
(1984) 02 MAD CK 0010

In the Madras High Court

Case No : Tax Case No's. 381 to 383 of 1979

Commissioner of Income Tax

APPELLANT

Vs

M.V.S. Sastry

RESPONDENT

Date of Decision : 07-02-1984

Acts Referred:

Income Tax Act, 1961 — Section 155(5), 33, 34, 34(3), 41(2)

Citation : (1986) 157 ITR 543

Hon'ble Judges : V. Ratnam, J;G. Ramanujam, J

Bench : Division Bench

Advocate : J. Jayaraman, for the Appellant; M. Uttam Reddy, for the Respondent

Judgement

Ramanujam, J.—The following two common questions have been referred to this court at the instance of the Revenue by the Income Tax

Appellate Tribunal :

1. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that when the Hindu undivided family

business, after partition was converted into a partnership business there was no transfer involved and that, therefore, the development rebate

allowed to the Hindu undivided family could not be withdrawn u/s 155(5) of the Act ?

2. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that there was no violation of section

34(3)(a) ?

2. The assessee is a Hindu undivided family represented by its karta, Shri M. V. S. Sastry. The Hindu undivided family, consisting of the karta and

his three major sons, was carrying on business of printing and was allowed

development rebate on the machinery used in that business. There was a partition on March 31, 1974, and the joint family business was converted into a business of partnership consisting of Shri M. V. S. Sastry and his three sons as partners. Thus the business and the assets which originally belonged to the Hindu undivided family became the assets of the partnership firm and this according to the Income Tax Officer involved a transfer as contemplated u/s 155(5)(i) of the Income tax Act, 1961, hereinafter referred to as the Act, justifying the withdrawal of the development rebate allowed to the Hindu undivided family earlier. The Income Tax Officer was of the view that the development rebate allowed to the Hindu undivided family is wrong as there is a transfer of assets within 8 years from the joint family to the partnership firm after partition and in that view, he withdrew the development rebate allowed on the machinery used in the printing business for the assessment years 1966-67, 1968-69 and 1969-70 by rectifying the earlier assessment orders.

3. The assessee took the matter in appeal and the Appellate Assistant Commissioner, following the decision of the Kerala High Court in A. Abdul Rahim, Travancore Confectionery Works Vs. Commissioner of Income Tax, , held that the Hindu undivided family and the partnership are two different entities and as the assets belonging to the Hindu undivided family have been transferred to the partnership firm, the withdrawal of the development rebate u/s 155(5)(i) of the Act was fully justified.

4. There was a further appeal by the assessee to the Income Tax Appellate Tribunal contending that when there was a partition in the Hindu undivided family, there was no transfer of assets and when the partnership was formed after partition, even then there was no transfer as the partnership firm is not a legal entity and is only a convenient and compendious name given to a contractual relationship in which two or more persons combined their efforts and conjointly applied the same to a commercial activity with a view to make profits. On the other hand, the contention of the Revenue before the Tribunal was that the Hindu undivided family and the partnership firm are two different entities and when the business and the assets belonging to the Hindu undivided family became the assets of the partnership, there is a transfer from one entity to another entity and the action of the Income Tax Officer in withdrawing the development

rebate u/s 155(5)(i) was justified, and reliance was placed by the Revenue on the decision of the Supreme Court in Commissioner of Income Tax, Gujarat Vs. B.M. Kharwar, . The Tribunal, relying on the decisions in D. Kanniah Pillai Vs. Commissioner of Income Tax, and A. Subbiah Nadar Vs. Commissioner of Income Tax, , held that when the Hindu undivided family business after partition was converted into a partnership business, that did not involve any transfer to justify the withdrawal of the development rebate. The Tribunal also found that there are clear recitals in the partition deed that the capital account of the family standing in the books of the printing business was first debited with the amounts provided for the wife and daughters of the karta for their maintenance and the balance was divided into equal shares and the individual accounts of the partners were credited with their 1/4th share in the capital account and the contention of the Revenue that a portion of the amount credited to the reserve account u/s 34(3)(a) was distributed to the female members of the Hindu undivided family at the time of the partition was not established and, therefore, there is no utilisation of the reserve for non-business purposes as alleged by the Revenue. Aggrieved by the decision of the Tribunal, the Revenue sought and obtained a reference on the questions set out above.

5. Section 155(5) provides that where an allowance by way of development rebate has been made wholly or partly to an assessee in respect of a machinery in any assessment year u/s 33 and subsequently at any time before the expiry of eight years from the end of the previous year in which the machinery was installed, the machinery is sold or otherwise transferred by the assessee to any person, or at any time before the expiry of the said eight years, the assessee utilises the amount credited to the reserve account under clause (a) of sub-section (3) of section 34 for distribution by way of dividends or profits or for any remittance outside India as profits or for any other purpose which is not a purpose of the business of the undertaking, then the development rebate originally allowed shall be deemed to have been wrongly allowed and the Income Tax Officer may recompute the total income of the assessee for the relevant previous years and make the necessary amendment u/s 154.

6. Admittedly, in this case, the Hindu undivided family had been originally given the development rebate for the three years in question.

Subsequently, after the disruption took place in the Hindu undivided family, a firm was constituted by the erstwhile members of the family and the business assets which originally belonged to the Hindu undivided family became the property of the partnership. It is also not in dispute that the Hindu undivided family had a reserve account as contemplated by section 34(3). According to the Revenue, when the joint family assets became the assets of the partnership firm, another taxable entity, it amounts to a transfer as contemplated by section 155(5)(i) and, therefore, the development rebate granted to the Hindu undivided family has to be withdrawn. It is also contended by the Revenue that since the portion of the reserve created u/s 34(3) by the joint family had been transferred to the female members of the family, it amounted to utilisation for a non-business purpose as contemplated by section 155(5)(ii) and, therefore, the withdrawal of the development rebate could be justified on that ground.

7. On a perusal of the order passed u/s 155(5)(i) by the Income Tax Officer, it is seen that the withdrawal of the development rebate was only on the ground that there is a transfer of assets as contemplated by section 155(5)(ii). A perusal of the order of the Appellate Assistant Commissioner also indicates that the withdrawal of the development rebate was not based on section 34(3)(a) read with section 155(5)(ii). It is only at the stage of the appeal before the Tribunal, it was contended that there was a violation of section 155(5)(ii) in that there has been a distribution of the reserve amount to the female members of the Hindu undivided family at the time of the partition. The Tribunal has specifically found that in view of the recitals in the partition deed, there is no basis for the contention of the Revenue that a portion of the amount credited to the reserve account u/s 34(3)(a) was distributed to the female members of the family at the time of the partition. In view of the factual position arrived at by the Tribunal, it cannot be held that there has been a violation of section 34(3)(a) read with section 155(5)(ii). We, therefore, answer the second question in the affirmative and against the Revenue.

8. Coming to the first question, as already stated, the Tribunal, relying on the decisions in *D. Kanniah Pillai Vs. Commissioner of Income Tax*, and

A. Subbiah Nadar Vs. Commissioner of Income Tax, , held that the conversion of the joint family business into a partnership business does not

involve any transfer and, therefore, the withdrawal of the development relate cannot be justified. *D. Kanniah Pillai Vs. Commissioner of Income*

Tax, , was a case where the assessee, an individual, who was carrying on transport business, converted his proprietary business into a business of

partnership consisting of himself and another person and the question arose whether by conversion of the proprietary business into a partnership

business, any transfer of assets of the business from the assessee to the partnership firm is involved. The court held that there was no transfer from

the assessee to the partnership firm either u/s 41(2) or u/s 45 of the Act. In *A. Subbaiah Nadar v. CIT [1976] 104 ITR S64*, the assessee along

with his two sons constituting a Hindu undivided family owned certain lorries which were later transferred to a partnership firm consisting of the

assessee, his two sons and the assessee's divided brother. The question arose as to whether the difference between the market value of the lorries

and the written down value is chargeable to tax u/s 41(2). The Tribunal held that by the transfer of the lorries to the partnership, the ownership was

transferred from the joint family to a different entity and hence section 41(2) was attracted. Reversing the decision of the Tribunal, the High Court

held that there was no transfer when the partnership firm took over the lorries from the joint family and that the true legal position is that when a

business carried on by a Hindu undivided family after partition was converted into a partnership business, there was no transfer involved either for

purposes of section 41(2) or of section 45. In *Additional Commissioner of Income Tax Vs. Dalmia Magnesite Corporation*, , the question arose as

to whether the relief granted to a firm u/s 15C of the 1922 Act could be withdrawn on the ground that there has been a splitting up or

reconstruction of the firm which carried on the industrial undertaking and the court held that there is no reconstruction or splitting up of a business

already in existence and, therefore, the benefit of relief granted to the firm u/s 15C cannot be withdrawn. In *Malabar Fisheries Co. Vs.*

Commissioner of Income Tax, Kerala, , the Supreme Court had dealt with a question as to whether the distribution of assets between the partners

on dissolution amounts to a transfer so as to attract sections 34(3)(b) and 155(5) of the Act and the Supreme Court had held that the partnership

firm under the Indian Partnership Act, 1932, is not a legal entity apart from the partners constituting it, that equally in law the firm as such has no

separate rights of its own in the partnership assets, that when the partnership assets are distributed as between the partners at the time of the dissolution, there is no transfer of assets involved even in the sense of any extinguishment of the firm's rights in the partnership assets and that, therefore, section 34(3)(b) will not stand attracted. In Commissioner of Income Tax, Tamil Nadu-I Vs. S. Balasubramanian, , this court directly dealt with the question of withdrawal of development rebate based on the alleged violation of sections 34(3)(b) and 155(5). This court, after a detailed consideration of the earlier decisions both of this court and of the Supreme Court, held that three conditions must be satisfied for the withdrawal of the development rebate under sections 34(3)(b) and 155(5), namely, (1) the machinery or plant must have been sold or otherwise transferred; (2) that such a sale or transfer must be by the assessee; and (3) that the sale must be before the expiry of eight years from the end of the previous year in which it was acquired or installed. In that case, it was held that though there was a transfer of the machinery, the transfer was not by the assessee but by some other person to whom the assets had been allotted. Thus, even assuming that after the partition of the joint family assets among its coparceners, they had transferred their share in the assets to the partnership, (the transfer was) not by the assessee and the same cannot attract the provisions in sections 34(3)(b) and 155(5). Thus, as a result of the above discussion, in any event, sections 34(3)(a) and 155(5) cannot be applied to the facts of this case and the development rebate granted already could not be withdrawn.

9. In this view of the matter, we have to agree with the order of the Tribunal. Hence, the first question is also answered in the affirmative and against the Revenue. The Revenue will pay the costs of the assessee. Counsel's fee Rs. 500 (one set).