

A COMMISSIONER OF INCOME-TAX, MADHYA PRADESH

v.

DEWAS CINE CORPORATION

November 8, 1967

B [J. C. SHAH, V. RAMASWAMI AND V. BHARGAVA, JJ.]

Indian Income-tax Act, 1922, s. 10(2) (vii) 2nd proviso—Two persons entering into partnership, each contributing a cinema theatre—on dissolution of partnership theatres returned to respective owners at original price—Depreciation equally divided between partners—Return of theatres whether sale for purpose of s. 10(2)(vii), 2nd proviso.

C S and H formed a partnership to carry on business in partnership as exhibitors of cinematograph films with effect from March 1, 1947. Each partner who was an owner of a cinematograph theatre brought his theatre into the books of the partnership as an asset of the partnership. For the assessment years 1950-51 to 1952-53 the Income-tax Officer allowed depreciation aggregating to Rs. 44,380/- in respect of the two theatres. The partnership was dissolved on September 30, 1951, and on dissolution it was agreed between the partners that the theatres should be returned to their original owners. In the books of account maintained by the partnership, the assets were shown as taken over on October 1, 1951, at the original price less the depreciation allowed—the depreciation being equally divided between the two partners. In proceedings for assessment for the year 1952-53 the respondent was treated as a registered firm. The Appellate Tribunal held that by restoring the two theatres to the two original owners "there was a transfer by the firm and the entries adjusting the depreciation and writing off the assets at the original value amounted to total recoupment of the entire depreciation by the partnership and on that account" proviso 2 to s. 10(2)(vii) of the Income-tax Act, 1922, applied. The High Court, in reference, held in favour of the assessee. The Revenue appealed, contending, that on the transfer of the theatres from the partnership to the original owners there was a sale.

F HELD : The expressions "side" and "sold" are not defined in the Income-tax Act : Those expressions are used in s. 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 is it for a price. [176A-B]

G 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 where in satisfaction of the claim of the partner to his share in the value of the residue determined on the footing of an actual or notional sale property is allotted, the property so allotted to him cannot be deemed in law to be sold to him. [176E]

Addanki Naravanappa and Anr. v. Bhaskara Krishnappa and Ors. [1966] 3 S.C.R. 400, referred to.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 2163 of 1966.

H Appeal from the judgment and order dated April 15, 1964 of the Madhya Pradesh High Court in Misc. Civil Case No. 22 of 1963.

Niren De, Solicitor-General, S. K. Aiyar, R. N. Sachthey and S. P. Nayar, for the appellant. A

Naunir Lal and B. P. Singh, for the respondent.

The Judgment of the Court was delivered by

Shah, J. S. G. Sanghi and Hari Prasad entered into an agreement to carry on business in partnership as exhibitors of cinematograph films in the name and style of "Dewas Cine Corporation" with effect from March 1, 1947. Each partner who was an owner of a cinematograph theatre brought his theatre into the books of the partnership as an asset of the partnership. For the assessment years 1950-51 to 1952-53 the Income-tax Officer allowed depreciation aggregating to Rs. 44,380/- in respect of the two theatres. The partnership was dissolved on September 30, 1951, and on dissolution it was agreed between the partners, that the theatres should be returned to their original owners. In the books of account maintained by the partnership, the assets were shown as taken over on October 1, 1951 at the original price less the depreciation allowed—the depreciation being equally divided between the two partners. B
C
D

In proceedings for assessment for the year 1952-53 the respondent was treated as a registered firm. The Appellate Tribunal held that by restoring the two theatres to the two original owners "there was a transfer by the firm and the entries adjusting the depreciation and writing off the assets at the original value amounted to total recoupment of the entire depreciation by the partnership and on that account" proviso 2 to s. 10(2)(vii) of the Income-tax Act, 1922, applied. The High Court of Madhya Pradesh answered the following question referred to it by the Tribunal in the negative : E

"Whether on the facts and in the circumstances of the case, the amount of Rs. 44,380/- was rightly included in the total income of the assessee in the year 1952-53 under the second proviso to s. 10(2)(vii) of the Income-tax Act?" F

The Commissioner of Income-tax has appealed to this Court with certificate granted by the High Court. G

Section 10(2) of the Income-tax Act permits certain allowances to be debited in the computation of profits or gains of the business, profession or vocation carried on by the assessee in the year of account; one such allowance is prescribed by cl. (vii), the material part of which is : H

"in respect of any such building, machinery or plant which has been sold or discarded or demolished or des-

- A troyed, the amount by which the written down value thereof exceeds the amount for which the building, machinery or plant, as the case may be, is actually sold or its scrap value :

Provided that

- B Provided further that where the amount for which any such building, machinery or plant is sold, whether during the continuance of the business or after the cessation thereof, exceeds the written down value, so much of the excess as does not exceed the difference between the original cost and the written down value shall be deemed to be profits of the previous year in which the sale took place :"
- C

- D In respect of each of the theatres depreciation was allowed by the taxing authorities in proceedings for assessment. The Income-tax Appellate Tribunal was of the view that since the theatres were returned to the partners in settling the accounts of the partners on dissolution, the theatres were in law sold to the partners. The High Court disagreed with that view.

- E Under the Partnership Act, 1932, property which is brought into the partnership by the partners when it is formed or which may be acquired in the course of the business becomes the property of the partnership and a partner is, subject to any special agreement between the partners, entitled upon dissolution to a share in the money representing the value of the property. When the two partners brought in the theatres of their respective ownership into the partnership, the theatres must be deemed to have become the property of the partnership. Under s. 46 of the Partnership Act, 1932, on the dissolution of the firm every partner or his representative is entitled, as against all the other partners or their representatives, to have the property of the firm applied in payment of the debts and liabilities of the firm, and to have the surplus distributed among the partners or their representatives according to their rights. Section 48 of the Partnership Act provides for the mode of settlement of accounts between the partners. It prescribes the sequence in which the various outgoings are to be applied and the residue remaining is to be divided between the partners. The distribution of surplus is for the purpose of adjustment of the rights of the partners in the assets of the partnership; it does not amount to transfer of assets.
- F
- G

- H 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 share in the residue. The expressions "sale" and "sold" are not defined in the Income-tax Act; those expressions are used in s. 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.

The Solicitor-General appearing for the Revenue submitted that each partner is entitled to have the assets of the partnership sold for discharging the debts and obligations of the partnership, and for the purpose of dividing the residue among the partners if property is allotted to the partners in satisfaction of their claims. the transaction must be deemed in law to take the form of a notional sale of the property to the partner in consideration of the money value of his share. Counsel relied upon the statement of the law in *Lindley on Partnership*, 12th Edn., at p. 568 :

".....in the absence of a special agreement to the contrary, the right of each partner on a dissolution is to have the partnership property converted into money by a sale, even although a sale may not be necessary for the payment of debts.",

and also upon the decision of this Court in *Addanki Narayanappa and another v. Bhaskara Krishnappa and others*⁽¹⁾. 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 where in satisfaction of the claim of the partner to his share in the value of the residue determined on the footing of an actual or notional sale property is allotted, the property so allotted to him cannot be deemed in law to be sold to him.

The High Court was, therefore, in our judgment, right in deciding the question referred in favour of the assessee. The appeal fails and is dismissed with costs.

G.C.

Appeal dismissed.

(1) [1966] 3 S.C.R. 400.