
(2006) 08 KAR CK 0067

In the Karnataka High Court

Case No : IT Reference No. 21 of 1999 4 August 2006 A.Y. 1993-94

Suvaradhan

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 04-08-2006

Acts Referred:

Income Tax Act, 1961 — Section 2 (47), 45 (4)

Citation : (2006) 156 TAXMAN 229

Hon'ble Judges : R. Gururajan, J;Jawad Rahim, J;Gururajan, J

Bench : Full Bench

Advocate : S. Parthasarathi, for the Petitioner M.V. Seshachala,, for the appearing parties;

Judgement

Gururajan, J.

M/s. Suvaradhan of Bangalore is before us seeking an opinion in the light of the order of the Tribunal in ITA No. 405 /Bang/ 1997, dated 22-12-1997.

2. The assessee is a registered firm which came into existence by way of partnership deed dated 23-7-1986. Partnership consists of three persons. On 1-7-1998 one of the partners retired and the other two continued the partnership in terms of partnership deed dated 17-10-1988. Survey was conducted in the business premises of the assessee. It came to light that the firm had been dissolved and the business had been taken over by one of the partners Smt. Anuradha Maruthi Gokarn. It was also noticed that the partnership was dissolved on 1-4-1992 and the assets and liabilities had been taken over by the said lady. The assessing officer proposed to apply section 45(4) of the Act. Notice was issued. Assessee filed a Nil return. Thereafter, the assessing officer concluded the assessment u/s 144 of the Act charging capital gain in the hands of the firm in respect of the assets transferred by the firm. An appeal was filed. Appeal stood dismissed. Matter was taken to the Tribunal. Tribunal rejected the appeal. Thereafter, at the instance of the assessee, Tribunal has chosen to refer the following questions of law for our consideration:

"Whether, on the facts and in the circumstances of the case, the Tribunal was justified in coming to the conclusion that the assessee-firm was liable to capital gains u/s 45(4) on the ground that there was transfer or distribution of capital assets on the dissolution of the partnership firm?"

3. Heard Sri Parthasarathi, learned counsel appearing for the appellant. He would invite my attention to section 45(4) of the Income Tax Act to contend that the orders of the Tribunal requires our consideration. He would also refer to section 2(47) for the definition of "transfer" in the case on hand. He wants both the provisions to be read together for the purpose of "no transfer" in the case on hand. He would also rely on number of judgments in support of his submission. Per contra, Sri M.V. Seshachala, learned counsel for the department would support the order.

4. After hearing, we have carefully gone through the material placed on record.

5. As we mentioned earlier, it is seen that the partnership stood dissolved on 1-4-1992. Nil return was filed. Same was not accepted by the assessing officer. Assessment Officer notices in his order the dissolution deed and also of taking over of assets and liabilities at book value as on 1-4-1992. He also noticed clause 3 of the Dissolution Deed in his order. After noticing the same, he comes to the conclusion that it is incorrect to say that there is no distribution of assets in terms of Income Tax laws. It is in these circumstances that he has chosen to consider section 45(4) of the Income Tax Act for the purpose of levy of tax. When this was challenged, the appellate authority noticed the definition of transfer u/s 2(47). After noticing, the appellate authority states that it is inclusive definition. Thereafter, the appellate authority would hold that the assessing authority is right in the matter. He would come to the conclusion that this is a case of transfer by way of distribution of capital assets on dissolution of the firm in terms of section 45(4) of the Act, and that the profits or gains therefrom is chargeable to tax. When this was challenged, the Appellate Tribunal, after noticing section 45(4) and the definition of transfer, has come to the conclusion that the authorities are right in rejecting the case of the assessee.

6. The admitted facts would reveal of dissolution of the firm. In terms of the dissolution deed, the retiring partner would be entitled to be paid balance standing to his credit as on 31-3-1992 together with profit up to that date in one or more instalments. The dissolution deed also would show that the retiring partner has no objection whatsoever in the assessee continuing its business in the same name either as sole proprietrix in any other manner as she may think fit. The authorities, after noticing the same, have come to the conclusion that there is transfer in the case on hand. Assessee in terms of the materials placed on record has taken over the entire assets and liabilities of the partnership firm, as rightly ruled by the authorities.

7. Section 45(4) of the Income Tax Act, 1961 reads as under:

"(4) The profits or gains arising from the transfer of a capital asset by way of

distribution of capital assets on the dissolution of a firm or other association of persons or body of individuals (not being a company or a co-operative society) or otherwise, shall be chargeable to tax as the income of the firm, association or body, of the previous year in which the said transfer takes place and, for the purposes of section 48, the fair market value of the asset on the date of such transfer shall be deemed to be the full value of the consideration received or accruing as a result of the transfer."

A reading of the said provision would show that the profits or gains arising from transfer of capital assets by way of distribution of capital assets on dissolution of a firm shall be chargeable to tax as income of the firm in the light of transfer that has taken place. Transfer has been defined u/s 2(47) of the Act. What is contended before us that if section 2(47) read with section 45(4), there is no transfer at all, and if there is any transfer, it is not by the assessee but by the retiring partner. Therefore, according to Sri Parthasarathi, orders are bad in law. To consider this aspect of the matter, we have to notice section 47 of the Income Tax Act. Section 47 is a special provision which would say as to which are the transactions not regarded as transfer. A reading of the said section 47 of the Act would show that several transactions were considered as no transfer for the purpose of section 45 of the Act. Prior to amendment section 47(2) read as under:

"(2) any distribution of capital assets on the dissolution of a firm, body of individuals or other association of persons."

This was omitted by the Finance Act, 1987 with effect from 1-4-1988. Therefore, in our view, any transaction resulting in distribution on dissolution of a firm has to be considered as "transfer" in terms of section 47. In the light of omission of clause (it) of section 47 prior to 1-4-1988, it cannot be said that section 45 is inapplicable to the facts in the case on hand as argued by Sri Parthasarathi.

8. Sri Parthasarathi, learned counsel, however, would rely on a judgment of Madhya Pradesh High Court in Commissioner of Income Tax Vs. Moped and Machines, . In the said judgment, there is no reference to omission of clause (it) of section 47 as it stood prior to 1-4-1988. In the said judgment what was considered was section 45(4) and section 2(47), as it stood then. Therefore, the said judgment would not be applicable to the issue involved in the case on hand. On the other hand, as rightly pointed out by Sri Seshachala, learned counsel for the department, a similar question was considered by the Bombay High Court in the case of Commissioner of Income Tax Vs. A.N. Naik Associates and Another and Rangavi Realtors and Another, . In the said judgment, Bombay High Court has noticed the effect of Act of 1987. After noticing, the Bombay High Court has ruled that section 45 of the Income Tax Act is a charging section. Bombay High Court further ruled that :

".. . . From a reading of sub-section (4) to attract capital gains tax what would be required would be as under: (1) transfer of capital asset by way of distribution

of capital assets: (a) on account of dissolution of a firm; (b) or other association of persons; (c) or body of individuals; (a) or otherwise; the gains shall be chargeable to tax as the income of the firm, association or body of persons. The expression "otherwise" has to be read with the words "transfer of capital assets". If so read, it becomes clear that even when a firm is in existence and there is a transfer of capital assets it comes within the expression "otherwise". The word "otherwise" takes into its sweep not only cases of dissolution but also cases of subsisting partners of a partnership, transferring assets to a retiring partner (p. 347)

Bombay High Court has noticed section 2(47) and thereafter ruled reading as under:

". . . The Finance Act, 1987, with effect from 1-4-1988, omitted this clause, instead of amending section 2(47), the effect of which is that distribution of capital assets on the dissolution of a firm would be regarded as transfer... ." (p. 347)

9. We are in respectful agreement with the judgment of the Bombay High Court. When the Parliament in its wisdom has chosen to remove a provision, which provided "no transfer", there is no need for any further amendment to section 2(47) of the Act as argued before us. In our view, despite no amendment to section 2(47), in the light of removal of clause (ii) to section 47, transaction certainly would call for tax at the hands of the authorities.

10. In the circumstances, we deem it proper to answer the question under reference in favour of the revenue and against the assessee. Ordered accordingly. No costs.