

**IN THE HIGH COURT OF KARNATAKA  
AT BANGALORE**

**ITA No.1305/2006**

**C/W**

**ITA Nos.1303/2006, 1301/2006, 1293/2006, 1288/2006, 1286/2006 And  
1290/2006**

**1) THE COMMISSIONER OF INCOME TAX  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**2) THE JOINT COMMISSIONER OF INCOME TAX, (ASSESSMENT)  
SPECIAL RANGE, NO 55/1, SHILPASHREE,  
VIDHYARANYA COMPLEX,  
VISHVESHWARANGAR, MYSORE**

**Vs**

**M/s MANGALORE GANESH BEEDI WORKS,  
VINOBA ROAD, MYSORE,  
NOW DISSOLVED: REPRESENTED BY  
SMT M MEMALATHA, EX-PARTNER,  
W/O SRI K RAGHUNATH SHENOY,  
R/A NO 2987/1, TEMPLE ROAD,  
V V MOHALLA, MYSORE - 570012**

**Appellant Rep by:** Sri E R Indra Kumar, Adv.

**Respondent Rep by:** Sri Kulkarni for M/s K R Prasad, Adv.

**ITA NO.1303/2006**

**1) THE COMMISSIONER OF INCOME TAX  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**2) THE JOINT COMMISSIONER OF INCOME TAX, (ASSESSMENT)  
SPECIAL RANGE, NO 55/1, SHILPASHREE,  
VIDHYARANYA COMPLEX,  
VISHVESHWARANGAR, MYSORE**

**Vs**

**M/s MANGALORE GANESH BEEDI WORKS  
VINOBA ROAD, MYSORE  
NOW DISSOLVED: REPRESENTED BY  
SMT PUSHPALATHA, EX-PARTNER,  
W/O SRI SUBRAYA BALIGA,  
R/A NO 37, GOKULAM ROAD,  
JAYALAKSHMIPURAM, MYSORE-570012**

**Appellant Rep by:** E R Indra Kumar, Adv.

**ITA NO 1301/2006**

**1) THE COMMISSIONER OF INCOME TAX  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX,  
VISHVESHWARANGAR, MYSORE**

**2) THE JOINT COMMISSIONER OF INCOME-TAX, (ASSESSMENT)  
SPECIAL RANGE, NO 55/1, SHILPASHREE,  
VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**Vs**

**M/s MANGALORE GANESH BEEDI WORKS  
VINOBA ROAD, MYSORE,  
NOW DISSOLVED: REPRESENTED BY  
SRI B RAGHURAMA PRABHU EX-PARTNER,  
S/O SRI B MUKUNDA PRABHU,  
R/A NO 2665, 3RD MAIN, V V MOHALLA, MYSORE 570002**

**Appellant Rep by:** E R Indra Kumar, Adv.

**ITA NO. 1293/2006**

**1) THE COMMISSIONER OF INCOME TAX  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**2) THE JOINT COMMISSIONER OF INCOME TAX, (ASSESSMENT)  
SPECIAL RANGE, NO 55/1, SHILPASHREE,  
VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**Vs**

**M/s MANGALORE GANESH BEEDI WORKS  
VINOBA ROAD, MYSORE  
NOW DISSOLVED: REPRESENTED BY  
SRI M VISHWANATHA RAO EX-PARTNER  
S/O SRI B MADHAVA SHENOI,  
R/A SHANTI PRASAD, NO CH 33,  
VANIVILAS ROAD, MSYORE-570004**

**Appellant Rep by:** E R Indra Kumar, Adv.

**ITA NO 1288/2006**

**1) THE COMMISSIONER OF INCOME TAX,  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**2) THE JOINT COMMISSIONER OF INCOME TAX, (ASSESSMENT)  
SPECIAL RANGE, NO 55/1, SHILPASHREE,  
VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**Vs**

**M/s MANGALORE GANESH BEEDI WORKS  
VINOBA ROAD, MYSORE  
NOW DISSOLVED: REPRESENTED BY  
SRI ANAND RAO EX-PARTNER**

**Appellant Rep by:** E R Indra Kumar, Adv.

**ITA NO.1286/2006**

**1) THE COMMISSIONER OF INCOME TAX  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX  
VISHVESHWARANAGAR, MYSORE**

**2) THE JOINT COMMISSIONER OF INCOME TAX, (ASSESSMENT)  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**Vs**

**M/s MANGALORE GANESH BEEDI WORKS  
VINOBA ROAD, MYSORE,  
NOW DISSOLVED: REPRESENTED BY  
SMT ARATHI SHENOY EX-PARTNER**

**Appellant Rep by:** E R Indra Kumar Adv.

**Respondents Rep by:** Sri Kulkarni for M/s K R Prasad, Adv.

**ITA NO. 1290/2006**

**1) THE COMMISSIONER OF INCOME TAX  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX  
VISHVESHWARANAGAR, MYSORE**

**2) THE JOINT COMMISSIONER OF INCOME TAX, (ASSESSMENT)  
NO 55/1, SHILPASHREE, VIDHYARANYA COMPLEX,  
VISHVESHWARANAGAR, MYSORE**

**Vs**

**M/s MANGALORE GANESH BEEDI WORKS  
VINOBA ROAD, MYSORE,  
NOW DISSOLVED: REPRESENTED BY  
SRI M VINODA RAO EX-PARTNER  
S/O SRI B MADHAVA SHENOI,  
R/A MADHAVA KRUPA, NO 883/1A,  
VANIVILAS ROAD, MYSORE - 570004**

**V G Sabhahit and B Manohar, JJ**

**Dated: December 23, 2010**

**JUDGEMENT**

These appeals u/s 260-A of the Income Tax Act, 1961, (hereinafter called as 'Act') are directed against the order dated 7.4.2006 wherein the Income Tax Appellate Tribunal has dismissed the appeals and cross objections filed by the parties.

2. These appeals have been admitted for consideration of the following substantial question of law as framed in ITA. No.1286/06:

(1) Whether the Tribunal was right in applying the decision rendered in ITA No.974/B/98 and in holding that the same is identical to the case on hand, when the assessment in the present case was made in the status of a firm, where as in the aforesaid appeal, assessment was made in the status of A.O.P.?

(2) Whether the Appellate Commissioner was right in holding that partnership deed dated 30.6.1982 came to be dissolved on 6.12.1987 by virtue of the order of this Court dated 14.6.1991, which continued up to 17.11.1994 till the assessment year 1995-96, without considering the legal evidence contrary on record?

(3) Whether the Appellate Commissioner was right in taking profit of the sale of the firm for the assessment year 1995-96 is not assessable to capital gains tax under section 45(1) or section 45(4) of the Income Tax Act?

3. The material facts of the case giving rise to the above said substantial questions of law are as follows:

In 1939, late S. Raghuram Prabhu Started the business of manufacturing beedies. Subsequently, his brogher-in-law, Sri Madhav Shenoy also joined him in the business as a partner and thus M/s. Mangalore Ganesha Beedi Works (for short 'MGBW'), the firm, came into existence with effect from 28.3.1940. Thereafter, the said firm was reconstituted from time to time. The last reconstitution of the firm was evidenced by a partnership deed dt.30.6.1982 and according to the averments made in the deed, the last reconstitution of the firm became effective from 6.6.1982 and according to the deed of partnership, the firm comprised of the following 13 partners.

Sl. No.	Name of the Partners	% age of share
01.	B Raghurama Prabhu	14.50%
02.	M Janardhana Rao	7.65%

03.	M Ananda Rao	7.65%
04.	M Vinoda Rao	7.50%
05.	M Pushpalatha w/o Subraya Baliga	12.50%
06.	Hemalatha w/o Raghunath Shenoy	12.50%
07.	M Suresh Rao	7.55%
08.	M Vishwanath Rao	7.55%
09.	M Ramanatha Rao	2.50%
10.	Jaganath Shenoy	2.50%
11.	Vatsala Shenoy	7.55%
12.	M Gopinath Shenoy	2.50%
13.	Arathi Shenoy D/o M Janardhana Rao	7.55%

4. Clause (3) of the partnership deed provided for the duration of the firm. This clause reads as under:

*"3. The duration of the Partnership shall be five years in the first instance: but by mutual agreement the parties hereto may extend the said duration. If during the subsistence of this Partnership any of the partners desire to retire from the partnership he or she can do so, if all the other partners agree to the said retirement. However, if all the other partners do not agree to the said retirement the partner intending to retire shall give six months notice in writing of his or her intention to retire and on expiration of the period of the said notice the said Partner shall cease to be a Partner and subject to para 14 infra from that date all his or her liabilities and rights as a Partner of the firm shall come to an end."*

5. Clause (16) of the partnership deed had made specific provisions for the manner in which the affairs of the firm were to be wound up after its dissolution. It reads as under:

*"16. If the Partnership is dissolved, the going concern carried on under the name of the Firm MANGALORE GANESH BEEDI WORKS and all the trade marks used in course of the said business by the said firm and under which the business of the Partnership is carried on shall vest in and belong to the Partner who offers and pays or two or more Partners who jointly offer and pay the highest price therefore as a single group at a sale to be then held as among the Partners shall be entitled to bid. the other Partners shall execute and complete in favour of the purchasing Partner or Partners at his/her or their expense all such deed instruments and applications and otherwise aid him/her or them for the registration his/her name or their names of all the said trade marks and do all such deed, acts and transactions as are incidental or necessary to the said transferee or assignee Partner or Partners."*

6. Pursuant to Clause 3 of the Partnership Deed, the Partnership was dissolved by efflux of time on 5.6.1987, but because of the mutual agreement among the partners as provided in clause (3) itself the duration was extended for a further period of six months i.e., upto 5.12.1987 and therefore the firms stood dissolved with effect from 6.12.1987. Thereafter, the affairs of the firm had to be wound up

after its dissolution under Clause 16 of the Partnership Deed as referred to above. However, because of the difference of opinion among the erstwhile partners the affairs of the firm could not be wound up. Therefore, two of the partners of the firm filed a petition before this court under the provisions of Part X of the Companies Act, 1956, for winding up of the affairs of the firm in terms of Section 583 (4)(a) thereof. This petition was registered as Co P.1/1988. In the said petition by order dated 5.5.11. 1988, this court permitted the group of partners (7) having controlling interest to continue the business as an interim arrangement till the completion of winding up proceedings. However, subsequently by order dated 14.6.1991, in modification of the earlier order framed the scheme for winding up of the affairs of the firm by selling its assets as a going concern. Paragraph 29 of the order contains the scheme Clauses (i), (iii) and (v) of this scheme are reproduced hereunder.

*"(i) The dissolved partnership firm-Mangalore Ganesh beedi works as a going concern shall be sold to such of its partners who makes an offer of highest price, the same not being less than the minimum (reserved) price of Rs.30 crores (Rs. Thirty crores) within 11.7.1991 accepting further liability to pay interest at 15% per annum towards the amount of the price payable to partner/s from 6.12.1987 till the date of deposit.*

*(ii) \*\* \*\* \*\* \*\**

*(iii) If no offer for purchase of the dissolved partnership form as a going concern, adverted to in clause (ii) above, is received within the stipulated time or if any of the offers made by the partner/s is not accepted by the court, the Official Liquidator shall invite offers for purchase of the dissolved partnership firm as a going concern from the public including the partners by giving publicity in three consecutive issues of two English daily national newspapers which have wide circulation in the country and one Kannada daily newspaper having wide circulation in karnataka the time allowed for making offers being at least 45 days between the last publication and the date fixed for receipt of the offers.....*

*(iv) \*\* \*\* \*\* \*\**

*(v) If the sale of the dissolved partnership firm as a going concern in favour of any partner or partners or an outsider is accepted by the Court, such offerer shall, within 60 days from the date of the acceptance of the offer, deposit with the Official Liquidator the price or such part of the price together with interest on the total amount of the price at 15% per annum from 6.12.1987 till the date of deposit, which may become liable to be paid to the partner or partners towards their share of the price in the partnership firm together with interest on such amount: "*

7. The above said scheme was assailed by some of the partners before the Hon'ble supreme court in special Leave Petition in SLP 10680/1991 which was ultimately dismissed as withdrawn in 1994. In response to the scheme framed by this court by order dated 14.6.1991 several partners either individually or in groups offered their bids. The bid offered by an association of persons comprised of three partners namely M. Vishwanath Rao, M Jaganath Shenoy and M Gopinath shenoy (hereinafter referred to as the 'AOP-3') was found to be the highest being of Rs.92 crores and the same was accepted by this court vide its order dated 21.9.1994 and the following order as passed on the said day:

"The highest bid amount of Rs. Ninety two crores is accepted and the group of persons offering the said amount are directed to deposit within 60 days from today with the Official Liquidator the entire amount of ninety two crores together with actual profits earned from 6.12.1987 till 31.3.1994 and proportionate profit from 1.4.1994 till the date of deposit in terms of the orders of this Court earlier issued in C.A.No.313/1994."

8. At the instance of the three partners offering highest bid. Clause (1) of the order defendant 21.9.1994 was amended by a subsequent order defendant 19.9.1994. The modified clause (1) of the order defendant 21.9.1994 read as under:

"The highest bid amount of Rs. ninety two crores is accepted and the group of partners offering the said amount are directed to deposit that part of the bid amount of rupees ninety two crores which is proportionate to the shares held by the outgoing partners together with profits on the same basis from 8.12.1987 till the date of deposit, within a period of 60 days from 29.9.1994 in any of the nationalised banks in the name of the Official Liquidator. The rest of our order defendant 21.9.1994 remains in tact."

9. The value of Rs.92 crores for which the assets of the going concern MGBW were purchased by the erstwhile 3 partners was accepted and final order was passed as referred to above. The said transaction was not shown in the return filed by the Association of persons and right from the beginning the assessee had taken a stand that they are not liable to pay on capital gain on account of the sale consideration received and therefore notice was issued to the partners of the firm MGBW and the assessee filed the reply and did not show any additional return as according to them they were not liable to assessment as the firm had dissolved on 6.12.1987 itself and was not in existence thereafter and that in pursuance of the order passed by the High Court the business was being done by the erstwhile partners and returns were being filed by Association of Persons (erstwhile partners) and the profit was accounted and depreciation was claimed. However, the firm was dissolved on 6.12.1987 itself and it was not in existence on 17.11.1994 when the assets of the going concern MGBW was sold. However, the Assessing Officer held that the outgoing persons who have received the payment of the value of the assets of the firm are liable to pay capital gain. Since the firm had distributed the amount that was deposited he made an order of protective assessment against the firm also holding that all the partners of the erstwhile firm-MGBW are jointly and severally liable to pay the tax payable on the amount received by them by way of capital gain. The Assessing Officer by his order dated 31.5.1999 ordered that the partners of the going concern would be liable to tax on capital gain u/s 45(1) and in the present case since the quantum has been distributed among the partners Section 45(4) is squarely applicable and accordingly held that since the matter is pending before the ITAT and since there has been confusion regarding the status and also since the department has a right to assess the income in the hands of the correct assessee the protective order was passed against MGBW represented by its erstwhile partners and it was held that all the erstwhile partners are jointly and severally liable for the amount of tax payable u/s 45(4) of the Act. Being aggrieved by the said order passed by the Assessment Officer the erstwhile partners who were imposed tax by admitting the capital gain as taxable on the firm u/s 45 (4) of the Act, preferred appeal before the Commissioner of Income Tax (Appeals)-III, Bangalore and the Appellate Authority reversed the finding of the Assessing Officer and held that the out going partners of MGBW are liable to pay capital gain u/s 45(1). However, the

firm M/s. MGBW has been dissolved with effect from 6.12.1987 and the firm was not in existence during the previous assessment year 1994-95 and the relevant assessment year 1995-96 and accordingly cancelled the order of assessment dated 31.5.1999 and accordingly allowed the appeal. Being aggrieved by the order passed by the first appellate authority the Revenue preferred the appeal Nos.466 to 471, 473 to 475 and 477/Bang/2000 before the Income Tax Appellate Tribunal (hereinafter called ITAT) and ITAT by order dated 7.4.2006 confirmed the order passed by the first Appellate Authority commissioner of Income tax by holding that the MGBW was dissolved with effect from 6.12.1987 and the firm was not in existence during the relevant assessment year 1995-96 and the Tribunal in ITAT 974/Bang/98 has held that the order passed by the first Appellate Authority is justified and accordingly dismissed the appeals filed by the erstwhile partners. Being aggrieved by the above said order of the ITAT, these appeals are filed by the Revenue.

10. We have heard learned senior counsel appearing for the appellants and the learned counsel appearing for the respondent.

11. Learned counsel appearing for the appellants submitted that the protective order was passed against the firm and in view of the fact that the matter was pending before the ITAT as to whether the liability to pay tax on capital gain would be on the firm or individual partners the Assessing Officer had passed the protective order against the firm also and the ITAT held that the individual partners would be liable to pay tax on capital gain as firm has ceased to exist during the assessment year 1995-96. The said order passed by the ITAT was challenged before this court in ITA No.134/2000, 135/2000, 136/2000, 137/2000, 138/2000, 139/2000, 140/2000, 144/2000, 147/2000 and 146/2000 and therefore these appeals are filed by the revenue.

12. Learned counsel for the respondent-assessee submitted that since the order passed by the ITAT is in consonance with the order passed earlier in the appeals which were pending consideration in ITA Nos.134/2000, 135/2000, 136/2000, 137/2000, 138/2000, 139/2000, 140/2000, 144/2000, 147/2000 and 146/2000, therefore these appeals are liable to be dismissed.

13. We have given careful consideration to the contention of the learned counsel appearing for the parties.

14. It is clear from the material on record that the Assessing Officer held that the income which was received by accepting the highest bid of Rs.92 crores was paid to the erstwhile 9 partners and highest bid was offered by erstwhile 3 partners and it is also clear that the firm M/s.MGBW had dissolved on 6.12.1987 itself and it was not in existence thereafter and returns were being filed by the erstwhile partners in view of the direction issued by this court in the Company Petition as referred to above and the Assessing Officer has passed an order of protective assessment against the firm represented by its partners. This Court while considering the appeal in ITA Nos.134/2000, 135/2000, 136/2000, 137/2000, 138/2000, 139/2000, 140/2000, 144/2000, 147/2000, and 146/2000, disposed of by separate order today has held that the firm-MGBW was dissolved on 6.12.1987 and that the outgoing partners of the firm are liable for capital gain u/s 45(1) of the Act and not the firm and in view of the said findings thereunder which are disposed of by a separate order in ITA Nos.134/2000, 135/2000, 136/2000, 137/2000, 138/2000, 139/2000, 140/2000,



144/2000, 147/2000 and 146/2000, we hold that the order passed by the ITAT is justified and does not call for interference in those appeals. Accordingly, we answer the substantial questions of law against the revenue and in favour of the assessee and pass the following order:

ITA Nos.1305/2006, 1303/2006, 1301/2006, 12293/2006, 1288/2006, 1286/2006 and 1290/06 are dismissed.