
(1973) 01 P&H CK 0025

In the Punjab And Haryana At Chandigarh

Case No : Income-tax Reference No. 11 of 1972

Dharam Pal Sat Dev

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 04-01-1973

Acts Referred:

Income Tax Act, 1961 — Section 187(2), 188
Partnership Act, 1932 — Section 42

Citation : (1974) 97 ITR 302

Hon'ble Judges : Prem Chand Pandit, J;Bhopinder Singh Dhillon, J

Bench : Division Bench

Advocate : S.P. Mehta and J.D. Chopra, for the Appellant; D.N. Awasthy and B.S. Gupta, for the Respondent

Judgement

Bhopinder Singh Dhillon, J.—The brief facts giving rise to this Income Tax reference are that Sarvshri Dharam Pal, Sat Dev and Ram Rattan entered into a partnership, vide partnership deed dated December 8, 1954, for carrying on the business of wholesale cloth dealers. Shri Ram Rattan died on June 6, 1966. There was no provision in the partnership deed for the continuance of the partnership in the event of death of any partner and, therefore, it is pleaded by the assessee that, in view of the provisions of Section 42(c) of the Indian Partnership Act, the firm stood dissolved on June 6, 1966, On June 9, 1966, a new partnership was formed between Sat Dev and Dharam Pal, partners of the dissolved firm, and Shri Sham Lal, son of the deceased partner, Shri Ram Rattan, Two returns were filed for the assessment year 1967-68, the first for the period from December 18, 1965, to June 8, 1966, and the second for the period from June 9, 1966, to March 31, 1967. The Income Tax Officer, while assessing, vide his order dated March 13; 1968, clubbed the income of the two firms and passed a single assessment order holding the view that it was a case of a change in the constitution of the firm. The appeal filed by the assessee before the Appellate Assistant Commissioner failed and, similarly, the second appeal filed before the Tribunal also having failed, this reference was made to this court at the instance

of the assessee, in the following terms:

"Whether, on the facts and in the circumstances of the case, the assessment for both the periods was justified in view of the provisions of Section 187(2) of the Income Tax Act, 1961 ? "

2. The main contention of the learned counsel for the assessee is that the provisions of Section 188 of the Income Tax Act, 1961, are applicable to the facts of the present case as, according to the learned counsel, the firm of which Ram Rattan, deceased, was a partner stood dissolved in view of the provisions of Section 42(c) of the Indian Partnership Act, as there was no provision in the partnership deed providing that, in the event of death of any partner, the partnership would continue. It is contended that a completely new entity came into being on June 9, 1966, when a new partnership was formed with Sat Dev and Dharam Pal, the two partners of the previous firm and Sham Lal, son of the deceased partner, Ram Rattan. It is, therefore, contended that, keeping in view the provisions of the Partnership Act, this was a new entity coming into existence and, therefore, it was a case of succession of one firm by another. It is contended that provisions of Section 187(2) of the Income Tax Act, 1961, have been wrongly applied by the Income Tax authorities and a legal entity which stood dissolved by the death of one of the partners cannot be said to be continuing when another legal entity was brought into existence by the partnership deed by way of a new firm.

3. In order to appreciate the point involved in the case, a few relevant provisions of the Income Tax Act, 1961, may be reproduced.

4. Section 170 of the Income Tax Act deals with the succession of business or profession by another person who continues to carry on the business or profession, whereas Section 188 of the Income Tax Act deals with succession of one firm by another which may be reproduced as under :

"188. Succession of one firm by another firm.--Where a firm carrying on a business or profession is succeeded by another firm, and the case is not one covered by Section 187, separate assessments shall be made on the predecessor-firm and the successor-firm in accordance with the provisions of Section 170."

5. Section 187 of the Act deals with the change in the constitution of the firm and is in the following terms :

"187. Change in constitution of a firm.--(1) Where at the time of making an assessment u/s 143 or Section 144 it is found that a change has occurred in the constitution of a firm, the assessment shall be made on the firm as constituted at the time of making the assessment:

Provided that-

(i) the income of the previous year shall, for the purposes of inclusion in the total incomes of the partners, be apportioned between the partners who, in such

previous year, were entitled to receive the same ; and

(ii) when the tax assessed upon a partner cannot be recovered from him, it shall be recovered from the firm as constituted at the time of making the assessment.

(2) For the purposes of this section, there is a change in the constitution of the firm-

(a) if one or more of the partners cease to be partners or one or more new partners are admitted, in such circumstances, that one or more of the persons who were partners of the firm before the change continue as partner or partners after the change ; or

(b) where all the partners continue with a change in their respective shares or in the shares of some of them."

6. Lastly, Section 189 of the Act deals with the dissolved firms. The purpose of enacting these provisions by the legislature is to provide for all exigencies so that the assessee, who are liable to pay the Income Tax, do not escape their liability in different eventualities. It is conceded by the learned counsel for the assessee that, where the provisions of the Income Tax Act are clear, no other enactment has to be taken into consideration while considering the liability of the assessee. In this view of the matter, the provisions of the Partnership Act can only be referred to if it is found that a particular situation is not covered by the provisions of the Income Tax Act. Though a particular firm, in view of the provisions of Section 42(c) of the Indian Partnership Act, may stand dissolved, if we come to the conclusion that such a case is covered by the provisions of Section 187 of the Act, the assessee cannot get the benefit of the said dissolution of the firm for the purposes of the Income Tax Act. The case of the assessee is that his case is covered by Section 188 of the Act, The bare reading of this section makes it clear that this section would not apply to cases which are covered by Section 187 of the Act. So the whole question to be considered is whether, keeping in view the facts and circumstances of the present case, the provisions of Section 187 of the Act are attracted or not; in other words, whether it is a change in the constitution of the firm or not. Section 187(2) of the Act defines as to what is to be considered as a change in the constitution of the firm so as to make applicable the provisions of Sub-section (1). It is provided that if one or more of the partners cease to be partners or one or more new partners are admitted, in such circumstances that one or more of the persons who were partners of the firm before the change continue as partner or partners after the change; or where all the partners continue with a change in their respective shares or in the shares of some of them, it shall be considered to be a change in the constitution of the firm for the purposes of Sub-section (1). The question is whether the facts of the present case answer the description of the change in the constitution as defined in Sub-section (2) and the clear answer is that it does. In the present case, only one partner, namely, Ram Rattan, ceased to be a member of the firm on account of his death and his son, Sham Lal, was entered as a new

partner in his place. The other two partners, namely, Sat Dev and Dharam Pal, remained the same. Therefore, the two partners remaining the same and there being only a change in one partner, as one partner ceasing to be a partner on account of his death and another partner entering into partnership, this answers the description of Sub-section (2) of Section 187 of the Act and it has been rightly held by the authorities below that this constituted a change in the constitution of the firm.

7. The contention that the previous firm as a legal entity, came to an end on the death of Ram Rattan and a new firm came into existence by the joining of Shami Lal loses sight of the fact that, for the purposes of the Income Tax Act, this will be considered to be a change in the constitution of the firm as when dealing with the matters under the Income Tax Act, as to whether a particular case is a change in the constitution of the firm or not, the ingredients of Sub-section (2) of Section 187 of the Act have to apply. A particular case can only be covered by Section 183 of the Act when it is a succession of one firm by another, meaning thereby that there is a complete change and no one of the partners in the previous firm continue to be a partner in the latter firm, which is; not the present case.

8. In Commissioner of Income Tax, Bihar and Orissa Vs. Kirkend Coal Co., , the Supreme Court relied upon the observations made in Shivram Poddar Vs. Income Tax Officer, Central Circle II, Calcutta, and Another, wherein their Lordships of the Supreme Court, while examining the scheme of Section 44 (before it was amended by the Finance Act of 1958) and its inter-relation with the provisions of Sections 26(2), etc., observed as under:

""Where the firm is dissolved, but the business is not discontinued, there being a change in the constitution of the firm, assessment has to be made u/s 26(1), and if there be succession to the business, assessment has to be made u/s 26(2). The provisions relating to assessment on reconstituted or newly constituted firms, and on succession to the business are obligatory. Therefore, even when there is change in the ownership of the business carried on by a firm on reconstitution or because of a new constitution, assessment must still be made upon the firm. When there is succession, the successor and the person succeeded have to be assessed each in respect of his actual share. This scheme of assessment: furnishes the reason for omitting reference to dissolution of a firm from Section 44 when such dissolution is not accompanied by discontinuance of the business."

9. The next case which may be usefully referred to at this stage is a Bench decision of this court in Hoshiarpur Electric Supply Co. Vs. Commissioner of Income Tax, . In that case the relevant question which may be useful for the purposes of the present case was whether the petitioner-firm was liable to be assessed to tax under the second proviso to section 10(2)(vii) of the Act in respect of depreciation allowed to it right from its inception in 1930. It was held by the learned judges of this court that the technical view of the nature of a

partnership under English law or Indian law could not be taken in applying the law of Income Tax. The true question to decide is one of the identity of the unit assessed under the Income Tax Act. It was held that a firm is a unit of assessment as an independent unit with a personality which survives its reconstitution. On the facts of that case it was held that the business of the firm, originally constituted, continued as the electrical undertaking at Hoshiarpur from the very beginning right down to the purchase by the Punjab Government, and it continued to be the same unit throughout, carrying on the same business of supply of electricity at the same place and there was no cesser of that business or any change in the unit. Therefore, it was held that the petitioner-firm was liable to be assessed to tax under the second proviso to Section 10(2)(vii) in respect of depreciation allowed to it right from its inception in 1930. It may be pointed out that there was change in the partnership of the said firm on various dates. The first change was that one of the three partners of the firm, Ealmokand, dropped out and subsequently two new partners were taken in the partnership. R. B. Mohan Lal, a partner of the firm, died subsequently, and his minor son, Mohinder Lal, was given the benefits of the partnership under the guardianship of his mother and a partnership deed was drawn up. In this context it was argued by the counsel for the firm that at the time of the death of R. B. Mohan Lal, the previous partnership deed had no clause that the partnership would continue on the death of a partner and, therefore, it was pleaded that, on his death, there was dissolution of the partnership in view of the provisions of the partnership deed, and by a new partnership deed, wherein Mohinder Lal, son of R. B. Mohan Lal, was brought in as a partner, a new partnership came into existence. This contention was not accepted by the learned judges and was repelled. It was held that irrespective of the fact that there was change in the partners of the firm four times including that on the death of one of its partners, R. B. Mohan Lal, the firm remained the same entity.

10. Similar view was taken by the Allahabad High Court in *R.B. Jessa Ram Fateh Chand Vs. Commissioner of Income Tax*, . In that case a partner of the assessee-firm died on August 1, 1958, during the accounting year, October 24, 1957, to November 11, 1958. After the death of that partner, the business was continued by the remaining 11 partners and a fresh deed of partnership was executed on August 20, 1958. The assessee-firm filed two returns for the relevant assessment year, one for the period from October 24, 1957, to August 1, 1958, and the other from August 1, 1958, to November 11, 1958, claiming losses in both the periods. The Income Tax Officer did not accept the claim of loss for the first period and made an addition of a sum of Rs. 9,305. Both the Appellate Assistant Commissioner and the Appellate Tribunal rejected the assessee's plea that the Income Tax Officer was in error in making two separate assessments for the two periods. On these facts it was held by a Division Bench of the Allahabad High Court that a change occurred in the constitution of the firm within the meaning of Section 26(1) of the Indian Income Tax Act, 1922, and the assessment should have been made on the firm as constituted at the time of

making the assessment. It was held that the Income Tax Act recognises a firm for purposes of assessment as a unit independent of the partners constituting it; it invests the firm with a personality which survives reconstitution. It was further held that where the firm is dissolved, but the business is not discontinued, there being change in the constitution of the firm, assessment has to be made u/s 26(1) and if there be succession to the business, assessment has to be made u/s 26(2) of the Act.

11. From what has been stated above, there is absolutely no doubt left in my mind that keeping in view the facts and circumstances of the case, the provisions of Section 187 of the Income Tax Act are attracted and, therefore, the present case cannot be covered by the provisions of Section 188 of the Act.

12. Before I part with the judgment, the authorities referred to by the learned counsel for the assessee may be referred to.

13. As regards the decision of the Calcutta High Court in MOOLJI SICKA IN RE [NO. 2]., , suffice it to say that the said decision is not at all helpful for the purposes of the present case. The learned judges of the Calcutta High Court were considering the meaning of the words "change in the constitution of a firm" as provided in Section 26(1) of the Income Tax Act, 1922. In that case there was only a change in the apportionment of the shares of the partners and the question before the Bench was whether such a change in the shares of the partners amounted to a change in the constitution of the firm and it was held keeping in view the provisions of the Partnership Act that there was no change in the constitution of the firm within the meaning of Section 26(1) of the Income Tax Act, 1922. It is quite apparent that in enacting the Income Tax Act, 1961, the legislature has specifically provided Sub-section (2) of Section 187 wherein the definition of the words " change in the constitution of a firm " as referred to in Sub-section (1) of Section 187 has been given. In a particular case which answers the description of Sub-section (2) of Section 187, it will be considered to be a change in the constitution of the firm within the meaning of Section 187(1). Therefore, this authority is of no avail to the learned counsel for the assessee.

14. As regards the case Commissioner of Income Tax, West Bengal Vs. A.W. Figgies and Co. and Others, , the same is also not of any relevance to the facts of the present case. In that case a relief was being claimed by the firm u/s 25(4) of the Indian Income Tax Act, 19-22, as, according to the assessee, in spite of the mere changes in the constitution of the firm, the business of the firm, as originally constituted, continued right from its inception till the time it was succeeded by the limited company and that it was the same unit all through, carrying on the same business at the same place and there was cesser of that business or any change in the unit. On these facts, the Appellate Tribunal and the High Court allowed the assessee's claim and this decision of the Appellate Tribunal and the High Court was confirmed by their Lordships of the Supreme Court. That was again a case where on the facts it was held that in spite of the mere change in the constitution of the firm from time to time the firm remained

the same unit all through, and there was no cesser of that business or any change in the unit. I fail to understand as to how this authority can help the learned counsel for the assessee.

15. On similar grounds, the case in Commissioner of Income Tax Vs. Hans Raj and Others, is of no help to the learned counsel for the assessee, as in that case also it was held that the provisions of Section 25(4) of the Indian Income Tax Act, 1922, were not attracted, because none except one of the ingredients of Section 25, Sub-section (4), was satisfied. It was held that the so-called succession in that case was merely a change in the constitution of the firm.

16. The last case relied upon by the learned counsel for the assessee is Commissioner of Income Tax Vs. Kelukutty, which is a decision of the Kerala High Court. In that case also, it was held that a mere change in the personnel of the partners and in their respective shares, without a dissolution of the firm or division of its assets and liabilities, would not be sufficient to bring into being a totally different assessable unit. The findings of the Income Tax Appellate Tribunal were set aside and it was held, that the Tribunal was not correct in holding that the two firms were different and were not to be treated as one firm for the purpose of the Income Tax assessment. No doubt it is true that on the facts of that case there was a provision in the partnership deed that on the death of a partner the firm shall not dissolve, but I fail to understand as to how this will affect the merits of their case, keeping in mind the view we have taken regarding the interpretation of Section 187 of the Income Tax Act, 1961. Therefore, this authority is also of no assistance to the learned counsel for the assessee.

17. For the reasons recorded above, the question referred to this court for opinion is answered in the affirmative and in favour of the revenue, with costs.

Prem Chand Pandi, J.

18. I agree.