KERALA HIGH COURT

Commissioner of Income-Tax

Vs

C.M. Kunhammed

(P Govindan Nair and M Isaac, JJ.)

18.01.1972

JUDGMENT

Govindan Nair, J.

1. This is a reference under Section 256(1) of the Income-tax Act, 1961 (hereinafter referred to as " the Act"), at the instance of the Commissioner of Income-tax, Ernakulam. The questions referred are :

> "(1) Whether, on the facts and in the circumstances of the case, the development rebate granted to the assessee for the assessment years 1960-61 and 1961-62 cannot be withdrawn under section 155(5) of the Income-tax Act of 1961 ?
> (2) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the development rebate amounting to Rs. 9,482 and Rs. 4,844 for the assessment years 1960-61 and 1961-62 could not be withdrawn under Section 35(11) of the Indian Income-tax Act, 1922 ? "

2. The assessment years are 1960-61 and 1961-62 and the relative accounting periods are those that ended on the 31st July, 1959, and the 31st July, 1960, respectively. The assessee, an individual, had been carrying on business as timber merchant and was also running a saw mill under the style " The Seeyan Saw Mills". On the 1st August, 1960, he formed a partnership with his wife and his manager as partners. This is evidenced by a deed dated 1st August, 1960, which is annexure " D ". The business was thereafter carried on by the firm.

3. In the years of assessment 1960-61 and 1961-62, development rebate of Rs. 9,482 and Rs. 4,844, respectively, in respect of certain machinery installed during the respective accounting years were allowed.

4. On the formation of the partnership the Income-tax Officer felt that there had been a transfer of the machinery installed by the assessee to the firm that was constituted on August 1, 1960, and, therefore, he took action under Section 155(5) of the Act. The assessee's contention that there had been no transfer was negatived by the Income-tax Officer and two separate orders both dated October 8, 1964, were passed in relation to the two assessment years 1960-61 and 1961-62, amending the earlier assessment orders by withdrawing the development rebates that had been

allowed. The assessee appealed to the Appellate Assistant Commissioner but those appeals were dismissed. In the further appeal before the Tribunal two contentions were raised. The first was that only the provisions of the Indian Income-tax Act, 1922, would, if at all, apply, because the development rebate was allowed in an assessment made under the provisions of the 1922 Act and those assessments had been finalised before the Act came into force and even the alleged transfer of machinery had taken place before the Act came into force. It was, therefore, urged that if at all only Section 35(11) of the 1922 Act would apply. Secondly, it was urged that Section 35(11) was not attracted because there had been no transfer and in any event there had been no transfer to a " person ".

5. The Tribunal accepted both these contentions and held that Section 35(11) would apply and that there had been no transfer as envisaged by Section 35(11)(i) of the 1922 Act and hence allowed the appeal by its order which is annexure "E".

6. I understand the first question as raising the point as to whether it is Section 155(5) of the Act that would apply or whether it is Section 35(11) of the 1922 Act that would apply.
7. The Indian Income-tax Act, 1922, was repealed by Section 297(1) of the Act. Provision has been made in Sub-section (2) of Section 297 of the Act for action being taken as if the Act had not been passed. For instance, Section 297(2)(a) authorises proceedings for the assessment of a person who had filed a return before the commencement of the Act being taken and continued as if the Act had not been passed. It was not argued before us that the action taken under Section 155(5) of the Act for withdrawing the development rebate given was a proceeding in assessment. Assuming without deciding that it is not a proceeding in assessment and, therefore, Section 297(2J(a) has no application, the question arises whether action can be taken under Section 155(5) either by the vigour of that section or that section read with Section 34(3)(b) of the Act. We may also mention here that no reliance has been placed on any clause of Sub-section (2) of Section 297 as authorising action being taken under the Act. I shall now read Section 34(3)(b) and Section 155(5) of the Act.

> " 34. (3)(b) 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 under Section 33 or under the corresponding provisions of the Indian Income-tax Act, 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 :
> Provided that this clause shall not apply--
> (i) where the ship has been acquired or the machinery or plant has been installed before the first day of January, 1958 ; or
> (ii) where the ship, machinery or plant is sold or otherwise transferred by the assessee to 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; or
> (iii) where the sale or transfer of the ship, machinery or plant is made in connection with the amalgamation or succession, referred to in Sub-section (3) or Sub-section (4) of Section 33."
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> "155. (5) 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 under Section 33 or under the corresponding provisions of the Indian Income-tax Act, 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 denned in Section 617 of the Companies Act, 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, re-compute 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 so utilised. "

8. The wording of these sections, I think, makes it abundantly clear that when the conditions mentioned in those sections are satisfied action can be taken under Section 155(5) for withdrawal of the development rebate that had been allowed in an assessment that was made under the 1922 Act which was completed before the Act came into force and where the transfer of plant or machinery in regard to which development rebate had been granted also took place before the coming into force of the Act. All the necessary conditions for application of the section may take place before the Act came into force. Even then the section permits action being taken under that section. For the purpose of this case it is even unnecessary to refer to Section 34(3)(b) excepting to understand the scheme of the Act and to understand its true scope and intent, for the facts of the case are such that would attract Section 155(5). The relevant accounting periods for the two assessment years 1960-61 and 1961-62 were, as already stated, the years that ended on July 31, 1959, and July 31, 1960. The development rebate had been allowed on the installation of machinery that took place during those accounting periods. Therefore, Section 155(5) was attracted because the installation was after the 31st day of December, 1957. It does not matter that the development rebate had been granted under the provisions of the 1922 Act because that too is covered by Section 155(5). The alleged transfer was within eight years of the end of the previous year as it is stated to have taken place on August 1, 1960. The section, therefore, is attracted and there is no impediment to action being taken under that section provided there had been a sale, or a transfer otherwise, of the plant or machinery. Section 155(5) deals with transfers that took place before the Act came into force as well as transfers after the coming into force of the Act. There being this clear provision in the section that action, can be taken under that section for withdrawal of the development rebate no further question arises excepting whether there has

been a sale, or transfer otherwise. So it is unnecessary to refer to the decisions of the Supreme Court in *Kalawati Devi Harlalka v. Commissioner of Income-tax*[1], , *S. Sankappa v. Income-tax Officer, Central Circle VI, Bangalore,*[2] and *T. S. Baliah v. T. S. Rangachari, Income-tax Officer, Central Circle VI, Madras*[3], These decisions are useful to understand the scope of the provision made in Section 297, or when there is no provision either in Section 297 or in the other sections of the Act to decide whether Section 6 of the General Clauses Act can be relied on. If there is no provision made in Section 297 or elsewhere in the Act, Section 6 of the General Clauses Act would apply (T. S. Baliah v. T. S. Rangachari, Income-tax Officer, Central Circle VI, Madras), But there is specific provision in the Act regarding withdrawal of development rebate in sections 34(3)(b) and 155(5) and when the conditions mentioned in these sections are satisfied, these sections must apply.

9. Two questions may, however, arise : (1) whether there had been a transfer or not, and (2) whether there has been a transfer or not should be decided with reference to the definition of the term " transfer " in Section 2(47) of the Act or whether it should be determined with reference to the law as it stood at the time of the alleged transfer. The answer to the second question is that whether there is a transfer or not must be determined with reference to the law at the time of the transfer. If the transfer took place before the Act came into force, the question will have to be decided without reference to the definition in Section 2(47) of the Act. In relation to the transfers that took place after the Act came into force, the definition might or might not apply depending on the scope of the definition. It was suggested that the definition would apply only for the purpose of capital gains as transfer is defined in relation to the transfer of a " capital asset ", which expression as such is used only in the section of the Act dealing with capital gains. It is unnecessary to decide this matter because the alleged transfer in this case took place before the Act came into force. I am unable to discern anything in either Section 34(3)(b) or Section 155(5) or for that matter in any other provision of the Act that has been brought to our notice which extends the definition of the term " transfer " in Section 2(47) of the Act to a transaction that took place before the Act came into force. No doubt, if there had been a transfer even before the Act, action can be taken under Section 155(5) as the section takes note of a past event for permitting action being taken under the Act. This, however, is not sufficient to make the definition of transfer applicable to transactions that took place before the Act came into force.

10. In the above view whether there has been a transfer or not covered by the first question posed in paragraph 8 must be decided without reference to the definition in Section 2(47) of the Act. If that be so, I think the matter is concluded by the decisions of the Supreme Court *inCommissioner of Income-tax v. Dewas Cine Corporation*[4], and *Commissioner of Income-tax v. Bankey Lal Vaidya*[5], In the earlier case dealing with the proviso to Section 10(2)(vii) of the Indian Income-tax Act, 1922, their Lordships observed as follows:

> " On dissolution of the partnership, each theatre must be deemed to be returned to the original owner, in satisfaction partially or wholly of his claim to a share in the residue of the assets after discharging the debts and other obligations. But thereby the theatres were not in law sold by the partnership to the individual partners in consideration of their respective shares in the residue. The expressions ' sale' and ' sold' are not defined in the Income-tax Act: those expressions are used in section 10(2)(vii) in their ordinary meaning. 'Sale', according to its ordinary meaning, is a transfer of property for a price, and adjustment of the rights of the partners in a dissolved firm is not a transfer, nor it is for a price. "

11. The question again arose before the Supreme Court in Commissioner of Income-tax v. Bankey Lal Vaidya. The section that fell for interpretation was Section 12B(1) of the Indian Income-tax Act, 1922, which mentioned sale, exchange or transfer of a capital asset. I shall extract the relevant passages from that judgment.

> " In the case in hand there is no sale and payment of price, but payment of the value of share under an arrangement for dissolution of the partnership and distribution of the assets. The rights of the parties were adjusted by handing over to one of the partners the entire assets and to the other partner the money value of his share. Such a transaction is not in our judgment a sale, exchange or transfer of assets of the firm. In Commissioner of Income-tax v. Dewas Cine Corporation in dealing with the meaning of the expressions ' sale ' and ' sold ', as used in Section 10(2)(vii) of the Indian Income-tax Act, 1922, this court observed that the expression ' sale' in its ordinary meaning is a transfer of property for a price, and adjustment of the rights of the partners in a dissolved firm by allotment of its assets is not a transfer for a price. In that case the assets were distributed among the partners and it was contended that the assets must in law be deemed to be sold by the partners to the individual partners in consideration of their respective shares, and the difference between the wntten-down value and the price realised should be included in the total income of the partnership under the second proviso to section 10(2)(vii). This court observed that a partner may, it is true, in an action for dissolution insist that the assets of the partnership be realised by sale of its assets, but property allotted to a partner in satisfaction of his claim to his share, cannot be deemed in law to be sold to him."

12. In view of these pronouncements it is impossible to hold that there has been a sale, or a transfer otherwise, of the machinery by the formation of the partnership, for the principle of the above decisions, which dealt with the question whether there was a transfer on the dissolution of a partnership and distribution of assets, must apply with equal force to the formation of a partnership. In fact, such a view has been taken by the Calcutta High Court in the decision in*Commissioner of Income-tax v. Hind Construction Ltd.*[6], and the Supreme Court in appeal therefrom (Civil Appeals Nos. 1287 (NT) of 1971 and 2001 of 1968) confirmed the decision.

13. I, therefore, answer question No, 1 in favour of the assessee and against the department. I answer question No. 2 also in the affirmative, that is, in favour of the assessee and against the department. I direct the parties to bear their respective costs.
14. A copy of this judgment under the seal of the High Court and the signature of the Registrar will be sent to the Appellate Tribunal as required by Sub-section (1) of Section 260 of the Income-tax Act, 1961.

Cases Referred.

1[1967] 66 I.T.R. 680 ; [1967] 3 S.C.R. 833 (S.C)
2[1968] 68 I.T.R. 760 ; [1968] 2 S.C.R. 764 (S.C.)
3[1969] 72 I.T.R. 787, [1969] 3 S.C.R. 65 (S.C.)
4[1968] 68 I.T.R. 240, 243 ; [1968] 2 S.C.R. 173 (S.C.)
5[197IJ 79 I.T.R. 594, 597 ; [1971] 3 S.C.R. 406 (S.C)
6[1970] 78 I.T.R. 664 (Cal)