
(1972) 02 AHC CK 0036

In the Allahabad High Court

Case No : Wealth-tax Reference No. 166 of 1970

Commissioner of Wealth Tax

APPELLANT

Vs

Padampat Singhania

RESPONDENT

Date of Decision : 09-02-1972

Acts Referred:

Wealth Tax Act, 1957 — Section 2
Wealth Tax Rules, 1957 — Rule 2

Citation : (1973) 90 ITR 418

Hon'ble Judges : S.N. Dwivedi, J; R.L. Gulati, J

Bench : Division Bench

Advocate : R.R. Misra, for the Appellant; V.B. Upadhyaya, for the Respondent

Judgement

Gulati, J.—This is a reference u/s 27(1) of the Wealth-tax Act, 1957. It is a consolidated reference relating to several assessment years, viz., 1957-58 to 1963-64. The following common question of law has been referred for the opinion of this court:

" Whether, on the facts and in the circumstances of the case, the provisions of Section 2(m) of the Wealth-tax Act, 1957, are applicable for determination of the assessee's interest in the wealth of the firm styled as M/s. J. K. Bankers for the assessment years 1957-58 to 1963-64 ? "

2. The assessee is a Hindu undivided family. It holds through its karta 1/3rd share in a partnership firm of the name and style of Juggilal Kamlatpat Bankers (hereinafter referred to as " the firm"). While computing the net wealth of the assessee for each of the seven years, the Wealth-tax Officer had to take into consideration the assessee's share in the wealth of the firm. While computing that share the Wealth-tax Officer took the net wealth of the firm as per its books of accounts ignoring the liability of the firm on account of the outstanding Income Tax. The assessee appealed and contended, inter alia, that in order to determine the net wealth of the firm for the purposes of including 1/3rd share of that wealth in the wealth-tax assessment of the assessee, it was necessary for

the Wealth-tax Officer to have deducted out of the assets of the firm its outstanding Income Tax liability, because net wealth had to be taken after deducting out of the gross assets of the firm its total debts and the Income Tax liability was a debt outstanding against the firm, which should have been taken into consideration. The Appellate Assistant Commissioner of Income Tax did not accept this contention. He held" that the liability on account of Income Tax could not be deducted while computing the net wealth of the firm because of the provisions contained in Sub-clauses (a) and (b) of Clause (iii) of Section 2(m) of the Act. On second appeal, the Income Tax Appellate Tribunal reversed the finding of the Appellate Assistant Commissioner of Income Tax and held that Section 2(m) was not applicable in the instant case and, as such, the outstanding Income Tax liability was deductible while computing the net wealth of the firm. The Commissioner is aggrieved and has brought this reference before us.

3. It appears that a large sum of money was due from the firm by way of Income Tax. The Income Tax liability was outstanding on the valuation dates of each of the assessment years in question. The firm had contested the liability by way of appeal but later on entered into a settlement with the department as a result of which the firm withdrew its appeals and the department granted installments for the payment of the outstanding Income Tax liability.

4. Where the assessee is an individual, his net wealth is to be computed in accordance with Section 4(1)(b) of the Wealth-tax Act, which reads :

" 4. Net wealth to include certain assets.--(1) In computing the net wealth of an individual, there shall be included, as belonging to that individual--.....

(b) where the assessee is a partner in a firm or a member of an association of persons, the value of his interest in the firm or association determined in the prescribed manner."

5. The manner for the determination of the value of the interest of an individual in a firm is contained in Rule 2 of the Wealth-tax Rules. Paragraph 1 of that rule is material and reads :

"2. Valuation of interest in partnership or association of persons.--(1) The value of the interest of a person in a firm of which he is a partner or in an association of persons of which he is a member, shall be determined in the manner provided herein. The net wealth of the firm or the association on the valuation date shall first be determined. That portion of the net wealth of the firm or association as is equal to the amount of its capital shall be allocated among the partners or members in the proportion in which capital has been contributed by them. The residue of the net wealth of the firm or association shall be allocated among the partners or members in accordance with the agreement of partnership or association for the distribution of assets in the event of dissolution of the firm or association, or in the absence of such agreement, in the proportion, in which the partners or members are entitled to share profits. The sum total of the amounts so allocated to a partner or member shall be treated as the value of the interest

of that partner or member in the firm or association."

6. It is thus clear that so far as the valuation of the interest of a partner in a firm is concerned, the same has to be arrived at in accordance with Rule 2. According to that rule, first of all the net wealth of the firm on the valuation date has to be determined. Thereafter the same is to be allocated between the partners in the manner indicated in that rule. We are not concerned in this case with the manner in which the net wealth of the firm is to be allocated between the partners. All we are concerned with is to find out as to how the net wealth of the firm should have been determined.

7. The term " net wealth " according to ordinary commercial principles means the real wealth of a man. His real wealth would be his total assets minus the debts owed by him. This is in essence the definition of " net wealth " as given in Section 2(m), which defines " net wealth " to mean " the amount by which the aggregate value computed in accordance with the provisions of this Act of all the assets, wherever located, belonging to the assessee on the valuation date, including assets required to be included in his net wealth as on that date under this Act, is in excess of the aggregate value of all the debts owed by the assessee on the valuation date other than" Then follow certain clauses of Section 2(m) which provide that certain kinds of debts shall not be excluded from the aggregate value of the assets. Clause (iii) relates to debts relating to tax, penalty or interest under certain taxing statutes and reads as under :

" (iii) the amount of the tax, penalty or interest payable in consequence of any order passed under or in pursuance of this Act or any law relating to taxation of income or profits, or the Estate Duty Act, 1953, the Expenditure-tax Act, 1957, or the Gift-tax Act, 1958;

(a) which is outstanding on the valuation date and is claimed by the assessee in appeal, revision or other proceeding as not being payable by him, or

(b) which, although not claimed by the assessee as not being payable by him, is nevertheless outstanding for a period of more than twelve months on the valuation date."

8. This is a special provision relating to liability on account of Income Tax, etc., which though a debt in the ordinary commercial sense, is not to be taken into consideration while determining the net wealth of an assessee. The idea of this provision obviously is to ensure that taxes are promptly paid by an assessee, otherwise he would be deprived of the benefit of their deduction while computing his net wealth. This provision obviously applies when computing the net wealth of an assessee.

9. In the instant case the firm is not the assessee so that the net wealth of the firm is not to be assessed. The assessee is the karta of a Hindu undivided family. In computing his net wealth any Income Tax liability outstanding against him may not be deducted under this provision but the Income Tax liability of a firm,

of which he is a partner, cannot be left out of consideration by virtue of this provision. While determining the net wealth of the firm not for the purpose of assessment but for the purpose of finding out an assessee's share in it, Sub-clauses (a) and (b) of Clause (iii) of Section 2(m) would not be applicable. The net wealth under Rule 2 is to be determined in accordance with the commercial principles and when so done, all the debts owed by a firm of whatever nature and of whatever duration have to be deducted so long as the debts are legally enforceable against the firm.

10. Now the Income Tax liability of the firm is a legally enforceable debt against it. The fact that it is payable in installments makes no difference. Any amount outstanding on the valuation date would be a debt deductible while computing net wealth of the firm. Rule 2 provides a complete mode for the determination of the net wealth of the firm for the purpose of allocating it among its partners and the special provision relating to Income Tax liability contained in Sub-clauses (a) and (b) of Clause (iii) of Section 2(m) cannot be applied.

11. There is yet another reason why the restrictions contained in Section 2(m) (iii) cannot be applied in such a case. The object of the restrictions, as has been stated earlier, is to put pressure upon the assessee to make prompt payment of tax liabilities. Where an assessee does not pay tax liability promptly he is deprived of the benefit of deducting the same in his wealth-tax assessment. A partner whose wealth-tax assessment is to be made may not be in arrears of Income Tax at all. He may have cleared all his Income Tax dues. In such a case there is no reason why he should be penalised for a default of a firm of which he is a partner. The interpretation that we have put appears to be in accordance with the intention of the legislature.

12. We accordingly answer the question in the negative. The assessee is entitled to the costs, which we assess at Rs. 200.