IN THE HIGH COURT OF JUDICATURE AT PATNA

Miscellaneous Appeal No.433 of 2004

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1. Commissioner of Income Tax-I, Patna
2. Income-tax Officer, Ward (1), Gaya

.... Appellants

Versus

M/S Anurag Rice Mills, Navi Nagar, Aurangabad, Gaya, Bihar

.... Respondent

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Appearance :

For the Appellant/s : Mrs. Archana Sinha
Mrs. Vijay Lakshmi Srivastava
Mr.Alok Kumar

For the Respondent/s : Mr. Rohitabh Das
Dr. R. Usha

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CORAM: HONOURABLE MR. JUSTICE RAMESH KUMAR DATTA
and
HONOURABLE JUSTICE SMT. ANJANA MISHRA

ORAL JUDGMENT

(Per: HONOURABLE MR. JUSTICE RAMESH KUMAR DATTA)

Date: 03-09-2015

Heard learned counsel for the appellants and learned counsel for the respondent.

The appeal has been filed against the order dated 21.05.2004 passed by the Income-tax Appellate Tribunal, Patna Bench, Patna, in I.T.A. No.26/PAT/2002 for the assessment year 1991-92, by which the appeal of the assessee has been allowed setting aside the addition made in the hands of the firm with regard to the amounts related to capital account of the partners in the books of the firm.

The facts of the case noted by the CIT appeal while confirming the order of the Assessing Officer are that the return in question was the first return filed by the partnership firm, by which it claimed the availability of opening capital by three partners aggregating to Rs. 2,67,789/- and additional capital brought in was shown as Rs. 5,55,000/- which was paid through gift/loan. The said gift/loan amounts have been received all in cash for the period 1986-87 and 1987-88. The partners of the partnership firm had also filed their income-tax returns for the assessment years up to 1991-1992 and those had been assessed under Section 143 (1) of the Act. However, the said amounts having been disbelieved by the Assessing Officer, were assessed as income of the firm under the provisions of Section 68 of the Income-tax Act. The assessee filed an appeal before the CIT (Appeal) who rejected the same by order dated 21.11.2001, against which the assessee filed a further appeal before the Income-tax Appellate Tribunal, Patna Bench, Patna which by its impugned order dated 21.5.2004 allowed the appeal relying upon a decision of the Madhya Pradesh High Court in the case of CIT vs. Metachem Industries: (2000) 245 ITR 160 and held that the amount should not have been added in the hands of the Firm and the Assessing Officer should have considered adding the amount in the hands of the partners and since that has not been done, the Tribunal has no any hesitation in deleting the addition.

Learned counsel for the Revenue-appellant has sought to rely upon a decision of this Court in the case of Commissioner of Income-tax vs. Anupam Udyog: (1983) 142 ITR 133, in which

Section 68 of the Income-tax Act, 1961 has been explained at page 137, which is quoted below:-

> "It is now well settled that there was no provision in the Indian I.T. Act, 1922 (hereinafter to be referred to as "the 1922 Act"), corresponding to this section. The section merely gives statutory recognition to the nature and source of cash credits where they stand in the assessee's account or in the account of a third party. The question of burden of proof cannot be made to depend exclusively upon the fact of a credit entry in the name of the assessee or in the name of a third party. In either case, the burden lies upon the assessee to explain the credit entry, though the onus might shift to the ITO under certain circumstances. Where, for instance, the assessee shows that entries regarding cash credits in a third party's account are genuine and the sums were in fact received from the third party as loans or deposits, he has discharged the onus; and in that case it is for the third party to explain the source of the moneys, and they cannot be charged as the assessee's income in the absence of any material to indicate that they belong to the assessee. These principles, which were well recognized by law under the 1922 Act, have not been

> altered by the introduction and insertion of s.68 of the Act. Nonetheless, there are two important departures from the law as it stood in the 1922 Act and that which stands after the insertion of s.68 of the Act.
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> And they are these: If there are cash credits in the books of a firm in the accounts of the individual partners and it is found as a fact that cash was received by the firm from its partners, then in the absence of any material to indicate that they are the profits of the firm, they cannot be assessed in the hands of the firm, though they may be assessed in the hands of the individual partners."

This Court while admitting the matter for hearing has framed the following substantial question of law on which the appeal was to be heard:-

> "Whether the order of the Tribunal deleting the addition of Rs.8,72,789/- in hands of the firm is legal and valid specially in view of the decisions of the Hon'ble Patna High Court in the case of Anupam Udyog reported in 142 ITR page-133."

Learned counsel for the appellants submits that in view of the provisions of Section 68 which have been interpreted in the aforesaid decision of the Patna High Court, there was nothing wrong in the decision of the Assessing Officer and the CIT appeal, including the aforesaid amount as income of the assessee partnership firm since the partner on enquiry had failed to show the source of such funds.

On the other hand, learned counsel for the respondent-assessee submits that the decision in the case of Anupam Udyog (supra) supports the stand of the respondent and since admittedly this was a first return filed by the firm and the amounts are shown to have been brought in by the partners of the firm, they could not be treated as the income of the firm itself and the Tribunal had rightly held that if at all the said amounts could not be explained then the assessment could only be made on the partners and not on the firm.

In support of the same, learned counsel for the respondent relies upon another decision of the Andhra Pradesh High Court in the case of Commissioner of Income Tax-2 vs. M/s. M. Venkateswara Rao & others dated 27th August, 2014 in I.T.T.A. No.29 of 2003, in which relying upon the aforesaid decision of the Patna High Court in Anupam Udyog's case (supra), it has been held as follows:-

> "…..It is a matter of record that the respondent-firm comprises of ten partners and each of them made contributions, be it in the form of cash or bank guarantees to be furnished to the Government, at the commencement of business. The returns submitted by the respondent-firm were processed, and the facts and

figures furnished by it were accepted. However, the matter was reopened at a later point of time. The Assessing Officer treated the capital raised by the firm in the form of contributions made by the partners as income. This conclusion was arrived at on the ground that source of income for the partners was not explained. Learned counsel for the appellant placed reliance upon the judgment of the Patna High Court in Commissioner of Income Tax vs. Anupam Udyog. The Tribunal rested its conclusions upon the judgment of the Bombay High Court in Narayandas Kedarnath vs. Commissioner of Income Tax and that of Allahabad High Court in Commissioner of Income Tax vs. Jaiswal Motor Finance.

Section 68 of the Act no doubt directs that if an assessee fails to explain the nature and source of credit entered in the books of account of any previous year, the same can be treated as income. In this case, the amount, that is sought to be treated as income of the firm, is the contribution made by the partners, to the capital. In a way, the amount so contributed constitutes the very substratum for the business of the firm. It is difficult to treat the pooling of such capital, as credit. It is only when the entries are made during the course of business that can be subjected to scrutiny under Section 68 of the Act. Even otherwise, it is evident that the respondent explained the amount of Rs.76,57,263/- as the contribution from its partners. That must result in a situation, where Section 68 of the Act can no longer be pressed into service. However, in the name of causing verification under Section 68 of the Act, the Assessing Officer has proceeded to identify the source for the respective partners, to make that contribution. Such an enquiry can, at the most be conducted against the individual partners. If the partner is an assessee, the concerned Assessing Officer can require him to explain the source of the money contributed by him to the firm. If on the other hand, the partner is not an assessee, he can be required to file a return and explain the source. Undertaking of such an exercise, vis-à-vis the partnership firm itself, is impermissible in law. In the judgment relied upon by the appellant itself, the Patna High Court held as under:

If there are cash credits in the books of a firm in the accounts of the individual partners and it is found as a fact that cash was received by the firm from its

> partners, then in the absence of any material to indicate that they are the profits of the firm, they cannot be assessed in the hands of the firm, though they may be assessed in the hands of the individual partners. Cash credits in the individual accounts of members of a joint family with third party cannot be assessed as the income of the family unless the Department discharges the burden of proof to the contrary.
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> Therefore, the view taken by the Assessing Officer that the partnership firm must explain the source of income for the partners regarding the amount contributed by them towards capital of the firm cannot be sustained in law….."

On a consideration of the submissions of learned counsels for the parties, we are of the view that the decision of this Court in the case of Anupam Udyog (supra) as a matter of fact is against the Revenue and does not support its stand. Undoubtedly, it is a case of a first return by the assessee firm and the amounts in question had been brought in by the partners.

In the present matter, the partners were also assessees and had been summarily assessed under Section 143 (1) of the Act for several years prior to the assessment year 1991-92. They have brought in the said amount to be included as a capital to the firm. Evidently, it is for the partner to explain the source of the said funds and it was not open to the Assessing Officer to have treated the said amounts as income of the firm as there was no business of the firm to carry forward such income, and it was not in dispute that the amounts had been brought in by the partners into the firm.

In the said circumstances, the Tribunal has rightly held that if at all the assessments had to be made, they may be of the partners of the firm and not the firm itself and such amounts could not have been treated as income of the firm by relying upon Section 68 of the Act.

For the aforesaid reasons, we are of the opinion that the impugned order of the Tribunal is legal and valid.

The appeal is, accordingly, dismissed.

V.P.Sinha/-

(Ramesh Kumar Datta, J)

(Anjana Mishra, J)

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