

(1971) 05 AHC CK 0031

In the Allahabad High Court

Case No : Civil Miscellaneous Writ No's. 341 and 1425 of 1969

Pt. Deo Sharma

APPELLANT

Vs

Income Tax Officer, B-Ward

RESPONDENT

Date of Decision : 13-05-1971

Acts Referred:

Income Tax Act, 1922 — Section 26, 44

Income Tax Act, 1961 — Section 147, 148, 149, 150, 153

Citation : (1972) 84 ITR 633

Hon'ble Judges : R.S. Pathak, J;H.N. Seth, J

Bench : Division Bench

Advocate : K.L. Misra and R.K. Gulati, for the Appellant; B.L. Gupta and R.R. Misra, for the Respondent

Final Decision : Allowed

Judgement

H.N. Seth, J.—On 3rd of December, 1968, the Income Tax Officer, Kanpur, issued two notices u/s 148 of the Income Tax Act, 1961, to the petitioner, Deo Sharma, stating that he had reasons to believe that the petitioner's income chargeable to tax for the assessment years 1948-49 and 1949-50 had escaped assessment within the meaning of Section 147 of the Act, and requiring the petitioner to file returns for the two years.

2. By Writ Petition No. 341 of 1959 the petitioner has challenged the notice issued for the assessment year 1948-49, whereas in Writ Petition No. 1425 of 1969 he has questioned the validity of the notice issued in respect of assessment year 1949-50. As both these petitions are based on identical facts, it will be convenient to deal with them together.

3. The facts leading to the two notices which are not in controversy are as follows : With effect from January 1, 1946, a partnership firm, M/s. Sharma & Co., became the sole selling agent of M/s. Cawnpore Cotton Mills Ltd. The firm, Sharma & Co., consisted of two partners, namely, Sri Sheo Nath Sharma and Smt. Chandan Devi, wife of the petitioner. This firm was dissolved on 31st

December, 1947, and with effect from 1st January, 1948, the petitioner, Sri Deo Sharma, took over as the sole selling agent of Cawnpore Cotton Mills Ltd. Subsequently, Sheo Nath Sharma also joined him as a partner. This newly constituted firm was also known as Sharma & Co. The agreement further provided that this new firm was to operate retrospectively with effect from January 1, 1948.

4. In respect of the assessment year 1947-48, the old Sharma & Co. made an application for registration u/s 26A of the Indian Income Tax Act, 1922. The Income Tax Officer rejected this application on the finding that the partners disclosed by the deed were not the real partners, the real partners of the firm being the petitioner, Deo Sharma (instead of Smt. Chandan Devi), and Sri Sheo Nath Sharma. Though the old firm, Sharma & Co., was not registered, the Income Tax Officer proceeded to assess this firm as a registered firm as provided in Section 23(5) of the Act. He determined the share income of the petitioner at Rs. 38,533 and included this amount in his individual assessment.

5. The petitioner claimed that as he was not a partner in the firm, Sharma & Co., the Income Tax Officer could not include any portion of the income of Sharma & Co. in his income. He also claimed that any assessment made against him in respect of the assessment of Sharma & Co. without notice to him was invalid. The pleas raised by the petitioner did not find favour with the Income Tax authorities. The matter was referred to the High Court, which on May 20, 1960, held that even if the petitioner's wife was a partner in the firm as his benami, and the petitioner was the real owner of her share of profits, he did not become a partner in the firm for the purposes of the Partnership Act. In proceedings u/s 23(5), allocation of the income of a firm had to be made between the partners and then the income of each partner had to be taken into account in the assessment of that partner. The proceedings u/s 23(5) should have stopped at that stage of allocation. The further order passed in those very same proceedings that the income allocated to the share of the petitioner's wife would be added in the petitioner's income was beyond the jurisdiction exercisable in those proceedings and the order being without jurisdiction could not attract the provisions of the proviso to Section 30(1) and be binding on the petitioner and bar him from contending that the income was not to be taxed in his hands. The fact that the partner happened to be the petitioner's wife, by itself, could not take away his right to be heard. The decision of the High Court has since been reported in PT. DEO SHARMA Vs. COMMISSIONER OF Income Tax, U. P. AND V. P., . Thereafter, the matter went back to the Income Tax Officer through the Tribunal and is still pending.

6. In the meantime assessment had been made against the old Sharma & Co. for the assessment years 1948-49 and 1949-50 in the years 1953 and 1957, respectively (relevant accounting periods being May 3, 1946, to June 20, 1947, and June 21, 1947, to December 31, 1947). The assessee contended that as the firm, Sharma & Co., had dissolved on 31st December, 1947, it ceased to exist as

a unit and no assessment could be made on it.

7. This contention was rejected up to the stage of the Appellate Tribunal, which held that the assessee's business had not been discontinued, certain changes had merely taken place in the constitution of the firm and that the firm as a unit of assessment had continued throughout. Relying upon Section 26(1) of the Act, it upheld the assessment. The matter was ultimately referred to the High Court (LT.Rs. Nos. 738 and 739 of 1962) which by its order dated 20th May, 1964, held that the old Sharma & Co. dissolved on 31st December, 1947, and thereafter the entire business was taken over by the petitioner, Deo Sharma. In the circumstances, the provisions of Section 44 of the Act could not be invoked. This court further expressed an opinion that Section 26(2) of the Act merely provided for apportionment of the tax liability between the original owner of the business and his successor. It did not provide for any procedure for assessment of cases falling within the section. In the result it held that the assessment made against Sharma & Co. after 31st December, 1947, was invalid. On receipt of the finding of the High Court the Income Tax Appellate Tribunal made an order dated 18th December, 1964, directing that the assessment made against Sharma & Co., after dissolution of the firm, was not valid and that it be set aside.

8. On 30th March, 1965, the Income Tax Officer issued notices u/s 148 of the Act to the new Sharma & Co., consisting of the petitioner and his brother, Sheo Nath Sharma, as the successor to the old Sharma & Co. which consisted of Sheo Nath Sharma and Smt. Chandan Devi in respect of the income for the assessment years 1948-49 and 1949-50. The new Sharma & Co. filed Writ Petitions Nos. 1463 and 1464 of 1965, contending that the Income Tax Officer had no jurisdiction to proceed against the new Sharma & Co. The writ petitions were allowed by this court by an order dated 21st April, 1966, holding that the new Sharma & Co. was not the successor of the old Sharma & Co., inasmuch as the business of the old Sharma & Co. did not directly devolve upon the new Sharma & Co. The assessment proceedings against the new Sharma & Co. were accordingly quashed.

9. The Income Tax Officer, thereafter, made fresh attempts for realising the dues of the old Sharma & Co. by issuing the impugned notices in respect of the assessment years 1948-49 and 1949-50 to the petitioner, Deo Sharma as, according to the decision of this court in Writ Petitions Nos. 1463 and 1464 of 1965, Deo Sharma was the real successor of the old Sharma & Co.

10. The petitioner has challenged the validity of these two notices, inter alia, upon the ground that they are barred by time as provided in Section 149 of the Act.

11. Section 149 Of the Act runs as follows:

"(1) No notice u/s 148 shall be issued,--

(a) in cases falling under Clause (a) of Section 147--

(i) for the relevant assessment year, if eight years have elapsed from the end of that year, unless the case falls under Sub-clause (ii);

(ii) for the relevant assessment year, where eight years, but not more than sixteen years, have elapsed from the end of that year, unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to rupees fifty thousand or more for that year ;

(b) in cases falling under Clause (b) of Section 147, at any time after the expiry of four years from the end of the relevant assessment year.

(2) The provisions of Sub-section (1) as to the issue of notice shall be subject to the provisions of Section 151.

(3) If the person on whom a notice u/s 148 is to be served is a person treated as the agent of a non-resident u/s 163 and the assessment, reassessment or recomputation to be made in pursuance of the notice is to be made on him as the agent of such non-resident, the notice shall not be issued after the expiry of a period of two years from the end of the relevant assessment year."

12. It will thus be seen that depending upon the amount of income that is said to have escaped assessment, a notice in a case falling u/s 147(a) can be issued up to the maximum period of 16 years after the end of the assessment year, the income of which is said to have escaped assessment. In cases falling u/s 147(b) of the Act the maximum period up to which a notice u/s 148 can be issued is four years from the end of the relevant assessment year. In this case the two notices have been issued for the assessment years 1948-49 and 1949-50. According to this section, a notice in respect of the assessment year 1948-49, could in no case be issued after the year 1965. Similarly, in respect of the assessment year 1949-50 it could not be issued after the year 1966. The notices in respect of the two years having been issued on 3rd of December, 1968, are prima facie barred by time.

13. Learned counsel for the revenue, however, contended that according to Section 150 of the Income Tax Act, a notice u/s 148 of the Act may be issued at any time notwithstanding the maximum period prescribed for the same in Section 149 of the Act, if it is issued for the purposes of making an assessment or reassessment or recomputation in consequence of or to give effect to any finding or direction contained in an order passed by any authority in any proceeding under this Act by way of appeal, reference or revision. He contended that in ITR No. 738 of 1962 connected with ITR No. 739 of 1962 (Sharma & Co. v. Commissioner of income tax), the High Court by its order dated 20th of May, 1964, held as follows :

" In the instant case the partnership was dissolved on December 31, 1947, and, thereafter, the entire business was taken over by Pt. Deo Sharma as sole proprietor thereof. It cannot be said that when he took over the business from January I, 1948, there was a mere change in the constitution of the assessee or

that a firm was newly constituted. It is true that some time after carrying on the business as sole proprietor, Pt. Deo Sharma entered into a partnership agreement with Deo Nath Sharma, and one of the stipulations in that agreement was that the partnership would be deemed to have commenced on January 1, 1948. Now, merely because the parties to a partnership agreement agree that the partnership will be deemed to have come into existence retrospectively does not, so far as third parties are concerned, entitle a plea to be raised that the partnership must indeed be said to have commenced on a date before it was entered into."

14. Learned counsel contends that this finding recorded by the High Court, in these references, clearly implied that the petitioner succeeded to the business of old Sharma & Co., on January 1, 1948, and as such he was liable to be assessed as successor to Sharma & Co. The notices were, therefore, issued to the petitioner in consequence of and in order to give effect to the finding recorded by the High Court in a reference under the Act and, therefore, as provided in Section 150 of the Act, the period of limitation for giving notice as mentioned in Section 149 did not apply.

15. In the instant case the stand taken by the revenue is that the notices in respect of assessment years 1948-49 and 1949-50 have been issued to the petitioner as successor to the old Sharma & Co., which was dissolved on December 31, 1947. Proceedings u/s 147(b) read with Section 150(i) were initiated against the petitioner as for the assessment year 1948-49 an income of Rs. 3,64,957 and for the assessment year 1949-50 an income of Rs. 1,55,328 had escaped assessment. It is not disputed that these two amounts represented the income of the old Sharma & Co., earned during the relevant accounting year, prior to its dissolution on December 31, 1947. Two questions, therefore, that arise for consideration are:

"(1) Whether it is open to the Income Tax authorities to tax the petitioner in respect of the income earned by old Sharma & Co., to whose business he succeeded ? and

(2) Whether there is no time limit for issuing the two notices as they had been issued in consequence of and in order to give effect to the finding recorded by the High Court in I.T.Rs. Nos. 738/62 and 739/62. (1) Since reported in [1965] 57 ITR 872 (All.).

16. Learned counsel for the revenue cited Section 44 of the Act in this connection. Section 44 of the Income Tax Act, 1922, as it stands after its amendment in the year 1958, provides that where any business, profession or vocation carried on by a firm or other association of persons has been discontinued or where a firm or other association of persons is dissolved, the Income Tax Officer is to make an assessment of the total income of the firm or other association of persons as such as if no discontinuance or dissolution had taken place. This section further provides that every person who was, at the time

of such discontinuance or dissolution, a partner of the firm or a member of the association, as the case may be, shall be jointly and severally liable for the amount of tax or penalty payable, and all the provisions of Chapter IV, so far as may be, shall apply to any such assessment or imposition of penalty. According to this section, it is the persons who were partners of that firm at the time of its dissolution who would be liable to pay the tax. The section indicates that the liability of the firm for payment of Income Tax on the income earned by it up to the date of its dissolution does not pass on to the successor, but continues to be that of the firm and the partners.

17. Reliance was then placed on Section 26 of the Act. According to this section, if a person carrying on a business, profession or vocation has been succeeded in such capacity by any person, such person and such other person shall, subject to the provisions of Sub-section (4) of Section 25, each be assessed in respect of the actual share, if any, of the income, profits and gains of the previous year. It will thus be seen that, normally, a person succeeding to a business as such is not liable for payment of, Income Tax in respect of the income derived by the person who has been succeeded. This section requires a separate assessment to be made on the person succeeded and the person succeeding, in respect of their actual share of the income, profits and gains of the previous year. The person succeeding does not come into the picture at all in respect of the income of the years earlier than the year in which the succession took place. So far as the year in which the succession took place is concerned, the income will have to be apportioned and the person succeeded and succeeding are to be assessed on the share of income earned by each of them. It is thus clear that there was no liability on Sri Deo Sharma in respect of the income earned by old Sharma & Co. up to 31st December, 1947, the date of its dissolution. The only exception to the general rule mentioned above, contemplated by this section, is when the person whose business, profession or vocation is succeeded cannot be found. In such a case the assessment of the profits of the year in which the succession took place up to the date of the succession, and for the year preceding that year is to be made on the person succeeding him in the like manner and to the same amount as it would have been made on the person succeeded or when the tax in respect of the assessment made for either of such years assessed on the person succeeded cannot be recovered from him, it shall be payable by and be recoverable from the person succeeding, and such person shall be entitled to recover from the person succeeded the amount of any tax so paid.

18. In the case before us there is no allegation that the partners of the old Sharma & Co. are not available for the purposes of assessment and recovery of tax in respect of the business carried on by the firm till 31st December, 1947, the date on which it was dissolved. In the circumstances, it is not possible to take any proceeding against the petitioner who was not a partner in the old Sharma & Co. in respect of the income that had accrued to the old Sharma & Co. up to the date of its dissolution.

19. It may be noticed that in the references decided by this court on 20th May, 1964, the only finding recorded was that the petitioner succeeded to the old Sharma & Co. This court did not record a finding that the petitioner was in any way liable to be assessed in respect of the income earned by the old Sharma & Co., up to the date of its dissolution on 31st December, 1947. As mentioned above neither Section 26 nor Section 44 of the Act authorise the Income Tax Officer to take proceedings against the petitioner in respect of that income. In the circumstances, it cannot be said that the two notices, the validity of which has been impugned in these petitions, were issued in order to give effect to or in consequence of any finding or direction issued by the High Court in Income Tax References Nos. 738 and 739 of 1962.

20. In this connection learned counsel for the revenue also relied upon Explanation III to Section 153 of the Act. However, in our opinion, the revenue cannot derive any support from it. Explanation III provides that where by an order u/s 250, 254, 260, 262, 263 or 264 any income is excluded from the total income of one person and is held to be the income of another person, then, an assessment of such income on such other person shall, for the purposes of Section 150 and Section 153, be deemed to be one made in consequence of or to give effect to any finding or direction contained in the said order provided such other person was given an opportunity of being heard before the said order was passed. In the first place, by its order dated 20th May, 1964, made in the References Nos. 738/62 and 739/62 this court merely decided that the petitioner succeeded to the business that was being carried on by the old Sharma & Co. on January 1, 1948. This finding cannot be construed as a decision holding that any part of the income in respect of which the two notices have been issued was not the income of old Sharma & Co., and that it was the income of the assessee. As mentioned above, the provisions of Section 26 and Section 44 of the Act (1) Sharma and Co. Vs. Commissioner of Income Tax, . make it absolutely clear that the income in respect of which the notices have been issued was not to be included in the income of the successor to the old Sharma & Co. In the second place, for the purposes of Section 150, the notice could be deemed to be issued in consequence of or to give effect to a finding or direction by which the income had been excluded from the income of old Sharma & Co., and was held to be the income of the assessee, only if the assessee had been given an opportunity of being heard before the order was made. The assessee was not a party to the Income Tax References Nos 738 and 739 of 1962 and the revenue has not taken up the case that he was given any opportunity of being heard before the High Court made the observation on which reliance is being placed. Even if by some stretch of imagination it could be said that in these references, the High Court had recorded a finding that income for the assessment years 1948-49 and 1949-50 had to be excluded from the total income of old Sharma & Co., and was to be included in the income of the assessee (which finding is not there at all), the revenue could still not have derived any benefit from Explanation III to Section 153 as that finding was not recorded after giving an opportunity to the

petitioner to be heard. As the notices had not been issued in order to give effect to a finding or direction contained in an order passed by any authority in any proceeding under the Act by way of appeal, reference or revision, the revenue cannot claim that the limitation as provided in Section 149 of the Act is not applicable in view of the provisions of Section 150 of the Act.

21. In this view of the matter the two notices issued to the petitioner much beyond the time limit prescribed by Section 149 of the Act are wholly without jurisdiction and are liable to be quashed. The petitioner also raised a question about the validity of Section 150 of the Act, but in the view which we have taken it is not necessary to go into that question.

22. In the result, we allow both the writ petitions with costs and quash the two notices dated 3rd December, 1968, issued by the Income Tax Officer to the petitioner u/s 148 of the Act in respect of the assessment years 1948-49 and 1949-50.