Popular Engineering Co. Vs. Commissioner of Income-tax

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Court : Madhya Pradesh

Decided On : Nov-12-1981

Reported in : [1983]140ITR398(MP)

Judge : S.S. Sharma and ;K.N. Shukla, JJ.

Acts : Income Tax Act, 1961 - Sections 41(2), 254, 254(1), 254(2), 254(4), 256, 256(1) and 263(1)

Appeal No. : Miscellaneous Civil Case No. 250 of 1980

Appellant : Popular Engineering Co.

Respondent : Commissioner of Income-tax

Advocate for Def. : R.C. Mukati, Adv.

Advocate for Pet/Ap. : G.K. Puranik, Adv.

Judgement :

Shukla, J.

1. This is a reference under Section 256(1) of the I.T. Act, 1961, by the Income-tax Appellate Tribunal, Indore, stating the case and referring the same to us for opinion on the following questions:

'(1) Whether, on the facts and in the circumstances of the case, the Tribunal was justified in confirming the assessment of a sum of Rs. 60,840 Under Section 41(2) of the Income-tax Act, 1961, on account of depreciation admittedly allowed to that extent to the assessee

(2) Whether, on the facts and in the circumstances of the case, the bidding amounted to a distribution of assets on dissolution of the assessee-firm and the matter fell outside the scope of Section 47(ii) of the Act and no amount was taxable as capital gain and

(3) Whether there was any mistake apparent in the order of the Tribunal dated 18th May, 1979, liable to be rectified Under Section 254(2) of the Act and, if so, to what effect '

2. Brief facts leading to the present reference are as follows : The assessee during the account year relevant to the assessment year 1964-65 was a registered firm consisting of the three partners Milkhiram, Madanlal Anand and Bramha Dutt. The

original assessment of the firm was completed on a total income of Rs. 2,08,230 on January 20, 1969. The Commissioner acting under Section 263(1) of the Act considered the assessment as prejudicial to the interest of the Revenue and set it aside, vide order dated January 15, 1971, with a direction to the ITO to make a fresh 'assessment. After remand, the facts which came to the notice of the ITO were that the partners of the firm acting under Clause (2) of the partnership deed dated June 1, 1962, had entered into an agreement dated August 24, 1963, Vide Clause 6 of the said agreement, it was decided that there would be an inter-bidding for a sale of the assets of the partnership firm and the highest bidder among the partners will be the purchaser of the entire property including its assets and liabilities and the sale proceeds were to be distributed among the partners according to their respective shares as specified in the partnership deed. In pursuance of the said agreement dated August 24, 1963, there was a bidding among the partners on August 25, 1963. Shri Milkhiram made the highest bid of Rs. 2,70,000. He was declared the purchaser of the business. Later, on 6th September, 1963, a dissolution deed was drawn up stating that the firm stood dissolved w.e.f. August 1, 1963.

3. In the dissolution deed the value of the goodwill was determined at Rs. 1,80,855.82 and the value of the remaining assets less liabilities to creditors as per balance-sheet, was determined at Rs. 89,146.18. On the above facts the ITO completed the fresh assessment on 25th May, 1976, on a total income of Rs. 2,00,895 including therein the following sums :

1. Profit Under Section 41(2) from sale of assets--Rs. 60,840.

2. Long-term capital gains on transfer of goodwill--Rs. 1,20,054.

4. The assessee preferred an appeal before the AAC challenging the additions made above. It was contended before the AAC that the sale of the business to one of the partners was a realisation sale after the dissolution of the firm and, therefore, the sum of Rs. 60,840 was not liable to tax under Section 41(2) of the Act. As regards the amount representing the value of the goodwill, it was contended that no capital gain was chargeable on the goodwill of the firm because the goodwill in the case of thisfirm was a self-generated asset. The AAC partly accepted this argument and deleted the addition of R. 1,20,054 representing the value of the goodwill of the firm, but confirmed the addition of Rs. 60,840 as profits under Section 41(2) of the Act.

5. The assessee as well as the Department filed appeals before the Income-tax Appellate Tribunal. The Tribunal dismissed both the appeals. As regards the addition of Rs. 60,840 on the sale of the assets under Section 41(2) of the Act, the Tribunal held that the sale was not a realisation sale after dissolution of the partnership but it was a transfer before the dissolution. Accordingly the Tribunal held that the addition of Rs. 60,840 under Section 41(2) of the Act was proper. As regards the addition of the value of the goodwill, the Tribunal concurred with the view of the AAC that this amount could not be added as capital gain because the goodwill in the instant case had been generated by the firm itself and there was no transfer of any asset. This order was passed by the Tribunal on 18th May, 1979 (annex. H).

6. Neither the assessee nor the Department filed any application under Section 256(1) of the Act requiring the Tribunal to refer to the High Court any question of law arising out of such orders. Consequently the order passed by the Appellate Tribunal in appeal became final under Section 254(4) of the Act.

7. The assessee after the dismissal of its appeal filed a miscellaneous application under Section 254(2) of the Act seeking the rectification of a mistake said to be apparent from the record. This application was dismissed by the Tribunal, vide order dated January 18, 1980, holding that there was no mistake apparent from the record and no question of rectification arose.

8. The assessee thereafter sought a reference under Section 256(1) of the Act on the following questions arising out of the order dated January 18, 1980, dismissing its application for rectification under Section 254(2) of the Act. The question which the assessee had formulated may be reproduced :

'1. Whether, on the facts and in the circumstances of the case, the Tribunal was justified in holding that there was no case for rectification of the order under Section 254?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was justified in holding that there was no mistake apparent on the record justifying rectification and

3. Whether, on the facts and in the circumstances of the case, the Tribunal ought to have held that the bidding amounted to only a distribution -consequent on dissolution which is outside Section 47(ii) of the Income-tax Act '

9. The Tribunal, however, formulated its own questions which have been reproduced in para, 1 of this order.

10. Before answering the reference made by the Appellate Tribunal, we may consider the maintainability of the reference itself against the order passed by the Appellate Tribunal in miscellaneous application filed under Section 254(2) of the Act. We have already mentioned that the appellate order passed by the Tribunal on the appeal filed by the assessee became final under Section 254(4) of the Act because no reference was sought in respect of any question arising out of that order. An application was filed under Section 254(2) by the assessee for amendment of the order on the ground that there was a mistake apparent from the record in the appellate order which required rectification. This application was dismissed because according to the Tribunal there was no mistake apparent from the record which required rectification. Thus the original order stood as it was.

11. Section 256(1) of the I.T. Act is as follows:

'256. (1) The assessee or the Commissioner may, within sixty days of the date upon which he is served with notice of an order under Section 254, by application in the prescribed form, accompanied where the application is made by the assessee by a fee of one hundred and twenty-five rupees, require the Appellate Tribunal to refer to the High Court any question of law arising out of such order and, subject to the other provisions contained in this section, the Appellate Tribunal shall, within one hundred and twenty days of the receipt of such application, draw up a statement of the case and refer it to the High Court:.....'

12. The language used in Section 256(1) shows that the order contemplated under Section 256(1) is the order passed under Section 254 of the Act. Under Section 254(1) the Appellate Tribunal passes an order on the appeal filed by the assessee or

the Revenue. This order may be amended under Section 254(2) of the Act with a view to rectifying any mistake apparent from the record. If, however, the application for rectification is dismissed, there is no amendment of the order passed under Section 254(1) of the Act. Since no reference in the instant case was sought in respect of the appellate order passed under Section 254(1), we are of the view that no reference from the order rejecting an application for rectification of any mistake is tenable under Section 254(1) of the Act. The position obviously would have been different had the Appellate Tribunal amended its appellate order with a view to rectifying any mistake apparent from the record. In that case the amended order could be a subject-matter of reference under Section 256(1) of the Act. But if the order is not amended and the application for rectification is dismissed, the only order which stands is the order passed in appeal under Section 254(1) of the Act and if no reference has been sought in respect of such order, the same becomes final in view of the language used in Section 254(4) of the Act. Nodirect decision on this question was brought to our notice but it will be useful, for the purpose of analogy, to refer to the decision of the Judicial Committee in CIT v. Tribune Trust [1948] 16 ITR 214. The context in which their Lordships made the observations at p. 226 of the report was of course different but the principle stated therein can be applied to the issue under discussion. In the cited case the assessee had moved the Commissioner under Section 33 of the Indian I.T. Act, 1922, before its amendment in 1939, for cancellation of the earlier assessments and for a refund of the tax in view of the Privy Council decision in relation to the assessee's claim for exemption in a later assessment year. The Commissioner rejected the application. Against this order of rejection a reference was sought to the High Court under Section 66 of the Act. The Commissioner declined to make a reference but the High Court directed him to do so and passed an order holding that the assessee was entitled to the refund. When the matter was taken to the Privy Council in appeal by the Revenue, their Lordships made the following observations (p. 226):

'For it is proper that, where the Commissioner does make an order which worsens the position of the assessee, the latter should have a right of appeal, since against that order he has no other right. It is further confirmed by the proviso to Section 66(2) which limits a reference from an order under Section 33 to cases where the question of law arises out of that order itself and excludes it where the question of law arises out of a previous order under Section 31 or Section 32 which is revised under Section 33. In the case in which a reference is permitted, there is a new point of law which could not be otherwise the subject of appeal; in the case in which it is excluded, the point of law was one that could already have been appealed under the appropriate section.'

13. Their Lordships thereafter observed that since the Commissioner did not enhance the assessment or otherwise alter the assessee's position for the worse, the reference was incompetent. We are aware of the difference between the provision which the Judicial Committee had construed and the corresponding provisions (Sections 254 & 256) of the 1961 Act. But the underlying principle stated by their Lordships of the Privy Council in the cited case can apply mutatis mutandis to the provisions of the I.T. Act of 1961 also.

14. In the present case also the appellate order dismissing the assessee's appeal against the addition of Rs. 60,840 under Section 41(2) of the Act had become final as no reference had been sought in respect of that order. It was not open to the assessee to enlarge the scope of a reference which is subject to a particular time-limit by

taking recourse to Section 254(2) of the Act seeking rectification of the order and then on refusal of the Tribunal to doso raising questions arising out of the main appellate order passed under Section 254(1) of the Act.

15. Coming to the questions referred by the Appellate Tribunal to us we find that the Appellate Tribunal had clearly recorded a finding in its appellate order as follows :

'Since the transfer of assets took place first and the dissolution later, the contention that the transaction in question was nothing but a realisation of the assets of the firm after the transfer cannot be accepted.'

16. This is a finding of fact binding on this court. (See CIT v. Manna Ramji and Co. : [1972]86ITR29(SC)). It was not disputed before us that if the sale in favour of one of the partners by virtue of the agreement dated August 24, 1963, had been made prior to the dissolution of the firm, recovery of the depreciation allowed in the preceding assessment years in respect of the plant, machinery, etc., could be treated as profit Under Section 41(2) of the Act. In A. S. Krishna Setty and Sons v. Addl. CIT : [1975]100ITR587(KAR) the Karnataka High Court was considering the withdrawal of development rebate allowed to the assessee-ftrm on machinery on transfer of the said machinery to some of the partners. Venkataramaiah J. (as he then was), held that such a sale during the subsistence of the partnership firm (i e., before its dissolution) would amount to a transfer within the meaning of Section 34(3)(b) of the I.T. Act, 1961, read with Section 155(5) thereof. The Supreme Court in Malabar Fisheries Co. v. CIT [1979] 20 ITR 49, cited by the learned counsel for the assessee, has taken the same view. In that case the assets of the firm were distributed after dissolution and, therefore, it was held that Section 34(3)(b) was not attracted. Conversely, if the sale was before dissolution of the firm, Section 41(2) of the Act was attracted.

17. In CIT v. Kartikey V. Sarabhai : [1981]131ITR42(Guj) , the Gujarat High Court considered the expression 'transfer' in the light of its definition in Section 2(47) of the I.T. Act, 1961. The ratio of the decision is that if the assets of a firm before dissolution are sold by the partners of a firm to one of them, capital gain under Section 45 will be chargeable as profits. The same principle will apply to the profits (balancing charge) received or accrued under Section 41(2) of the Act.

18. Learned counsel for the assessee vehemently argued that in fact the amount paid to the third partner as a result of inter-bidding in pursuance of the agreement dated August 24, 1963, was a realisation of the assets after the dissolution of the firm and not a 'sale' within the meaning of Section 41(2) of the Act. This argument cannot be accepted in view of the clear finding of the Appellate Tribunal that the sale of assets was prior to the dissolution of the firm and not after it. To skirt this finding of fact, learned counsel contended that this finding was perverse inasmuch as the Appellate Tribunal did not properly appreciate the effect of theagreement dated August 24, 1963, in pursuance of which the inter-bidding was carried out on August 25, 1963. According to the learned counsel, the document (annex. B) clearly showed that the parties had already agreed to dissolve the firm before holding a bid to determine the value of the assets. This argument has no substance because this court acting under Section 256(1) of the Act has only an advisory jurisdiction on a question of law arising out of findings of fact recorded by the Tribunal. It is not open to this court to exercise the appellate jurisdiction and question the findings of fact recorded by the Tribunal. Further, neither the assessee, in its application under Section 256(1) before the Tribunal, questioned the legality of the finding on this point nor sought a reference to

the effect that the finding recorded on this point was perverse. We, therefore, cannot go behind the finding of the Tribunal about the date of dissolution nor answer a question of law by recording a finding of fact contrary to the one recorded by the Tribunal on this issue.

19. Thus, on the facts and in the circumstances of the case, as found by the Tribunal, the Tribunal was justified in confirming the addition of Rs. 60,840 under Section 41(2) of the I.T. Act on account of the depreciation which was admittedly allowed to that extent to the assessee in the earlier assessment years. We also hold that on the facts and circumstances of the case, as found by the Tribunal, the Tribunal was justified in holding that the bidding did not amount to a distribution of assets on the dissolution of the asses-see-firm. Question No. (1) is, therefore, answered in the affirmative and in favour of the Revenue and question No. (2) is answered in the negative, in favour of the Revenue and against the assessee.

20. As regards question No. (3) we are of the view that there was no mistake apparent on the record in the appellate order of the Tribunal dated May 18, 1979, which required rectification under Section 254(2) of the Act. The finding of the Appellate Tribunal about the date of dissolution of the firm was based oh an appreciation of the evidence and the same could not be rectified under Section 254(2) of the Act by raising debatable or arguable questions. [See T. S. Balaram. ITO v. Volkart Brothers : [1971]82ITR50(SC)]. Besides, as discussed earlier, the question whether an order of the Tribunal rejecting an application for rectification can be a subject of reference under Section 256(1) or not is not free from doubt and according to us no reference in respect of such an order is tenable. For these reasons we answer question No. (3) also in the negative, in favour of the Revenue and against the assessee.

21. Reference answered accordingly. There will be no order as to costs.