Supreme Court of India
Shivram Poddar vs Income-Tax Officer, Central ... on 13 December, 1963
Equivalent citations: AIR 1964 SC 1095, 1964 51 ITR 823 SC
Author: Shah
Bench: A S Shah, M Hidayatullah
JUDGMENT Shah, J.

1. Balmokand Radheshyam (hereinafter called "the firm"), having its head office at Calcutta, carried on business in commission agency and cotton piece-goods. The firm which consisted of four partners, one of whom was Shivram Poddar, appellant in this appeal, was dissolved in February, 1950, and it appears that thereupon its business was discontinued. For the assessment year 1949-50, one of the partners of the firm submitted a return of its income and it was assessed on October 28, 1952, in the status of an unregistered firm.

2. On March 28, 1955, the Income-tax Officer issued a notice under section 34 read with section 22 (2) of the Indian Income-tax Act, 1922, addressed to the appellant as a partner of the firm at the time of its dissolution calling upon him to submit a return of the income of the firm for the year ending March 31, 1950. The appellant moved the High Court of Judicature at Calcutta for a writ of mandamus under article 226 of the Constitution commanding the Income-tax Officer to forbear from giving effect to the notice. The petition was dismissed by D. N. Sinha J. and that order was confirmed in appeal under the Letters Patent by the High Court.

3. The question which falls to be determined in this appeal is whether the income earned by the firm in the year ending March, 1950, could be assessed to tax under section 44 of the Indian Income-tax Act, 1922, after the firm was dissolved. Section 44 of the Indian Income-tax Act, 1922, before it was amended by the Income-tax (Amendment) Act, 1958, stood as follows :

"Where any business, profession or vocation carried on by a firm or association of persons has been discontinued, or where as association of persons is dissolved, every person who was at the time of such discontinuance or dissolution a partner of such firm or a member of such association, be jointly and severally liable to assessment under Chapter IV and for the amount of tax payable and all the provisions of Chapter IV shall, so far as may be, apply to any such assessment."

4. The object of the enactment is clear : it is to authorise assessment of tax on income, profits or gains earned in a business, profession or vocation carried on by a firm or association before discontinuance of the business, profession or vocation, or before dissolution of the association, and to impose joint and several liability upon every person who was at the time of discontinuance a partner of the firm or a member of the association or at the time of dissolution a member of the association.

5. This court in dealing with the effect of section 44 of the Indian Income-tax Act upon the liability of partner to be assessed in respect of the income of a firm which had discontinued its business on account of dissolution, observed in C. A. Abraham v. Income-tax Officer, Kottayam :

"In effect, the Legislature has enacted by section 44 that the assessment proceedings may be commenced and continued against a firm of which business is discontinued as if discontinuance has not taken place. It is enacted manifestly with a view to ensure continuity in the application of the machinery provided for assessment and imposition of tax liability notwithstanding discontinuance of the business of firms."

6. In Abraham's case discontinuance of business of the firm was the result of dissolution upon the death of one of the partners. The primary question in that case was about the competence of the Income- tax Officer to order the levy of penalty against a firm, after it had discontinued its business upon dissolution, for concealing the particulars of income or for deliberately furnishing inaccurate particulars of income in a return of the income of the firm. The validity of the order of assessment of income of the firm was not challenged in that case, though at the date of the order of assessment the firm stood dissolved and its business was discontinued. But the court could not adjudicate upon the legality of the order imposing penalty without deciding whether there was a valid assessment, for an order imposing penalty predicates a valid assessment. We have reiterated this view in Commissioner of Income-tax v. Raja Reddy Mallaram in considering the application of section 44 of the Indian Income-tax Act in relation to the assessment of an association of persons which is dissolved.

7. Mr. Pathak for the appellant urged (and that was the only argument advanced in support of the appeal) that the notice addressed by the Income-tax Officer to the respondent was in law inoperative, since section 44 applies in relation to a firm only when there is discontinuance of its business and not when there is dissolution of the firm. Counsel submitted that members of an association of persons may be assessed under section 44 on discontinuance of business or upon dissolution of the association, but partners of a firm may be assessed under section 44 only on discontinuance of the business and dissolution of a firm are different concepts, urged counsel, for if discontinuance included dissolution it was plainly unnecessary to make an express provision with respect to the dissolution of association of persons. In support of his contention counsel relied upon the observations made by Chakravartti C.J. in R. N. Bose v. Manindra Lal Goswami :

"That section [section 44 of the Income-tax Act, 1922] speaks of a case where any business, profession or vocation carried on by a firm or association or persons has been discontinued and a case where an association of persons is dissolved. It does not speak of a case, at least expressly, where a firm has been dissolved. It will be noticed that when speaking of the discontinuance of a business, profession or vocation, the section speaks of both a firm and an association of persons, but when speaking of dissolution, it drops the 'firm'... Mr. Meyer..... contended that discontinuance included dissolution. I am unable to accept that contention, because although the dissolution of a firm must involve discontinuance of its business the converse need not necessarily be true and a firm may conceivably continue to exist after deciding to discontinue its business as firms very often do for various purposes, such as collecting their debts."

8. But these observations were obiter, for, as observed by the learned Chief Justice, the parties before him had throughout proceeded on the footing that section 44 applied to the case of a dissolved firm, and he would also proceed on the assumption that section 44 applied to the case of a dissolved firm.

9. Section 44 operates in two classes of cases : where there is discontinuance of business, profession or vocation carried on by a firm or association, and where there is dissolution of an association. It follows that mere dissolution of a firm without discontinuance of the business will not attract the application of section 44 of the Act. It is only where there is discontinuance of business, whether as a result of dissolution or other cause, that the liability to assessment in respect of the income of the firm under section 44 arises. In the case of an association, discontinuance of business for whatever cause, and dissolution with or without discontinuance of business, will both attract section 44. The reason for this distinction appears from the scheme of the Income-tax Act in its relation to assessment of the income of a firm. A firm whether registered or unregistered is recognised under the Act as a unit of assessment (section 3 and 2 (2)), and its income is computed under clauses (3) and (4) of Section 23 as the income of any other unit. Section 25(1) relates to assessment in case of a discontinued business--whether the business is carried on by a firm or by any other person. This is of course only an enabling provision giving the Income-tax Officer an option to make a premature assessment on the profits earned upto the date of discontinuance, in the year of discontinuance: Commn of Income-tax v. Srinivasau . Even if no premature assess" ment is made, the assessment for the entire year will be on the income computed upto the date of discontinuance. Then there is the spe-cial provision relating to assessment when at the time of making an assessment it is found that a change has occurred in the constitution of a firm, or a firm has been newly constituted : S. 26(1). The date on which the change has occurred is immaterial : it may' be in the year of account, in the year of assessment or even after the close of the year of assessment. The Income tax Officer has under S. 26(1) to as-sess the firm as constituted at the time of mak-ing the assessment, but the income, profits and gains of the previous year, have for the pur-pose of inclusion in the total income of the partners, to be apportioned between the part ners who were entitled to receive the same. Sub-section (2) of S. 26 relates to assessment in the case of succession to a person (which expression includes a firm) carrying on a busi ness by another person in such capacity. These provisions have to be read with S. 44, for that section provides that in the case of discontinu ance of business of firm or of an association or dissolution of an association, liability to assess ment is under Ch. IV and all the provisions of Ch. IV, so far as may be, apply to such assessment.

10. Discontinuance of business has the same connotation in section 44 as it has in section 25 of the Act; it does not cover mere change in ownership or in the constitution of the unit of assessment. Section 44 is, therefore, attracted only when the business of a firm is discontinued, i.e., when there is complete cessation of the business and not when there is a change in the ownership of the firm, or in its constitution, because by reconstitution of the firm, no change is brought in the personality of the firm, and succession to the business and not discontinuance of the business results. Under the ordinary law governing partnerships, modification in the constitution of the firm in the absence of a special agreement to the contrary amounts to dissolution of the firm and reconstitution thereof, a firm at common law being a group of individuals who have agreed to share the profits of a business carried on by all or any of them acting for all, and supersession of the agreement brings about an end of the relation. But the Income-tax Act recognises a firm for purposes of assessment as a unit independent of the partners constitu ting it: it invests the firm with a personality which survives reconstitution, A firm discon tinuing its business may be assessed . in the manner provided by S. 25(1) in the year of account in which it discontinues its business:

it may also be assessed in the year of assess ment. In either case it is the assessment of the income of the firm. Where the firm is dis solved, but the business is not discontinued, there being change in the constitution of the firm, assessment has to be made under S. 26(1). and if there be succession to the business, as sessment has to be made under S. 26(2). The provisions relating to assessment on reconsti tuted or newly constituted firms, and on suc cession to the business are obligatory. There lore even when there is change in the owner ship of the business carried on by a firm on reconstitution or because of a new constitu tion, assessment must still be made upon the firm. When there is succession, the successor and the person succeeded have to be assessed each in respect of his actual share. This scheme of assessment furnishes the reason Tor omitting reference to dissolution of a firm from S. 44 when such dissolution is not accompanied by discontinuance of the business.

11. A firm after it has discontinued its business, whether it is dissolved or not, will therefore be assessed either under section 25 (1) prematurely, or in the year of assessment; in both cases the procedure of assessment is as under section 23 (3) and (4) supplemented by sub- section (5). Section 44 provides an added incident that all persons who were partners at the time of discontinuance are jointly and severally liable to pay the tax payable by the firm. Under section 23 (5) by the second proviso to clause (a) in the case of a registered firm the firm is liable to pay tax on the share of the income of a partner only in the case of a partner who is non-resident. On the discontinuance of the business of a firm, however, by section 44 a joint and several liability of all partners arises to pay tax due by the firm. Except the general provisions relating to premature assessment under section 25 (1) and assessment on succession under section 26 (2) there is, in the Act, no provision which imposes joint and several liability on members of an association of persons, on dissolution or discontinuance of business and that is presum ably the reason why S. 44 was enacted as it stood prior to its amendment in 1958. Absence of reference to dissolution of a firm (not result ing in discontinuance) in S. 44 was therefore a logical sequal to the provisions relating to assessment of firms contained in Ch. IY, espe cially Ss. 23(5), 25(1), 26(1) and (2).

12. Balmokand Radheshyam was an unregistered firm and by the discontinuance of the business it neither ceased to be liable to pay tax on the income earned by it, nor could a procedure different from the one prescribed under Chapter IV apply for the assessment of the income of that firm.

13. We may observe that we have proceeded to decide this case on the footing that the business of the firm was discontinued on the dissolution of the firm. It is however necessary once more to observe, as we did in C. A. Abraham's case, that the Income-tax Act provides a complete machinery for assessment of tax, and for relief in respect of improper or erroneous orders made by the revenue authorities. It is for the revenue authorities to ascertain the facts applicable to a particular situation, and to grant appropriate relief in the matter of assessment of tax. Resort to the High Court in exercise of its extraordinary jurisdiction conferred on recognised by the Constitution in matters relating to assessment, levy and collection of income-tax may be permitted only when questions of infringement of fundamental rights arise, or where on undisputed facts the taxing authorities are shown to have assumed jurisdiction which they do not possess. In attempting to bypass the provisions of the Income-tax Act by inviting the High Court to decide questions which are primarily within the jurisdiction of the Revenue Authorities, the party approaching the Court has often to ask

the Court to make assumptions of facts which remain to be investigated by the Revenue Authorities.

14. The appeal fails and is dismissed with costs.

15. Appeal dismissed.