PATNA HIGH COURT

Commissioner of Income-Tax

Vs

Pure Nichitpur Colliery Company

(N Untwalia, C.J. S Jha, J.)

09.09.1974

JUDGMENT

Untwalia, C.J.

1. These three tax references under Section 256(1) of the IncomeAct,1961(hereinafter referred to as "the 1961 Act"), have been made by the Income-tax Appellate Tribunal, Patna, on a common question of law, as the facts are identical. The question of law referred for our opinion runs as follows :

> "Whether, on the facts and circumstances of the case, the order of the Tribunal annulling the assessment in view of the provisions of the Income-tax Act, 1961, is legal and proper ?"

2. The assessment years in question are 1964-65, 1965-66 and 1966-67. In respect of these three years some of the partners of the firm were assessed to income-tax. Subsequently, the firm was also assessed. The firm was an unregistered one. At the Tribunal stage the assessments have been annulled, following the decision of the Supreme Court in *Commissioner of Income-tax v. Murlidhar Jhawar and Purna Ginning and Pressing Factory*[1], and the decisions of the Allahabad High Court in *Girdhari Lal Laxman Prasad v. Commissioner of Income-tax2Hari Om Company v. Commissioner of Income-tax*[3]*, and India Army and Police Equipment Factory v. Commissioner of Income-tax*[4]*,* Briefly, on these grounds the question of law has arisen for our opinion, especially for a consideration of the question whether the law laid down by the Supreme Court still holds good in view of the amendment made in the Indian Income-tax Act 1922 (hereinafter called "the 1922 Act"), in the year 1956 as also in the 1961 Act.

3. As I have said above the assessee in these cases is an unregistered firm and derived income from coal mine. The firm was assessed to income-tax by the Income-tax Officer on the amounts mentioned in the statement of the case which are not necessary to be reproduced here. The

assessee challenged the figures of the assessment in appeal before the Appellate Assistant Commissioner. He modified the assessments. When further appeals were taken before the Tribunal the crucial point was taken that it was not legal to make an assessment on an unregistered firm after some of its partners had already been assessed to tax on their share of income from the firm and as such the assessments were all wrong and illegal. The partners' assessments were completed for all the three years in question on December 31, 1965, whereas the assessment of the unregistered firm was made on February 15, 1967, February 25, 1967, and February 28, 1967, respectively, for the assessment years 1964-65, 1965-66 and 1966-67. The Tribunal knocked down the assessments on the new ground taken on behalf of the assessee-firm. It did not accept the contention of the revenue that the law laid down in the cases noticed above was no longer good, in view of the various amendments in the statute.

4. Before I proceed to discuss the law, I may note one more fact from one of the appellate orders of the Tribunal, the other orders being identical, and that is this. The Income-tax Officer completed the assessment on the partners of the firm by taking the share income from the firm, subject to the same being liable to be rectified when the correct income of the unregistered firm was determined. In the view of of the Tribunal, the Income-tax Officer, therefore, had exercised the option to assess the individual partners in respect of the share income from the assessee-firm. Having once exercised that option, it was not legal for the Income-tax Officer to make an assessment on the firm in the status of an unregistered firm after some of its partners had been assessed to tax on the share income of the firm.

5. *In Commissioner of Income-tax v. Kanpur Coal Syndicate*[5], Subba Rao J. (as he then was), delivering the judgment on behalf of the court, pointed out at page 228 :

"Section 3 imposes a tax upon a person in respect of his total income. The persons on whom such tax can be imposed are particularized therein, namely, Hindu undivided family, company, local authority, firm, association of persons, partners of firm or members of association individually. The Section, therefore, does not in terms confer any power on any particular officer to assess one of the persons described therein, but is only a charging section imposing the levy of tax on the total income of an assessable entity described therein. The section expressly treats an association of persons and the individual members of an association as two distinct and different assessable entities. On the terms of the section the tax can be levied on either of the said two entities according to the provisions of the Act. There is no scope for the argument that under Section 3 the assessment shall be only on the association of persons as a unit though after such assessment the share of the income of a member of that association may be added to his other income under Section 14(2) of the Act. This construction would make the last words of the section, viz., 'members of the association individually' a surplusage. This argument is also contrary to the

express provisions of Section 3, which mark out the members of the association individually as a separate entity from the association of persons. Income of every person, whether he is a member of an association or not, is liable to the charge under the head 'every individual'. Section 14(2)(b) only says that if such an individual happens to be a member of an association of persons which has already been assessed, the tax would not be payable in respect of the share of his income again. That under the Act an assessment can be made on an association of persons as a unit or, alternatively, on the individual members thereof in respect of their respective shares of the income was assumed by this court in *Commissioner of Income-tax v. Raja Reddy Mallaram*[6], We, therefore, hold that Section 3 impliedly gives an option to an appropriate authority to assess the total income of either the association of persons or the members of such association individually."

6. Following this decision, Shah J. (as he then was) said in the case of Commissioner of Income-tax v. Murlidhar Jhawar and Purna Ginning and Pressing Factory :

> "The same principle would apply to the case of assessment of partners individually of an unregistered firm. The partners may be assessed individually or they may be assessed collectively in the status of an unregistered firm : the Income-tax Officer cannot, however, seek to assess the one income twice--once in the hands of the partners and again in the hands of the unregistered firm."

7. Following the decisions of the Supreme Court, the Allahabad High Court in the decisions referred to above has taken the same view. The Supreme Court decisions were in relation to a period which was not covered by the 1922 Act as it stood amended in 1956. The periods in some of the Allahabad decisions were covered by the amended law; yet the same view was taken. I now proceed to discuss the argument strenuously put by the learned standing counsel for the revenue to persuade us to hold that it is now possible to tax the share income in the hands of the partners as also the income in the hands of the firm.

8. Before the amendment of the 1922 Act by the Finance Act, 1956, which came into force from the 1st April, 1956, the law of taxing a partnership firm was simple. In the case of a registered firm no tax was levied on the firm ; tax was levied on the share income derived by the partners in their hands. In the case of an unregistered firm, it was the option of the Income-tax Officer to treat the unregistered firm as an entity by itself, tax the total income of the firm in its hands or to tax the share income in the hands of the partners, if'adopting the latter method was more advantageous to the revenue. Then came the amendment by the Finance Act of 1956, by which sections 14 and 23(5) of the 1922 Act were amended. I do not think it necessary to quote the amended provisions, because, more or less, such amended provisions were incorporated in the 1961 Act which I shall hereinafter quote. I may, however, state broadly the effect of the

amendment brought about by the 1956 Act, The effect was that in the case of a registered firm, so to say, there was a double taxation--certain amount of tax could be imposed upon the registered firm, but principally the share income derived by the partners was to be taxed in their hands. On the other hand, in the case of an unregistered firm option was given to the Income-tax Officer to tax the total income of the unregistered firm, treating it as a separate and distinct entity, or to tax the share income in the hands of the individual partners under certain circumstances, the circumstances being that the tax which would be payable by the partners would be greater than the aggregate amount which would be payable by the firm and the partners individually, if separately assessed. If the firm would have been taxed, then the share income of the partners could have been added to the other income of theirs only for the purpose of rate under Section 14 of the 1922 Act. I shall also refer in this judgment to the amendment which has been brought about by the Taxation Laws (Amendment) Act, 1970, with effect from the 1st April, 1971. Although the said amended law will not cover the periods in question; it will merely explain the position of law as it existed at the relevant time.

9. The relevant provisions, which are to be noticed in the 1961 Act as they stood before the amendment brought about from April 1, 1971, are the definition section of "person" in Section 2(31); Section 4, the charging Section; Sections 66 and 67, which corresponded to Section 16 of the 1922 Act; Section 86, which was equivalent to Section 14 of the 1922 Act; and Sections 182 and 183 corresponding to Section 23(5) of the 1922 Act. The charging Section 4 of the 1961 Act provides for imposition of tax in respect of the total income of every person. "Person" has been defined to include:

" (i) an individual,

(ii) a Hindu undivided family.

(iii) a company,

(iv) a firm,

(v) an association of persons or a body of individuals, whether incorporated or not,

(vi) a local authority, and

(vii) every artificial juridical person, not falling within any of the preceding Sub-clauses."

10. In the two decisions of the Supreme Court referred to above stress was laid on the charging Section 3 of the 1922 Act where the word "or" had been used, but in the said charging section the description of the various types of persons had been given, because Section 2(9), which had

defined the term "person" in the 1922 Act, had merely said that it included a Hindu undivided family and a local authority. Other types of persons were, therefore, enumerated in the charging section. But it is manifest that the total income of every person in Section 4 of the 1961 Act must mean any one person enumerated in Section 2(31), or in certain circumstances it may mean more than one, e.g., in the case of a registered firm, now, "person" would mean the firm as also the individual partner. But the deciding factor is not the charging Section. The charging section imposes the tax liability on the person. The machinery sections provide that in a given case who is the person to be assessed to income-tax--whether a firm or a partner or both ?

11. Section 182 of the 1961 Act provides for assessment of registered firms. The income-tax payable by the firm itself has to be determined under Clause (i) of Sub-section (1). The share of each partner in the income of the firm has to be included in his total income and assessed to tax accordingly. Section 183, as it stood at the relevant time, read as follows:

"In the case of an unregistered firm, the Income-tax Officer-

(a) may determine the tax payable by the firm itself on the basis of the total income of the firm ; or

(b) if, in his opinion, the aggregate amount of the tax payable by the partners if the firm were treated as a registered firm would be greater than the aggregate amount of the tax which would be payable by the firm under Clause (a) and the tax which would be payable by the partners individually, may proceed to make the assessment under Clause (ii) of subsection (1) of Section 182 as if the firm were a registered firm; and where the procedure specified in this Clause is applied to any unregistered firm, the provisions of Sub-sections (2), (3) and (4) of Section 182 shall apply thereto as they apply in the case of a registered firm."

12. Before I explain the meaning of Section 183, I would refer to the provisions of Section 66, which says :

"In computing the total income of an assessee, there shall be included all income on which no income-tax is payable under Chapter VII (which includes Section 86) and any amount in respect of which the assessee is entitled to a deduction from the amount of income-tax on his total income with which he is chargeable for any assessment year in accordance with, and to the extent provided in, Sections 87 and 88."

13. The method of computing a partner's share in the income of the firm has been prescribed in Section 67. Section 86(iii) runs as follows :

"Income-tax shall not be payable by an assessee in respect of the following--.....

> (iii) if the assessee is a partner of an unregistered firm, any portion of the assessee's share in the profits and gains of the firm computed in the manner laid down in Section 67 on which income-tax is payable by the firm."

14. It is not necessary to refer to Clause (iv) which provides that income-tax is not payable on, certain income on the assessee's share in the total income of the firm in certain respects. Reading all these provisions together it would be noticed that the option of the Income-tax Officer under Section 183 is either to determine the tax payable by the firm itself on the basis of the total income of the firm under Clause (a) or to tax the partners if, in his opinion, the aggregate amount of the tax payable by them if the firm were treated as a registered firm would be greater than the aggregate amount of the tax which would be payable by the partners individually by adding the share income for the purpose of rate only. It would thus be clear that even after the amendment brought about in the 1922 Act in the year 1956, Which was incorporated in the 1961 Act, the Income-tax Officer had the option in the case of an unregistered firm either to tax the total income in the hands of the firm, treating it as a separate entity, or to tax the share income in the hands of the partners. He could not do both. Neither the charging Section 4 nor any other provision of the 1961 Act empowered him to do so. It was still his option to do one or the other and not both. The law, therefore, laid down by the Supreme Court was still good, the new provisions did not bring about any change in respect of the exercise of the option, and once the option was exercised to tax the share income of the unregistered firm in the hands of the partners then, on computation of the income of the unregistered firm, the assessment of a partner could be rectified under Section 155 of the 1961 Act. But it was not open to the Income-tax Officer to change his option and tax the unregistered firm itself.

15. After the amendment brought about by the Taxation Laws (Amendment) Act, 1970, in Section 183(b) and the consequent amendments made in Sections 67 and 86(iii), it would be noticed that the law now is, as it was before, that the Income-tax Officer may treat the unregistered firm as a registered firm and proceed to tax the firm as also the share income in the hands of the partners in accordance with Sub-section (1) of Section 182 of the Act, whereas previously in Clause (b) of Section 183 reference was made only to Sub-clause (ii) of Sub-section (1)of Section 182 of the 1961 Act. It is not necessary for me to express any concluded opinion on the point, but if I may say so with respect, it is because of the amendment in the law brought about by the amending Act of 1970 that the learned author in his book, Iyengar on Income Tax, sixth edition (volume II) felt persuaded to say in his commentary on Section 67, at page 1217, as follows:

> "A partner is a separate assessable entity as distinguished from the firm of which he is a partner. The charging Section 4 of the Act of 1961 imposes a charge on 'every person'. So,

the circumstance that the partner has been assessed earlier is no bar to a later assessment of the firm. The decision of the Supreme Court to the contrary in Commissioner of Income-tax v. Murlidhar Jhawar & Puma Ginning and Pressing Factory was based on the language of Section 4 of the 1922 Act and laid down that both a firm (or association of persons) and its partners (or members) could not be charged to tax in respect of the same income. This decision will have no application under the 1961 Act. Even under the old Act, it was held not to apply to registered firms."

16. After the amendment brought about in the year 1971 by the 1970 amending Act, one may say that mere taxing the share income in the hands of the partner does not debar the Income-tax Officer from treating the partnership firm, which was an unregistered one, as a registered one and tax the firm itself under Section J82(1)(i). But I have referred to the view of the learned author and the amendment brought about with effect from the 1st April, 1971, not for the purpose of expressing any view of mine in that regard but only with the object of comparing the latter with the former law and to show that, as it stood at the relevant time governing the three tax cases in question, the decisions of the Supreme Court were applicable and once the option was exercised by the Income-tax Officer of taxing the share income in the hands of the partners, he had no jurisdiction to tax the total income of the unregistered partnership firm in its hands.

17. For the reasons stated above, the common question of law in all the three cases is answered in the affirmative, in favour of the assessee and against the revenue. I accordingly hold that, on the facts and in the circumstances of the case, the order of the Tribunal annulling the assessments for the three years in question was legal, valid and proper. The assessee must have the costs of all these references. A consolidated hearing fee is assessed at Rs. 150 only.

S.K. Jha, J.

18. I agree.

Cases Referred

1[1966] 60 ITR 95 (SC)
2[1968] 70 ITR 853 (All)
3[1969] 71 ITR 584 (A11)
4[1970] 75 ITR 693 (All)
5[1964] 53 ITR 225 (SC)
6[1964] 51 ITR 285 (SC)