INCOME-TAX REFERENCE.

Before Rankin C. J., C. C. Ghose and Buckland JJ.

1930 Dec. 9; 1931 Jan. 15.

In re NEEMCHAND DAGA.*

Income-tax—Double assessment for firms—Income that has escaped assessment—Proceedings against firm time-barred—Individual partners, if assessable—Indian Income-tax Act (XI of 1922), ss. 14 (2) (b), 34.

While both firms and individuals are liable to income-tax, clause (*b*) of sub-section (*2*) of section 14 of the Income-tax Act exempts the individual from payment in respect of certain profits as soon as those profits are, in the hands of the firm, assessed, but it does not exempt him at all in respect of profits which have not been assessed. But there is nothing in the Act to say that the firm is to be assessed first, still less that the assessment on the firm is to operate as a sort of estoppel in favour of the individual partners.

By the registration of a firm, the partners secure that they cannot, in respect of super-tax, be exposed to double assessment at all and that in respect of income-tax they can only be exposed to it on certain definite terms. But the Act does not give the partner any right to double assessment, if assessment is made at all.

Assessment can be made under section 34 and tax levied upon a partner of the firm in respect of his share of profits which have escaped assessment, although proceedings under the section against the firm have failed for lack of jurisdiction and fresh proceedings are time-barred.

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The assessee is a partner in the registered firm of Dulichand Thanmal. The firm was assessed for the year 1927-28, but the Income-tax Officer did not levy tax upon the firm, but forthwith assessed and charged tax upon the partners, direct, on their respective shares in the firm's profits.

On the 13th December, 1927, the Commissioner of Income-tax transferred the assessment of the firm for the year 1928-29 to the file of a Special Income-tax Officer. He came to the conclusion that certain profits of the firm for the year 1927-28 had escaped assessment in the previous year and instituted proceedings against the firm under section 34 of the Act. On the 15th January, 1929, the Income-tax Officer, who had originally assessed the firm for 1927-28, served notice under section 22(*2*)

*Income-tax Reference, No. 11 of 1930, under section 66 (*2*) of the Indian Income-tax Act.

read with section 34 on the partners. On the 26th February, 1929, the Special Income-tax Officer reassessed the firm for the year 1927-28, at an enhanced figure.

Subsequently, there was a decision of the High Court that the appointment of the Special Income-tax Officer was without jurisdiction and, in consequence thereof, the assessments made by such officer were cancelled. By that time, the institution of proceedings under section 34 would have been out of time. Therefore, the Income-tax Officer concerned proceeded to complete proceedings instituted against individual partners.

Thereafter, the matter came up before the Commissioner in the usual course and the following questions were framed before him:—

1. Whether a partner can be assessed for his proportionate share in the income of the firm, of which he is a partner, when the firm itself had not been assessed and had no assessable income?

2. Whether a notice, which was issued proposing assessment of the income from business, can be made the basis for revising the assessment of income arising from a partnership concern?

3. Whether section 14(*2*)(*b*) has been rightly interpreted to impose liability on a partner, irrespective of all considerations of the assessability of the firm?

4. What is the legal procedure for assessing a partner of a registered firm? Has the procedure been correctly followed in this case as to make the assessment valid in the case?

The Commissioner for Income-tax redrafted the question and referred the question stated in the judgment.

L. P. E. Pugh (*Nogen Bose* with him) for the assessee. Where there is a registered firm, it is the assessee. The individual partner is liable to assessment with respect to his other income, but he cannot be assessed on his share of the profits of the firm. Once there is assessment against the firm, you

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cannot assess the individual. See section 14, sub-section (*2*). There cannot be one assessment against the firm and another against the partner with regard to his share of the profits of the firm.

The assessment being bad, as against the firm, due to the proceedings under section 34 being bad and out of time, it is not possible to assess the partner by a notice under section 34, although such notice may be in time as against him individually.

N. N. Sircar, Advocate-General (*Radhabinode Pal* with him), for the Income-tax Department. A person cannot escape assessment under the head of income from a registered firm, even if that is his only income. Section 3 makes it clear. And sub-section (*1*) of section 16 shows that he must include in his return the income which is exempted from assessment under sub-section (*2*) of section 14.

Payment of tax is not the same as assessment and the partner is merely exempted from payment. Whether the firm is registered, or not, makes no difference. The partner can claim exemption only as regards profits as have been assessed already.

Pugh, in reply. When the firm was assessed, the assessment was on the total income. That concludes the matter.

Cur. adv. vult.

RANKIN C. J. The assessee is one Neemchand Daga, who has a share of 3 annas 7 pies in the firm of Dulichand Thanmal, which is a registered firm within section 2(*14*) of the Income-tax Act.

For the year of assessment 1927-28, the firm was assessed at a certain figure, but, in order to obviate the necessity of refunds being made under section 48(*2*) of the Act, tax was charged against the individual partners directly upon their shares in the firm's profits. This is a considerate and convenient course and the partners did not object to it. Early in 1929, the Income-tax authorities, having discovered that certain profits of the firm had escaped assessment for the year 1927-28, a notice was issued to each

partner under section 34 of the Act within the time limited by that section. For reasons, which are explained in the case stated by the Income-tax Commissioner, although a similar notice was issued upon the registered firm, the Income-tax authorities are not now in a position to rely upon this notice. Hence arises the question which has been stated for the opinion of the Court:

"When part of the profits of a registered firm has escaped assessment, can assessment be made under section 34 and tax levied upon a partner of the firm in respect of his share of such part, when proceedings under the said section against the firm itself, in respect of the said part, have failed for lack of jurisdiction and fresh proceedings are time-barred ?"

In my opinion, the answer is in the affirmative. The Indian practice is to impose income-tax by the Finance Act of each year at certain graduated rates upon individuals and at the maximum rate upon registered firms. Super-tax is not imposed upon registered firms, but is imposed under certain conditions upon the individual partner, in respect of his total income, which includes his share of the firm's profits. The firm and the individual are each required to render a return of total income [section 22(*2*)], and may each be required to produce accounts or documents [section 22(*4*)]. In some cases, these returns have to be made to different Income-tax Officers and in different places of assessment. The object of the Act in treating the firm, in addition to the individual partners, as itself a subject liable to assessment is not to differentiate in respect of the ultimate liability to tax, between the partners in a firm and the sole owner of a business or other assessee. The method of double assessment is employed in the case of firms as a device in the nature of taxation at the source as distinguished from the method of deduction of tax at the source which is employed to collect tax upon salaries and interest on securities. The object of the double assessment to tax in the case of partners and their firm is not to get it often but to get it early and to make sure of getting it: "the simple and effective expedient of "taxing the profits where they are found" [as

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Viscount Cave said in another class of case: *Williams* v. *Singer* (1)] and at the earliest stage at which they can be found. Hence the provisions of section 48(*2*), as to refund of tax over-paid, and of section 14(*2*)(*b*), which bears directly on the present case and says that tax shall not be *payable* by an assessee in respect of such an amount of the profits and gains of any firm which have been assessed to income-tax as is proportionate to his share in the firm at the time of such assessment. To collect the tax effectively, without unnecessary inconvenience to the subject without inconsistency in result and without unnecessary duplication of work on the part of the Income-tax authorities, it is obvious that the profits of the registered firm should be ascertained as a whole before assessment is made upon the individual partners. But I can find nothing in the Act to say that the firm is to be assessed first, still less that the assessment on the firm is to operate as a sort of estoppel in favour of the individual partners. In clause (*b*) of section 14(*2*), the word is "have," not "has." The language of this clause may be compared with that of clause (*a*) of the same sub-section and that of the proviso to section 55. It seems to me to be free of any suggestion that the individual is never to be liable to pay on any portion of the profits of the firm. This clause applies to firms which are not registered as well as to those which are registered. While both firms and individuals are liable to the tax by the plain wording of the Finance Act, the clause exempts the individual from *payment* in respect of certain profits as soon as those profits are in the hands of the firm assessed, but it does not exempt him at all in respect of profits which have not been assessed. To be taxed at the source is a liability rather than a right and, in any case, a partner, whose firm had not declared certain profits, can hardly be heard to complain that the profits have not been assessed upon the firm, or to require that an order of assessment should first be made upon the

(1) (1920) 7 Tax Cas. 387, 411.

firm in order that he might get the benefit of clause (*b*) of section 14 (*2*). That clause confers a benefit upon the individual partner, but only in respect of tax upon certain profits. As tax is chargeable upon the whole of the firm's profits and as the whole of a partner's share in the firm's profits is included in his total income regardless of any stipulation between the partners restricting the amount of profits which any partner may withdraw from the firm or of the amount actually drawn by him, it may be just conceivable that to assess a partner directly upon his share of escaped profits results in some way to his disadvantage. I have no real belief in the existence of such cases, but if they do exist, they merely mean that it may be worth a partner's while to see that the firm declares the whole of its profits. When the firm is registered under the Income-tax Act and Rules, what rights under the Act accrue from registration and to whom? Do they include a right on the part of the individual partner to require that all the firm's profits shall be assessed upon the firm and that whether they be declared or concealed? It is only upon this footing that he can claim a right that no part of the firm's profits shall be assessed as his taxable income, and it seems to me to be a very curious implication to make in this Act. When a firm is registered, the firm, not the individual partners, becomes assessable to income-tax at the maximum rate. The firm and not the partners escapes super-tax. But the partners, as individuals, get certain rights while the registration stands and the Income-tax authorities cannot dispute the amount of the individual's share as shown in the document which they have accepted for registration. The tax paid by the firm is treated as paid on his account in respect of his share and he gets the right to a refund upon this footing [section 48 (*2*)]. He has secured to him by section 24 the right to set off his share of the firm's losses against other items of his individual income—again upon the footing that double assessment is only machinery for collection. In effect,

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by the registration of a firm, the partners secure that they cannot in respect of super-tax be *exposed* to double assessment at all and that, in respect of income-tax, they can only be *exposed* to it on certain definite terms. But it is another thing altogether to treat the Act as giving to the subject a right to double assessment, if assessment is to be made at all.

Whether a notice under section 34 was served upon the firm or not, a notice under that section would have to be served on the partner who is now before us to prevent him escaping payment of super-tax and to collect income-tax on his individual income at the higher rate appropriate to his true income. He is clearly a person liable to pay tax on income of his own which has escaped assessment. What answer has he to the Finance Act of 1927 which imposed these taxes upon him? In my opinion, he has none.

The question referred to us should be answered in the affirmative and the assessee must pay the costs of the Reference.

GHOSE J. I agree.

BUCKLAND J. I agree.

Attorney for assessee: *H. C. Banerji.*

Advocate for Income-tax Department: *Radhabinode Pal.*

S. M.