
(1979) 10 AHC CK 0054

In the Allahabad High Court

Case No : Income-tax Reference No. 68 of 1977

Gurudeo Prasad Jagannath Prasad

APPELLANT

Vs

Income Tax Officer

RESPONDENT

Date of Decision : 17-10-1979

Acts Referred:

Income Tax Act, 1961 — Section 176(3), 184, 272

Citation : (1981) 131 ITR 486 : (1980) 3 TAXMAN 374

Hon'ble Judges : R.R. Rastogi, J;C.S.P. Singh, J

Bench : Division Bench

Advocate : J.C. Bhardwaj, for the Appellant; R.K. Gulati and A. Gupta, for the Respondent

Judgement

C.S.P. Singh, J.—The Tribunal has referred the following question of law for our opinion :

" Whether, on the facts and in the circumstances of the case, the Tribunal was right in directing the Income Tax Officer to treat the assessee as a registered firm and in making two separate assessments for the two periods in the status of a registered firm ? "

s 2. The assessee was doing business originally under the name and style of M/s. Gurdeo Prasad Jagannath Prasad which consisted of five partners and was constituted under a partnership deed, executed on the 1st of June, 1968. The partners" respective shares were :

(1) Gurdeo Prasad

20%

(2) Jagannath Prasad

25%

(3) Jamuna Prasad

20%

(4) Harihar Prasad

20%

(5) Baijnath Prasad

15%

3. Clause (6) of the partnership deed made provision for the continuance of the firm even in the event of the death of any partner, and provided that on the death of a partner, his heirs, legal assigns or successors-in-interest would ipso facto become a partner in the firm. Clause (7) of the deed of partnership provided for dissolution of the firm by mutual consent or by two months' registered notice by any of the partners to the others. This firm was registered in the year 1969-70 and continued to be assessed as such. On the 30th of September, 1972, two partners, viz., Gurudeo Prasad and Baijnath Prasad, retired from the partnership firm from October 1, 1972. On the retirement of these two partners a deed of dissolution appears to have been executed and a fresh partnership deed was drawn up on 18th October, 1972, with three of the surviving partners. In pursuance of these deeds a declaration u/s 184 in Form No. 12 was filed on September 6, 1973, for continuation of registration for the first period, and an application for registration in Form No. 11 was filed on 2nd December, 1972. The assessee filed two returns in keeping with the two deeds of partnership, one for the period up to 1st October, 1972, and the other for the subsequent period up to March 31, 1973. The ITO, however, held that the old firm continued, as no notice u/s 176(3) for discontinuance of the business was given by the assessee within 15 days, and it was only on 2nd December, 1972, when the new deed of partnership was filed along with an application in Form No. 11 for fresh registration that the ITO was informed of the matter. He took the view that as under Clause (6) of the original deed of partnership, the partners had agreed not to dissolve the firm even in the event of death of one of the partners and, further, that Clause (7) contemplated dissolution only after a notice, which had not been given, the erstwhile firm was not dissolved and all that happened was that there was a change in the constitution of the firm within the meaning of Section 187(2) of the I.T. Act. On this view he made a single assessment on the firm. As respects the registration applied for by the new firm on the basis of the new partnership deed, he found that although in para. (2) of the partnership deed of the 18th October, 1972, Jagannath Prasad, Jamuna Prasad and Harihar Prasad had shares in the ratio of 40%, 30% and 30%, respectively, the profits had been divided in the ratio of 25%, 25% and 25%. On this view the ITO held that no genuine firm had come into existence. The appeal filed by the assessee failed. Thereafter, the matter was taken up before the Tribunal. From the order of the Tribunal it appears that the dissolution deed was fitted before it and the Tribunal has recorded a finding that the dissolution deed was genuine. Taking into account this dissolution deed and the fact that the new

partnership deed had been drawn up later, it held that the earlier firm stood dissolved on 30th September, 1972. As regards the right of the partners to dissolve the partnership without notice it held that they could do so as they had mutually agreed upon such a course. Commenting upon the genuineness of the newly formed firm, it held that a mere mistake in the allocation of shares would not make the firm non-genuine. In consequence of these findings the Tribunal directed the ITO to make two assessments for the two periods in question treating the firm as a registered firm. Counsel for the department urged that inasmuch as no notice u/s 176(3) had been given by the assessee-firm for discontinuance of its business, the Tribunal erred in holding that a dissolution of the firm had taken place. It was also contended that Clauses (6) and (7) of the partnership deed of the 1st June, 1968, indicated that the firm would continue even in the event of the death of one of the partners and could be dissolved only after two months' notice by one of the partners to the others. We do not find any substance in these contentions. The Tribunal has recorded a finding of fact that after the dissolution of the partnership firm a dissolution deed was drawn up and the deed was genuine. It also found that all the partners mutually agreed to such a dissolution. Clauses (6) and (7) of the deed on which counsel for the department placed much reliance are of no avail because the partners had mutually agreed to dissolve the partnership. We need not quote Clause (6), for, that provides for continuance of the firm in the eventuality of death of one of the partners and as in the present case none of the partners has died Clause (6) does not affect the issue. We will extract Clause (7) of the deed which runs as under:

"That the partnership is at will and will be dissolved by mutual consent or by two months' registered notice by any of the parties to the others. "

4. It will be noticed that this provision indicates that the partnership is at will and can be dissolved by mutual consent of the partners. It is only when mutual consent is lacking, that a notice is necessary to dissolve the firm. In the present case as the Tribunal has found that all the partners had mutually consented to the dissolution, no notice was required for effecting the dissolution of the firm. There is also no substance in the contention that as notice of discontinuance u/s 176(3) had not been given by the firm to the ITO the firm should be held to be continuing. Section 176(3) does not set out the consequences of a notice not being given within the time stipulated therein. Thus, if a firm has in fact been dissolved the mere absence of a notice u/s 176(3) cannot lead to the result that the firm would continue for the purposes of the Act. It is also worthwhile pointing out that the only consequence of not giving a notice u/s 176(3) has been set out in Section 272 which provides for the imposition of a fine and this being so we cannot add to this the further consequence of the firm being treated as continuing. As the firm stood dissolved on the 1st of October, 1972, and as respects this period there is no finding that the share in the profits had not been allocated to the partners in accordance with the deed of the 1st June, 1968, the assessment for the period up to 30th September, 1972, had to be made in the

status of a registered firm. Coming now to the latter period, as the earlier firm stood dissolved, a separate assessment had to be made for this period. The question is whether the assessment had to be made in the status of a registered firm or otherwise. The main ground given by the ITO for refusing the registration for this period, apart from the fact that he held that the old firm continued, is that the shares in the profits had been allocated not in proportion to the shares of the partners as set out in the second deed of partnership. From the order refusing registration it does not appear that the assessee tried to explain this anomaly before the ITO. When the matter came up before the Tribunal, the assessee gave an explanation and that was to the effect that the allocation of shares had been made under a mistake which was rectified by passing reverse entries immediately when the mistake was known. The Tribunal has accepted this explanation. It is necessary to mention at this stage that in the reference application filed by the department, the department has sought for a reference of a question as to the justification of the Tribunal in admitting the assessee's contention for the first time in the appeal before it that the mistake in the allocation of shares amongst the partners had been rectified by passing reverse entries. The Tribunal, however, did not make any reference in respect of this question and referred only the question set out. No attempt was thereafter made to get this question referred. Therefore, we have to proceed on the basis that the Tribunal was justified in entertaining the explanation. The question is as to whether in view of this finding it can be held that the firm was not entitled to registration and it could not be treated as a genuine firm, for the reason that the shares were not allocated in accordance with the proportion set out in the partnership deed. Counsel for the department in support of his contention drew our attention to the case of *Setha Ram Dhanvir Singh Vs. Commissioner of Income Tax*, wherein it has been held that where the share of profits had been distributed otherwise than in accordance with the partnership deed, the ITO can cancel the registration of a firm on the ground that it is not genuine. In taking this view, the Bench followed the decision of the Supreme Court in *Khanjan Lal Sewak Ram Vs. Commissioner of Income Tax, U.P.*. In that case, profits earned in the black market had been distributed amongst the partners although they had not been shown in the books. It was held that the firm was not entitled to registration as in such cases the certificate given by the firm that the profits had been distributed in accordance with the partnership deed would be false. The decision in *Setha Ram Dhanvir Singh Vs. Commissioner of Income Tax*, has to be read in the context of the facts of that case. In that case the assessee's explanation that the discrepancy in the allocation of profits of the firm was due to a mistake, had been repelled by the Tribunal on the ground that the explanation was an after-thought. In the present case this is not so. The assessee's explanation that the error in the allocation of profits was due to a mistake and was corrected as soon as it was discovered has been accepted by the Tribunal. In such a situation, the decision of this court in the case of *Commissioner of Income Tax Vs. Hari Ram Khanna*, applies. There it was held that registration cannot be refused or cancelled on the ground of improper allocation if it had been made

due to an omission or inadvertence or mistake. In the present case this is precisely what the Tribunal has found. The Tribunal was, thus, right in directing the ITO to make two assessments in the status of a registered firm.

5. We, accordingly, answer this question in the affirmative, in favour of the assessee and against the department. In the circumstances, there will be no order as to costs.