

(1991) 03 AHC CK 0008

In the Allahabad High Court

Case No : Income-tax Reference No. 117 of 1979

TARUN BHAI

APPELLANT

Vs

COMMISSIONER OF Income Tax.

RESPONDENT

Date of Decision : 07-03-1991

Acts Referred:

COMPANIES ACT, 1956 — Section 617
Income Tax Act, 1961 — Section 154, 155, 2, 256, 261

Citation : (1992) 100 CTR 179 : (1992) 193 ITR 543

Hon'ble Judges : B. P. Jeevan Reddy, C.J.; B. P. Jeevan Reddy C. J., J

Bench : Division Bench

Judgement

B. P. JEEVAN REDDY C. J. - u/s 256(1) of the Income Tax Act, 1961, the Tribunal has stated the following question for the opinion of this court :

"Whether, on the facts and circumstances of the case, the Appellate Tribunal was justified in holding that conversion of the assessee's proprietary business into a partnership amounted to a transfer of the assets of the proprietary business to the partnership and, in that view, holding that the development rebate on plant and machinery of the proprietary business transferred to the partnership within eight years was wrongly allowed within the meaning of clause (b) of sub-section (3) of section 34 of the Income Tax Act, 1961, which could be withdrawn u/s 155(5) of the Income Tax Act, 1961 ?"

The assessee is an individual. During the accounting year relevant to the assessment years 1965-66, 1969-70, 1970-71 and 1971-72, he was carrying on the business of printing and publication as proprietary business up to May 31, 1972. On the plant and machinery employed in the said business, he claimed development rebate during the said year which was granted to him. The said proprietary business was converted into a partnership business on and with effect from April 1, 1972. The partnership consisted of the petitioner and his two sons wherein the assessee's share was 1/3rd. The Income Tax Officer held that inasmuch as there was a transfer of the said plant and machinery within a period

of eight years, the assessee became disentitled to the said rebate and, accordingly, revoked the said benefit by passing orders u/s 155(5) of the Income Tax Act. The Income Tax Officer was of the view that there was a transfer of the said assets on the formation of the partnership. This view was questioned in appeal by the assessee but without success. Then the matter was taken to the Tribunal which too disagreed with him and dismissed the appeal.

Section 33 of the Income Tax Act provides for development rebate. Sub-section (3) of section 34 provides that the development rebate provided u/s 33 shall not be allowed unless an amount equal to 75% of the development rebate actually allowed is debited to the profit and loss account of the previous year in respect of which the said deduction is allowed and credited to a reserve account. This reserve has to be maintained for a period of eight years. Clause (b) of sub-section (3) of section 34 further provides that :

"If any ship, machinery or plant is sold or otherwise transferred by the assessee to any person at any time before the expiry of eight years from the end of the previous year in which it was acquired or installed, any allowance made u/s 33 or under the corresponding provisions of the Indian Income Tax Act, 1922 (11 of 1922), in respect of that ship, machinery or plant shall be deemed to have been wrongly made for the purposes of this Act, and the provisions of sub-section (5) of section 155 shall apply accordingly."

Sub-section (5) of section 155 provides precisely for such a situation. Sub-section (5) reads as under :

"Where an allowance by way of development rebate has been made wholly or partly to an assessee in respect of a ship, machinery or plant installed after the 31st day of December, 1957, in any assessment year u/s 33 or under the corresponding provisions of the Indian Income Tax Act, 1922 (11 of 1922), and subsequently -

(i) at any time before the expiry of eight years from the end of the previous year in which the ship was acquired or the machinery or plant was installed, the ship, machinery or plant is sold or otherwise transferred by the assessee to any person other than the Government, a local authority, a corporation established by a Central, State or Provincial Act or a Government company as defined in section 617 of the Companies Act, 1956 (1 of 1956), or in connection with any amalgamation or succession referred to in sub-section (3) or sub-section (4) of section 33; or

(ii) at any time before the expiry of the eight years referred to in sub-section (3) of section 34, the assessee utilises the amount credited to the reserve account under clause (a) of that sub-section -

(a) for distribution by way of dividends or profits; or

(b) for remittance outside India as profits or for the creation of any asset outside India; or

(c) for any other purpose which is not a purpose of the business of the undertaking;

the development rebate originally allowed shall be deemed to have been wrongly allowed, and the Income Tax Officer may, notwithstanding anything contained in this Act, recompute the total income of the assessee for the relevant previous year and make the necessary amendment; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the previous year in which the sale or transfer took place or the money was utilised."

The question that arises for our consideration is where a person places his personal individual assets in a partnership of which he is a partner, whether it amounts to a transfer of those assets within the meaning of section 34(3)(b). This very question had arisen before the Karnataka High Court in *Addl. Commissioner of Income Tax, Mysore Vs. M.A.J. Vasanaik*, . It was held that, on the conversion of the property of an individual into property of a firm of which he is a partner, there is a transfer of interest of the individual to the partnership and section 34(3)(b) of the Act is attracted, where the development rebate had been allowed in respect of the assets which pass to the partnership. This decision has been expressly approved by the Supreme Court in *Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat*, though this was a case arising u/s 45 of the Income Tax Act. The Supreme Court considered the question now arising before us elaborately. It took note of the several decisions of High Courts and the Supreme Court on the subject and held that (at p. 520)" when the assessee brought the shares of the limited companies into the partnership firm as his contribution to its capital, there was a transfer of a capital asset within the meaning of the terms of section 45 of the Income Tax Act. In this view of the matter, we agree with the conclusion reached by the Kerala High Court in *Abdul Rahim (A.), A. Abdul Rahim, Travancore Confectionery Works Vs. Commissioner of Income Tax*, , the Karnataka High Court in *Addl. Commissioner of Income Tax, Mysore Vs. M.A.J. Vasanaik*, and by the Gujarat High Court in the judgment under appeal."

It is true that, prior to the decision of the Supreme Court in *Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat*, , several High Courts had taken the view that, in such a situation, no transfer was involved. They have, however, reversed their opinion after the decision of the Supreme Court. We may give an illustration; a Division Bench of the Andhra Pradesh High Court took the view, prior to the decision of the Supreme Court in *Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat*, , that no transfer was involved in such a case, vide *Commissioner of Income Tax, Andhra Pradesh Vs. S. Krishna Rao*, . But that very court has taken a contrary view in *Commissioner of Income Tax Vs. Suresh Chandra Jain*, , mainly on the basis of the decision of the Supreme Court in *Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat*, . It explained that its earlier decision was rendered prior to

the decision of the Supreme Court, but that in the light of the said decision, that view can no longer be taken. The subsequent decision of the Andhra Pradesh High Court in Commissioner of Income Tax Vs. Suresh Chandra Jain, elaborately considers the entire case law on the subject. We are in respectful agreement with the said view.

Learned counsel for the assessee, Sri Saran Behari Lal Srivastava, relied strongly upon the decision of the Supreme Court in Malabar Fisheries Co. Vs. Commissioner of Income Tax, Kerala, , but that was a case which dealt with a different situation altogether. There, a partnership firm owned certain plant and machinery in respect of which it claimed and obtained development rebate. The partnership firm was dissolved within eight years of the creation of the reserve and the said plant and machinery fell to the share of one of the partners. The Department took the view that there was a transfer of the said plant and machinery within the meaning of section 34(3)(b) of the Act and, accordingly, revoked the said benefit by passing an order u/s 155(5) of the Act. The Supreme Court held that, in such a situation, no transfer was involved. It held that, in all such cases, dissolution of the firm precedes the distribution of assets amongst the partners. Once dissolution takes place, it was explained, the firm comes to an end and the distribution of the assets amongst the partners thereafter does not amount to a transfer. It is relevant to notice that the aforesaid decision of the Karnataka High Court in Addl. Commissioner of Income Tax, Mysore Vs. M.A.J. Vasanaik, was brought to the notice of the court but it was distinguished on facts. The following observations in the judgment are relevant (p. 60 of 120 ITR) :

"Counsel for the Revenue referred us to a decision of the Karnataka High Court in Addl. Commissioner of Income Tax, Mysore Vs. M.A.J. Vasanaik, where that court has taken the view that when individual assets are brought into a partnership firm so as to constitute the partnership property, there is a transfer of interest of the individual to the partnership and sections 34(3)(b) and 155(5) of the 1961 Act are attracted. In the first instance, that decision dealt with the converse case and it does not necessarily follow on a parity of reasoning that the distribution, division or allotment of partnership assets to the partners of a firm upon its dissolution would amount to a transfer of assets as was sought to be contended by counsel for the Revenue. Secondly, it is unnecessary for us to express any opinion on the correctness or otherwise of the view taken by the Karnataka High Court in that case."

It is thus clear that not only the Supreme Court declined to express any opinion on the correctness or otherwise of the Karnataka High Court decision in Addl. Commissioner of Income Tax, Mysore Vs. M.A.J. Vasanaik, , but also it took pains to point out that the transfer of assets of an individual to a partnership of which he is a partner stands on a different footing from a case where the assets are distributed amongst the erstwhile partners following the dissolution. Be that as it may, since the Supreme Court has expressly approved the decision of the

Karnataka High Court in Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat, , we have no option but to follow it.

In this view of the matter, we do not think it necessary to refer to the several cases cited by learned counsel for the assessee, which take the view similar to the one in Commissioner of Income Tax, Andhra Pradesh Vs. S. Krishna Rao, . It would serve no purpose to refer to all of them in view of the decision of the Supreme Court in Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat, .

Lastly, learned counsel relies upon the following passage in the Commentary on the Income Tax Act, by Kanga and Palkhivala in support of his contention. The passage occurs at page 100 of Volume I of Eighth Edition, which deals with the definition of the expression "transfer" occurring in clause (47) of section 2. The passage reads :

"This clause defines the word transfer only in relation to a capital asset and has no bearing on the meaning of that word in any section where it is not used in relation to a capital asset. The expression capital asset is used in the provisions dealing with the head of capital gains, and therefore, this definition is relevant for the purposes of that head. The implications of this definition are dealt with post under sections 45 and 47 which deal with capital gains."

We are unable to see how the above passage advances the case of the petitioner. Indubitably, the plant and machinery which was transferred by the assessee to the partnership do constitute capital assets.

For the above reasons, the question referred is answered in the affirmative, i.e., in favour of the Revenue and against the assessee. No order as to costs.

Learned counsel for the assessee makes an oral request for certifying this case to be a fit one for appeal to the Supreme Court u/s 261 of the Act. It is also brought to our notice that the Andhra Pradesh High Court has granted leave to appeal against its judgment in Commissioner of Income Tax Vs. Suresh Chandra Jain, . In our opinion, this is a fit case for being certified as fit for appeal to the Supreme Court u/s 261 of the Act. A certificate shall, accordingly, issue.