WWW.LIVELAW.IN

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

R/SPECIAL CIVIL APPLICATION NO. 17915 of 2018

==========

MAMTA BHAVESH DAVE

Versus

INCOME TAX OFFICER, WARD 3, GANDHINAGAR

==========

Appearance:
MR B S SOPARKAR(6851) for the Petitioner(s) No. 1
M R BHATT & CO.(5953) for the Respondent(s) No. 1

==========

CORAM: HONOURABLE MR. JUSTICE J.B.PARDIWALA
and
HONOURABLE MS. JUSTICE NISHA M. THAKORE

Date : 18/01/2022

ORAL ORDER

(PER : HONOURABLE MR. JUSTICE J.B.PARDIWALA)

1. Draft amendment is allowed. Necessary incorporation shall be carried out by today itself.

2. By this writ application under Article 226 of the Constitution of India, the writ applicant/an assessee seeks to challenge the Notice issued by the Income Tax Department dated 31.03.2018 under Section 148 of the Income Tax Act, 1961 (for short 'the Act, 1961) for reopening of the assessment under Section 147 of the Act with respect to A.Y. 2011-12.

3. It appears from the reasons recorded by the Income Tax Officer that the department intends to reopen the assessment on the ground that the writ applicant herein as one of the partners of the partnership firm, failed to show the remuneration and interest received from the partnership firm when the return of the writ applicant was processed under

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

Section 143(1) of the Act on 06.03.2012. The case of the department is that the total remuneration and interest paid is to the tune of Rs.75,11,147/-. Each of the partners have a share of 50% in the partnership firm. The writ applicant herein has been shown as a “Working Partner”. The writ applicant filed her objections dated 28.10.2018 pointing out that she had not received any income in the form of remuneration and interest from the partnership firm and therefore, there was no question of adding some income or showing such income in the return of income.

4. The objections raised by the writ applicant came to be disposed of vide the order dated 01.11.2018 on the ground that the writ applicant/assessee had received share of profit from the firm and such share received by the writ applicant/assessee as per the partnership deed would include the remuneration and interest which has not been debited from the profit and loss account of the firm.

5. We have heard Mr. Bandish Soparkar, the learned counsel appearing for the writ applicant and Mr. M.R. Bhatt, the learned Senior Counsel appearing for the Revenue.

6. Mr. Soparkar, pointed out that the department also thought fit to proceed against the partnership firm and restricted the deduction under Section 10A by applying the provisions of Section 10A read with Section 80-IA(8) and 80-IA(10) of the Act.

7. It appears that the partnership firm challenged the order passed by the CIT(A) by filing an appeal before the Income Tax Appellate Tribunal. The Income Tax Appellate Tribunal allowed

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

the appeal holding as under:

> *"8. We have heard the rival contentions and perused the materials available on record. The controversy in the case before us relates to the deduction of remuneration/interest on partner's capital not claimed by the assessee in its profit and loss account. The fact is that there was a specific clause in the deed of partnership. Therefore, the deduction for the remuneration/ interest on capital was made by the AO which was subsequently confirmed by the ld. CIT(A) with the direction to allow the claim of deduction to the firm for the remuneration/interest on capital but tax the same in the hands of the partners of the firm.*
>
> *8.1 It is an undisputed fact that the deed of partnership requires a partner to claim the deduction for the remuneration and the interest on capital. The dispute arises whether the clause mentioned in the deed of partnership is compulsory/mandatory on the part of the assessee.*
>
> *8.2 The partnership firm comes into existence with mutual understanding between the persons. These understanding can be reduced in writing or without in writing the same. Thus, it is clear that it is not necessary to execute the deed of partnership in writing. However, in the current scenario, it is not possible to work under the module of the partnership without executing the same in writing. It is because to run the business one needs to have a bank account, PAN, etc. which is not possible to obtain without having the deed of partnership in writing. Thus, the deed of the partnership will reveal the understanding on the basis of which partners agreed to work between them.*
>
> *From the above, it is clear that the clauses mentioned in the partnership deed are not mandatory but made to avoid any ambiguity and misunderstanding. As such, there is no dispute among the partners for not claiming the remuneration/interest of on capital in the profit and loss account of the firm. Therefore, in our considered view the conduct of the partners of the firm suggests that it was agreed not to claim any remuneration/interest on the capital account. In holding so, we find support and guidance from the order of Amritsar Tribunal in the case of ITO vs. Mala Tondon in ITA No.319/ASR/2010 vide order dated 14.06.2011 wherein it was held as under:*
>
> > *"6. We have heard both the parties and given our thoughtful consideration to the rival submissions, examined the facts of the case, evidence and material placed on record and also gone through the orders of the authorities below. A careful perusal of the impugned appellate order clearly reveals that the Ld. CIT(A), has considered and adjudicated the issue, in question, in greater detail. after appreciation of the evidences and material on record, as also the legal and factual position of the case. Needless to say that the impugned appellate order is well reasoned and based on the cogent and credible material and facts of the case. However, it would pertinent to reproduce the relevant part of the decision of the CIT(A), for the purpose of proper appreciation of the same:*
> >
> > *"3.4. I have considered the rival submissions carefully. An identical issue has been decided in the case of Rohit Tandon,*

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

husband of the appellant, the other partner in M/s. Dynamech holding 50% share in the partnership firm for the assessment year 2006-07. In that case also, the AO had added the interest payable on the capital of Sh. Rohit Tandon and remuneration payable to Sh. Rohit Tandon to the total income of the assessee, I have adjudicated that appeal vide order dated 14.7.2009 in appeal No.591/08-09/CIT(AV/Jal and have deleted similar additions as under:

"9.5 I have considered the rival submissions carefully. Clause 4 and 5 of the partnership deed providing for interest on capital and salary are as under:

"4. The capital of the partners is as per their respective accounts in the books of the partnership. The partners shall be entitled to interest on their capital 18% per annum or at such other rate or rates as the partners may at the end of each financial year mutually settled subject to the maximum amount admissible under the Income-tax Act, 1961.

5. Both the partners shall diligently attend to the business of the partnership and carry on the same for their greatest common advantage. Both the working partners shall be entitled to a remuneration of Rs.48,000/- per annum each or at such other rate or rates as the partners may at the end of each financial year, mutually settle subject to the maximum amount admissible under the Income-tax Act, 1961.

." 9.6. The aforesaid clauses of the partnership deed are clearly enabling clauses since the word used in both the clauses are "the partners shall be entitled...". This shows that the partners were entitled to get interest on the capital and to draw remuneration for their services without binding them to do so. This, in my opinion, is not a mandatory provision in the partnership deed which would be worded like the partners shall be provided/given... Further, it is also mentioned in both these clauses, that the rate or rates of interest and the remuneration would be mutually settled by the partners at the end of each financial year. Now, a partnership, by its very name and as per the provisions of Partnership Act is by will of the partners. There are only two partners in this firm. both having equal shares. The accounts drawn up at the end of the year reveal that no interest on the capital or remuneration to the partners has been provided in the accounts of the firmM/s.Dynamech. This act by itself signifies that the partners have agreed not to provide interest on their capital or to charge remuneration for their services. In my opinion, the terms of the partnership deed do not signify that interest on capital and remuneration to partners had necessarily to be provided in the account of M/s. Dynamech...

9.7. The AO has drawn support from the provisions of section 801A(10) This sub-section provides that where the affairs between the eligible business and any other person is so arranged that more than ordinary profits arise to the assessee, the AO shall, in computing the profit and gains of such an eligible profits for the purposes of deduction under this section, take the amount of profits as may be reasonably taken to have been derived therefrom. Thus sub-section has been made applicable to section 801B by virtue of sub-section (13) of section 80IB. However, this sub-section only enables, the AO to effect the profit of the undertaking claiming deduction u/s 801B, which is M/s. Dynamech in this case. This

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

does not enable the AO to alter the profits or the income of the other person referred to in this sub-section. It is a fact that the assessee has not received interest and remuneration from M/s. Dynamech. As noted earlier, the terms of partnership deed are not so worded so as to make payment of interest on capital and remuneration to partners as mandatory. It is also not rebutted by the AO that no interest or remuneration has been received by the appellant in earlier years also. This income has not accrued or arisen to the assessee. I therefore, hold that the AO was not justified in making the addition on account of interest on capital in M/s. Dynamech and remuneration receivable from M/s. Dynamech. This ground of appeal is allowed."

3.5. Following the decision in the case of Sh. Rohit Tandon (supra), ground No.3 of appeal is allowed."

6.1. In view of the above, we do not find any infirmity in the findings of the CITIA), as the same are based on proper appreciation of the legal and factual position of the case. Accordingly, this appeal of the revenue is dismissed."

From the above we note that it is not compulsory to claim the remuneration/interest on partner's capital account despite the fact there was a specific clause in the deed of partnership.

8.3 The next controversy arises in the case before us from the directions given by the ld. CIT(A) to tax the amount of remuneration/ interest on partner's capital account in the hands of the partners. It is a fact that the AO allowed the claim of the deduction for the remuneration/interest on partner's capital account in his computation of income. But the same was added back by the AO on the ground that it was not claimed as a deduction in the profit and loss account. However. the ld. CIT(A) directed to delete the addition made in the hands of the firm and further directed to tax the same in the hands of the partner of the firm.

8.4 From the preceding discussion, we note that there was no issue to tax the remuneration/interest on the capital in the hands of the partners. Thus, in our considered view ld. CIT(A) has exceeded his jurisdiction by giving direction to the AO for the dispute which is not arising from the order of the AO. In this regard, we find support and guidance from the order of this Tribunal in the case of Income Tax Officer vs. Biotech Ophthalmic Pvt. Ltd. reported in ITA No.443/Ahd/2011 vide order dated 31.08.2014 wherein it was held as under:

"9. The assessee has also moved a cross objection which seeks to expunge CIT(A)'s directions to bring this deemed dividend to tax in the hands of Shri Mehul P Asnani, director in assessee's company.

10. Learned counsel submits that while deciding appeal of the assessee before him, it was not open to the CIT(A) to give adjudication on taxability of this income in the hands of a person other than this assessee. He has clearly exceeded his jurisdiction in holding that the amount in question is taxable in the hands of Shri Mehul P Asnani. He urges us to expunge these observations. In support of his prayer. learned counsel for the assessee invites our attention to a decision of coordinate bench in the case of Jagat Minerals (P.) Ltd. v. Dy.

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

CIT [IT Appeal Nos 2110, 2403 and 2750/Ahd/11: dated 22.4.2015) whereby similar remarks made by the CIT(A) have been modified

11. Learned Departmental Representative, on the other hand, relies upon the stand taken by the CIT(A), He submits that when the impugned addition was deleted solely on the ground that it was required to be taxed in the hands of the director concerned, the CIT(A) was quite justified in directing the Assessing Officer to bring it to tax in the hands of that director.

12. We have heard the rival contentions, perused the material on record and duly considered facts of the case in the light of the applicable legal position.

13. In our considered view, it is important to first understand the role played by the findings or directions of this nature. We are dealing with the assessment year 2006-07 and the order of the CIT(A) was served on the Assessing Officer on 5th January 2011. Obviously, the assessment must have attained finality, by the time the Assessing Officer came to know of these directions, since in terms of Section 153(1) "no order of assessment shall be made under section 143 or section 144 at any time after the expiry of (a) two years from the end of the assessment year in which the income was first assessable; or (b) one year from the end of the financial year in which a return or a revised return relating to the assessment year commencing on the 1st day of April, 1988, or any earlier assessment year, is filed under sub-section (4) or sub-section (5) of section 139, whichever is later". No doubt, under section 153(2A), when an assessment is set aside or cancelled under section 250, 254, 263 or 264 a fresh assessment, as a result of such a cancellation, can be framed within one year from the end of the financial year in which the order under section 250 or section 254 is received by the Commissioner or the order under section 263 or section 264 is passed by the Commissioner. However, this provision comes into play only when the order passed under section 250, 254, 263 or 264 in the case of the assessee himself. That is not the situation that we are dealing with at present.

14. Section 153(3), dealing with the impact of the findings or direction given by the revisionary, appellate or judicial authorities, prescribes that "the provisions of inter alia section 151(1) "shall not apply to the ..... assessments, reassessments and recomputations which may, s bject to the provisions of sub-section (2A) be completed at any time where the assessment, reassessment or recomputation is made on the assessee or any person in consequence of or to give effect to any finding or direction contained in an order, under sections 250, 254, 260, 262, 263 or 264 1535 or in an order of any court in a proceeding otherwise than by way of appeal or reference under this Act". In other words, when effect of a finding or direction of an revisionary, appellate or judicial authority is to be given, that exercise can be carried out any point of time de hors the time limits specified in section 153(1). However, even this relaxation of time limits is subject to certain riders, including rider contained in Explanation 3 to Section 153(3) which provides that, where by a revisionary, appellate or judicial order of the above nature, an income is excluded from the income of one assessee and held to be income of the other assessee, the assessment of

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

such an income in the hands of another assessee "be deemed to be one made in consequence of or to give effect to any finding or direction contained in the said order, provided such other person was given an opportunity of being heard before the said order was passed (Emphasis by underling supplied by us)." Clearly, therefore, unless the person in whose hand income is directed to be added has been heard before such directions are issued, the directions issued by the revisionary, appellate or judicial authority are an exercise in futility. This rider equally relevant in respect of reopening of an assessment under section 154, as a result of the findings or directions of the revisionary, appellate or judicial authorities.

15. It is an position, on the facts of this case, that Shri Mehul P Asnani, in whose hands CIT(A) has directed this income to be added, has not been granted an opportunity of hearing by the CIT(A) before these directions were issued. Such being the admitted facts, it's beyond doubt that a completed assessment cannot be disturbed or reopened to give effect to such findings or directions.

16. There is, however, an even more fundamental issue, and that issue is whether the direction that the deemed dividend income being brought to tax in the hands of Shri Asnani is a direction necessary for the disposal of case. This issue assumes significance in view of the legal position that, as held by Hon'ble Supreme Court in the case of Rajinder Nath v. CIT [1979] 120 ITR 14/2 Taxman 204, "As regards the expression "direction" in s. 153(3)(ii) of the Act, it is now well settled that it must be an express direction necessary for the disposal of the case before the authority or Court. It must also be a direction which the authority or Court is empowered to give while deciding the case before it." Their Lordships then added that "The expressions "finding" and "direction" in s. 153(3)(ii) of the Act must be accordingly confined" and that "Sec 153(3) (ii) is not a provision enlarging the jurisdiction of the authority or Court."

17. As to what constitutes "an express direction necessary for disposal of a case", we find the following guidance from Their Lordships:

> *"To be a necessary finding, it must be directly involved in the disposal of the case. It is possible in certain cases that in order to render a finding in respect of A, a finding in respect of B may be called for. For instance, where the facts show that the income can belong either to A or B and no one else, a finding that it belongs to B or does not belong to B would be determinative of the issue whether it can be taxed as A's income. A finding respecting B is intimately involved as a step in the process of reaching the ultimate finding respecting A. If, however, the finding as to A's liability can be directly arrived at without necessitating a finding in respect of B, then a finding made in respect of B is an incidental finding only. It is not a finding necessary for the disposal of the case pertaining to A. The same principles seem to apply when the question is whether the income under enquiry is taxable in the assessment year under consideration or any other assessment year. As regards the expression "direction" in s. 153(3)(ii) of the Act, it is*

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

now well settled that it must be an express direction necessary for the disposal of the case before the authority or Court. It must also be a direction which the authority or Court is empowered to give while deciding the case before it."

18. Let us now, in the above light, revert to the facts of the case before us. The authorities below were dealing with a deeming fiction, i.e. deemed dividend, about an income. The case of the assessee was that this deeming fiction of deemed dividend could not be invoked in the present case because the assessee did not hold the shareholdings in the company which had extended loan to the assessee. This plea has been accepted by the CIT(A), but, for accepting such a plea, it is not a condition precedent that this deeming fiction must come into play in the hands of some other assessee other than this assessee. Whether the loan received by the assessee is held to be deemed dividend in the case of some other person or not is wholly irrelevant for deciding whether or not this is deemed dividend in the hands of this assessee or not. Learned CIT(A) holds that since Mehul P Asanai is a shareholder in the said company, the receipt can be added as deemed dividend in the hands of Mehul P Asnani, but then what he overlooks is that all the conditions precedent for taxing a receipt as deemed dividend are to be satisfied qua the assessee in whose income is to be taxed, and being a shareholder is only one such precondition. Learned CIT(A) has, as noted earlier in this order, observed that "If the recipient of loan is not a shareholder and the transaction is covered by this provision, the addition is to be made in the hands of the shareholder", but then it is difficult to comprehend as to how one can come to a conclusion that a transaction is covered by this provision, i.e. deeming fiction of the deemed dividend, without examining the transaction between the shareholder of the company and the company in which such shares are held. Without even giving a finding about satisfaction of all these conditions, learned CIT(A) proceeds to hold that it is an income to be taxed in the hands of the shareholder i.e. Mehul P Asnani. It is a classic case of putting cart before the horse and is wholly based on fallacious logic. The direction is thus not only unnecessary but patently incorrect. Viewed thus, the direction given by the CIT(A), for taxability of this deemed dividend in the hands of Shri Asnani, does not constitute "ant express direction necessary for disposal of a case". Nothing really turns on his direction, as such. Even if this direction was correct, learned CIT(A) had no business to give such a direction without affording an opportunity of hearing to the affected party and that too when it was absolutely necessary to decide the issue in appeal before him. There is a certain degree of restraint that is expected of the appellate authorities in discharge of their judicial functioning.

19. As we part with our adjudication on this issue, we may also take note of learned Departmental Representative's contention that the assessee has no locus standi to raise any grievance against these directions as he is not the aggrieved party vis-à-vis these directions. We are unable to see any merits in this plea either. The manner in which the appeal has been decided by the CIT(A) gives an impression, which is a wholly inappropriate impression and which has also been reiterated before us by the learned Departmental Representative, that the impugned additions have been

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

> *deleted in the hands of the assessee as these additions are required to be made in the hands of someone else.. The deletion of the impugned addition in the hands of the assessee company has been thus projected to be, though perhaps at a somewhat subliminal level, dependent of the addition being confirmed in the hands of the director. The directions given by the CIT(A) do prejudice. interests of the assessee inasmuch as these directions not being implemented may be viewed as detrimental to the interests of the assessee but then the directions suffer from legal infirmities, from glaring procedural flaws, and are incapable of being implemented anyway. In any case, since these directions are given in the case of this assessee and the appellate order by the CIT(A) in the case of this assessee cannot be challenged, in appeal before us, by a third party, the only way to prevent these directions reaching the finality is a challenge by this assessee himself, particularly because, as is the settled legal position, the statutory provisions are to be construed ut res magis valeat quam pereat i.e., in such a manner as to make it workable rather than redundant. The assessee before us, therefore, has, in our considered view, locus standi to challenge legality of these directions.*
>
> *20. In view of the above discussions, and bearing in mind entirety of the case, we vacate the directions in questions. The cross objection is thas allowed."*
>
> *In view of above, we hold that the ld. CIT(A) erred in directing the AO to tax the amount of remuneration and interest in the hands of the partner of the firm. Thus, we set aside the order of ld. CIT(A) and direct the AO to the addition in terms of the above. Thus, the ground of appeal of the assessee is allowed."*

8. Thus, the ITAT adjudicated the controversy as regards the deduction of remuneration/interest on the partners capital not claimed by the assessee i.e. the partnership firm in its profit and loss account. The Tribunal took notice of the fact that the CIT Appeals had directed to tax the amount of remuneration/interest on the partners capital account in the hands of the partners. The AO had allowed the claim of the deduction for the remuneration/interest on the partners capital account however, the same was added back by the AO on the ground that it was not claimed as a deduction in the profit and loss account. The CIT Appeals directed to delete the addition made in the hands of the firm and further directed to tax the same in the hands of the partner of the firm. The aforesaid was not approved by the Tribunal taking the view that there was no

Downloaded on : Tue Feb 01 19:33:18 IST 2022

WWW.LIVELAW.IN

good ground to tax the remuneration/interest on the capital in the hands of the partners and the CIT(Appeal) could be said to have exceeded its jurisdiction by issuing such directions to the AO for the dispute which was not arising from the order of the AO.

9. In view of such findings recorded by the Appellate Tribunal, nothing survives in the present matter so far as the reopening of the assessment of the partner of the partnership firm is concerned.

10. At this stage, Mr. Soparkar, pointed out that a Co-ordinate Bench of this Court while issuing Notice vide order dated 28.11.2018, had directed by way of ad-interim relief that the final order shall not be passed without the permission of the Court. However, the final order of assessment ultimately came to be passed. In such circumstances, the Co-ordinate Bench vide order dated 04.10.2021 directed that there shall be no coercive action inclusive of penalty in connection with the order of the assessment. In view of the aforesaid, even the final order of assessment will have to be quashed and set aside.

11. In the result, this writ application succeed and is hereby allowed. The impugned Notice dated 31.03.2018, Annexure – A to this writ application, is hereby quashed and set aside. The final order of assessment dated 25.09.2021 is also hereby quashed and set aside.

(J. B. PARDIWALA, J)

(NISHA M. THAKORE,J)

NEHA

Downloaded on : Tue Feb 01 19:33:18 IST 2022