. Commissioner of Income Tax, Poona*, was not applicable to the facts of the present case and that the decision in *R.B. Jessa Ram Fateh Chand Vs. Commissioner of Income Tax*, would govern the facts of the case. The Revenue also relied upon the decision in *Excel Productions, Alleppey Vs. The Commissioner of Income Tax, Kerala, Ernakulam*, . Even apart from these derisions, the Revenue urged before the Tribunal that the provisions of Section 187 were mandatory and the expression "change in constitution" as provided in Section 187 would be applicable to the facts of the case. The Tribunal came to the conclusion that the assessee's case clearly fell within the expression "change in constitution" as defined in the Act and the fact that the new firm had made some averments in the partnership deed would not make any difference to the requirements of the law which were quite clear on the point. The Tribunal, therefore, held that the provisions of Section 188 were not applicable but the assessee's case was governed by the provisions of Section 187 of the Act. The Tribunal, therefore, set aside the order of the Appellate Assistant Commissioner and restored the order of the income tax Officer. Thereafter, at the instance of the assessee, the questions hereinabove set out have been referred to us for our

opinion.

6. We find that the point which arises for our consideration in this case is now covered by a decision of this High Court in Addl. Commissioner of Income Tax, Gujarat Vs. Harjivandas Hathibhai, . This High Court has pointed out in Addl. Commissioner of Income Tax, Gujarat Vs. Harjivandas Hathibhai, that the decision of the Allahabad High Court in R. B. Jessa Ram Fateh Chand [1972] 81 ITR 409 has been overruled by the decision of a Full Bench of the same High Court in Dahi Laxmi Dal Factory v. ITO [1971] 103 ITR 517, After considering the legal position, it was held that Section 187 of the income tax Act does not introduce any change in the relationship between the parties and does not introduce a change from the general law of partnership as laid down by the Indian Partnership Act. It was contended on behalf of the Revenue before us, as has been contended in the instant case that, in view of the provisions of Section 187 and particularly Sub-section (2) of that section, even if there is a dissolution of an old firm and some of the partners continue in the new firm, by virtue of Sub-section (2) of Section 187, there is, in the eye of the law, particularly the income tax law, a mere continuation of the firm and not a case of succession of one firm by another. After examining the different decisions on the point and the provisions of the Partnership Act, this High Court Addl. Commissioner of Income Tax, Gujarat Vs. Harjivandas Hathibhai, agreed with the summary of the legal position as set out by Gulati J. in the Full Bench decision Dahi Laxmi Dal Factory Vs. Income Tax Officer and Another, and the summary is to the following effect (see Addl. Commissioner of Income Tax, Gujarat Vs. Harjivandas Hathibhai,

To sum up, the legal position that emerges is that Section 187 applies only where a firm is reconstituted in accordance with Sections 31 and 32 of the Indian Partnership Act, namely, when a new partner is taken or an existing partner retires with the consent of all the partners or without their consent if the contract of partnership so provides. But, where a firm is dissolved either by agreement of the partners or by operation of law and another firm takes over the business that will be a case of succession governed by Section 188 of the Act even though some of the partners of the two firms are common.

7. This High Court has also pointed out (see Addl. Commissioner of Income Tax, Gujarat Vs. Harjivandas Hathibhai,

Even apart from the decision of the learned judges of the Allahabad High Court in the Full Bench decision referred to above, it is obvious on general principles that unless the words of the income tax Act compel us to do so, it would not be correct to depart from the well-known principles of partnership law. The partnership law contemplates retirement of a partner and even though a partner retires, the firm continues as before. What is meant by a change in the Constitution of the firm is coming in of a new partner with the consent of all the existing partners or by the retirement of a partner with the consent of all the partners in such cases there is a mere change in the, Constitution of the firm and nothing more. The same firm continues as before. The question of dissolution of

a firm either by operation of law or by act of parties is a different thing altogether. When a firm is dissolved, the old relationship comes to an end and a new relationship comes into existence and if the succeeding partnership firm continues the old business, then, there is succession of one firm by another as contemplated by Section 188. Sub-section (2) of Section 187 merely specifies two kinds of changes in the Constitution of the firm. Clause (a) of Sub-section (2) of Section 187 refers to the continuance of the firm on one or more of the partners ceasing to be partners or one or more new partners being admitted. It deals with cases of retirement of partners and introduction of new partners but the firm under the Indian Partnership Act would continue in such a case. Therefore, all that Sub-section (2) of Section 187 points out is that with the retirement of one or more of the partners, so long as one of the old partners continues and with the introduction of new partners so long as one of the old partners continues, there is a mere change in the Constitution of the firm. Again, under Clause (b) of Sub-section (2) of Section 187, by a mere variation in the respective shares of the partners or shares of some of the partners, there is no change in the firm itself. The old firm still continues and that is emphasised by Clause (b) of Sub-section (2) of Section 187.

8. For the reasons set out in the decision in *Addl. Commissioner of Income Tax, Gujarat Vs. Harjivandas Hathibhai*, it must be held that the view taken by the Tribunal in the instant case was not in accordance with law.

9. The facts are not in dispute and cannot be in dispute. The major partners, namely, Raichand Chunilal Daxini and Chaturdas Nihalchand Tanna who were the major partners in the old firm, agreed to dissolve the firm and that agreement of the two partners in the firm which was a partnership at will, as pointed out by the deed of partnership dated June 24, 1963, annexure 'J' to the statement of the case, and in view of the recital in the deed of partnership dated January 24, 1968, annexure 'L' to the statement of the case, it is obvious that the major partners of the said firm had agreed to dissolve the old firm and the same partners, along with Amritlal Nihalchand, who had in the meantime attained majority, agreed to start the new firm with effect from January 23, 1968. It is true that, subsequently, the two adult partners, Raichand Chunilal Daxini and Chaturdas Nihalchand Tanna executed a deed of dissolution dated February 18, 1968, stating that that firm had been dissolved by them with effect from January 22, 1968, but merely because the decision to dissolve taken in the past came to be recorded subsequently in the form of a deed of dissolution, it does not mean that there was earlier dissolution of the firm. Moreover, as Mr. Thakore for the assessee has pointed out, the intimations had been sent to the Registrar of Firms about the dissolution of the old firm and also to the income tax Officer about the dissolution of the old firm and hence the dissolution of that firm can be safely accepted. Even Mr. Kaji for the Revenue has not urged that there was no dissolution of the firm. All that he contends is that, in spite of the dissolution of the firm, by virtue of Section 187, Sub-section (1), of the Act, it must be held that there was a mere change in the Constitution of the firm and that the old

firm had continued and so far as the income tax law was concerned, there was no succession within the meaning of Section 188. For the reasons stated above, this contention on behalf of the Revenue must be rejected.

10. It must, therefore, follow that the view of the Tribunal about there being a mere change in the Constitution of the firm within the meaning of Section 187 was not correct and it must be held that this is a case of succession within the meaning of Section 188 and the case did not fall under the provisions of Section 187 of the Act. The view taken by the Tribunal that there was a change in the Constitution of the firm within the meaning of the said expression u/s 187 of the Act and accordingly the provisions of Section 188 were not applicable was not correct. It is true, as has been pointed out before us, that Section 188 mentions that it would apply when the case is not one covered by Section 187 but once it is found that no departure from the provisions of the Indian Partnership Act is contemplated by Section 187 of the income tax Act, 1961, it must follow that the instant case would not fall u/s 187 and, therefore, this being a case of succession of the old firm by the new firm, the case would be governed by Section 188.

11. We, accordingly, answer the questions referred to us as follows :

Question No. 1. In the negative, that is, in favour of the assessee and against the Revenue.

Question No. 2. In the negative, that is, in favour of the assessee and against the Revenue.

ORDER

The question at issue in this case is fully covered by the decision of this Court in Wazid Ali Abid Ali Vs. Commissioner of Income Tax, Lucknow, . This appeal, therefore, fails and is dismissed. No costs.