

आयकर अपीलीय अधिकरण न्यायपीठ “एक-सदस्य” मामला रायपुर में

**IN THE INCOME TAX APPELLATE TRIBUNAL
RAIPUR BENCH “SMC”, RAIPUR**

**श्री रवीश सूद, न्यायिक सदस्य के समक्ष
BEFORE SHRI RAVISH SOOD, JUDICIAL MEMBER**

आयकर अपील सं./ITA No. 220/RPR/2018

निर्धारण वर्ष / Assessment Year : 2014-15

M/s. D.M Builders
3rd Floor, D.M Plaza,
Chhotapara, Raipur (C.G.)
PAN : AAGFD6481J

.....अपीलार्थी / Appellant

बनाम / V/s.

The Assistant Commissioner of Income Tax-4(1),
Raipur (C.G.).

.....प्रत्यर्थी / Respondent

Assessee by : Shri R.B Doshi, CA
Revenue by : Shri S.K Meena, Sr. DR

सुनवाई की तारीख / Date of Hearing : 23.12.2022

घोषणा की तारीख / Date of Pronouncement : 22.02.2023

आदेश / ORDER**PER RAVISH SOOD, JM**

The present appeal filed by the assessee is directed against the order passed by the CIT(Appeals)-II, Raipur dated 02.11.2018, which in turn arises from the order passed by the A.O under Sec. 143(3) of the Income-tax Act, 1961 (in short 'the Act') dated 29.12.2016 for the assessment year 2014-15. The assessee has assailed the impugned order on the following grounds of appeal:

“1. In the facts and circumstances of the case and in law, Ld. CIT(A) erred in upholding the action of the A.O of assessing the appellant in the status of “AOP” instead of “partnership firm” and in holding that the appellant is not a valid partnership firm. The appellant is liable to be assessed in the status of “partnership firm” and not as “AOP”.

2. The Assessing Officer erred in confirming the disallowance of Rs.13,19,518/- made by the A.O invoking Sec.14A, without appreciating the facts and the law properly. The disallowance u/s.14A made by the A.O and confirmed by the Ld. CIT(A) is arbitrary and not justified.

3. Ld. CIT(A) erred in not adjudicating upon ground no.3 taken by the appellant regarding disallowance of Rs.28,600/- on account of donation.

4. The appellant reserves the right to add, amend or modify any of the ground/s of appeal.”

2. Succinctly stated, the business premises of the assessee firm which is engaged in construction business was visited by the department u/s.133A of the Act on 09.04.2013. The assessee firm, thereafter, filed its return of income for A.Y.2014-15 on 15.10.2014,

declaring an income of Rs.69,310/-. Subsequently, the case of the assessee was selected for scrutiny assessment u/s.143(2) of the Act.

3. During the course of the assessment proceedings, it was observed by the A.O that the assessee firm was constituted vide a partnership deed dated 05.03.2009 comprising of four partners who represented their respective firms, as under:

- a. Shri Suresh Chandra Dayabhai Manik (Representative of a firm namely Manik Brothers Raipur)
- b. Shri Hemendra Kumar Dayabhai Manik (Representative of a firm namely M/s. Thackers H.P & Co, Raipur)
- c. Shri Paresh Kumar Dayabhai Manik (Representative of a firm namely M/s. Everest Leaves Co. Raipur)
- d. Shri Yogesh Kumar Dayabhai Manik (Representative of a firm namely M/s. Manik & Co.)

On a perusal of the records, it was observed by the A.O that each of the aforesaid partners was having 25% share in their representative capacity as a partner of their respective firms. Also, it was observed by the A.O that all the four partners had contributed the following properties by way of their capital contributions in the assessee firm on 05.03.2009, as under:

Sl. No.	Name	Location of land	Kasra No.	Area of Land	
				Hec.	Acre
1.	Suresh Chandra Dayabhai Manik (Representative of M/s. Manik	Rawabhata	405	0.263	0.650

	Brothers, Raipur)				
2.	Hemendra Kumar Dayabhai Manik (Representative of M/s. Thackers H.P & CO.)	Rawabhata	404/1 404/2 404/3 404/4 404/5	0.550	1.360
3.	Paresh Kumar Dayabhai Manik (Representative of M/s. Everest Leaves Co.)	Rawabhata	403	0.316	0.780
4.	Yogesh Kumar Dayabhai Manik (Representative of M/s. Manik & Company, Raipur)	Birgaon	65/3 65/8 65/4	0.259 0.270 0.135	0.650 0.670 0.330
			Total	1.793	4.440

Observing, that the aforesaid respective partnership firms had associated as partners in the assessee firm, the A.O on the basis of his conviction that a partnership firm could not be taken up as a partner, thus, called upon the assessee to explain as to why the assessment may not be framed in its hands by treating it as an Association of Person ("AOP"). In reply, it was claimed that as the assessee firm was established through a partnership deed which was duly registered with the Registrar of firms and societies, therefore, it was a validly constituted firm. However, the aforesaid reply did not find favour with the A.O who assessed the assessee firm in the status as that of an "AOP".

4. Also, the A.O in the course of the assessment proceedings observed, that though the assessee during the year under consideration had disclosed exempt dividend income of Rs.20,29,632/-, but it had on a suo-motto basis not offered any disallowance u/s.14A of the Act. On a perusal of the record, it was observed by the A.O that the assessee had raised a claim for deduction of interest expenditure of Rs.60,91,354/- in its profit & loss account on interest bearing borrowed funds, which, he was of the view could safely be related to its exempt income yielding investments in mutual funds. The A.O on the basis of his aforesaid observations worked out the disallowance u/s.14A at Rs.13,19,518/-, viz., (i) U/rule. 8D(2)(ii): Rs.12,50,745/-; and (ii) U/rule 8D(2)(iii) : Rs.68,773/-. The A.O further disallowed the assessee's claim for deduction of donation of Rs.28,600/-. Accordingly, the A.O vide his order passed u/s.143(3) of the Act dated 29.12.2016 assessed the income of the assessee firm in the status of an "AOP" at Rs.14,17,430/-.

5. Aggrieved, the assessee carried the matter in appeal before the CIT(Appeals) but without any success.

6. The assessee being aggrieved with the order of the CIT(Appeals) has carried the matter in appeal before me.

7. I have heard the ld. authorized representatives of both the parties, perused the orders of the lower authorities and the material available on record, as well as considered the judicial pronouncements that have been pressed into service by the Ld. A.R to drive home his contentions.

8. My indulgence in the present appeal has been sought for adjudicating three issues, viz. (i) sustainability of the framing of the assessment of the assessee firm in the status as that of an "AOP" by the A.O ; (ii) sustainability of the disallowance u/s.14A made by the AO; and (iii) disallowance of the assessee's claim for deduction of donation : Rs.28,600/-.

9. Ostensibly, the A.O drawing support from the judgment of the Hon'ble Supreme Court in the case of Dulichand Laxminarayan Vs. Commissioner of Income Tax (1956) 29 ITR 535 (SC), had observed, that as per the Indian Partnership Act, 1932, a partnership firm could not become a partner of another partnership firm, therefore, the assessee firm which was constituted of four partnership firms that had associated and joined hands for carrying on the business could not be held to be a valid firm and was liable to be assessed as an "AOP". Apropos the aforesaid view taken by the A.O, I am principally in agreement with him. As per Section 4 of the Indian

Partnership Act, 1932 the term “partner” and “firm” is defined as under:

“Partnership” is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all.

Persons who have entered into partnership with one another are called individually "partners" and collectively "a firm", and the name under which their business is carried on is called the "firm name".

Accordingly, a “person” who had entered into partnership with one another are collectively called a “firm”. On the issue as to whether a “firm”, as such, can enter into partnership firm with another firm or an individual, it would be apposite to answer the said issue i.e. as to whether a “firm” can be called a “person” under the Indian Partnership Act, 1932 by referring to the judgment of the Hon’ble Apex Court in the case of Dulichand Laxminarayan Vs. Commissioner of Income Tax (supra). In its aforesaid order, it was held by the Hon’ble Apex Court that as a “firm” is not an entity or a “person” in law but is merely an association of individuals, therefore, it is not entitled to enter into a partnership with another firm or an individual. I am, thus, on the basis of the aforesaid settled position of law as had been laid down by the Hon’ble Apex Court, principally in agreement with the observation of the A.O that a partnership firm cannot become a partner in another partnership firm.

10. It is in the background of the aforesaid position of law that I shall now look into the sustainability of the view taken by the A.O that the assessee was liable to be assessed as an "AOP". Although, it is observed by the A.O that the assessee firm was comprising of the aforesaid four partnership firms as partners, but the said observation had been rebutted by the Ld. Authorized Representative (for short 'AR'), on the ground that those were the respective individuals, viz. (i) Shri Suresh Chandra Dayabhai Manik; (ii) Shri Hemendra Kumar Dayabhai Manik; (iii) Shri Paresh Kumar Dayabhai Manik; and (iv) Shri Yogesh Kumar Dayabhai Manik who had associated in their individual capacities, though, representing their respective firms, to constitute the assessee firm, viz. M/s. D.M Builders. It was averred by the Ld. AR that there was no restriction on nominating a person to become a partner in a firm in his individual capacity. The Ld. AR in support of his aforesaid contention had relied on the judgment of the Hon'ble Supreme Court in the case of Rashik Lal & CO. Vs. CIT (1998) 229 ITR 458(SC). My attention was drawn by the Ld. AR to the relevant observations of the Hon'ble Apex Court in the case of Rashik Lal & Co. Vs. CIT (supra). It was submitted by the Ld. AR that though the respective partners in the present case were qua the assessee firm partners in their personal capacity, but qua the third parties i.e. other partners of the firms which they represented were acting in

their respective capacity as that of a partner. It was, thus, the claim of the Ld. AR that the A.O had grossly erred in law and the facts of the case in misconceiving the factual position and declining the assessee's claim for being assessed as a partnership firm.

11. Apropos the disallowance made by the A.O u/s.14A of the Act, it was submitted by the Ld. AR that as the assessee had substantial interest free funds available with it, therefore, there was no justification for the A.O to have made any disallowance u/s.14A r.w.r. 8D(2)(ii). My attention was drawn by the Ld. AR to the "balance sheet" of the assessee firm which revealed 'opening balance' in the partner's capital on 01.04.2013 of Rs.2.53 crore (approx.), and 'closing balance' in the partner's capital account on 31.03.2014 of Rs.2.74 crore (approx.). It was submitted by the Ld. AR that as no interest was being paid on the capital of the respective partners, therefore, there were sufficient self-owned interest free funds available with the assessee firm to make an investment of Rs.60.91 lac in the exempt income yielding mutual funds during the year under consideration. Accordingly, it was submitted by the Ld. AR that as the A.O had grossly erred in failing to appreciate the aforesaid factual position while working out the disallowance of Rs.13,19,518/- u/s.14A of the Act, therefore, the same could not be sustained and

was liable to be struck down. The Ld. AR in support of his aforesaid contention had relied on the judgment of the Hon'ble High Court of Gujarat in the case of Pr. CIT Vs. Sintex Industries Ltd. (2018) 403 ITR 418 (Guj.).

12. Per contra, the Ld. Departmental Representative (for short 'DR') relied on the orders of the lower authorities.

13. I have given a thoughtful consideration to the issue in hand, i.e., sustainability of the disallowance u/s.14A made by the A.O, and find substance in the claim of the Ld. AR. Now when the interest free funds available with the assessee firm were in excess of the investment made in the exempt income yielding mutual funds, therefore, no disallowance of any part of the interest expenditure could have been made in its hands. My aforesaid view that when both interest free funds and interest-bearing funds are available, then, it can safely be presumed that the interest free advances or investments in exempt income yielding assets were made out of the interest free funds is supported by the judgment of the Hon'ble High Court of Gujarat in the case of Pr. CIT Vs. Sintex Industries Ltd. (2018) 403 ITR 418 (Guj.). Also, a similar view had been taken by the Hon'ble High Court of Bombay in the case of HDFC Bank Ltd. Vs. DCIT, (2016) 383 ITR 529 (Bom). I, thus, in terms of my aforesaid

observation that the assessee had sufficient interest free funds available with it to source the investments in exempt income yielding mutual funds, thus, vacate the disallowance of Rs.13,19,518/- made/sustained by the lower authorities u/s.14A of the Act. Thus, the **Ground of appeal No.2** raised by the assessee is allowed in terms of my aforesaid observations.

14. I shall now deal with the issue as to whether or not the lower authorities had rightly concluded that the assessment in the case of the assessee firm was to be framed in the status as that of an "AOP".

15. As observed hereabove, I am principally in agreement with the observation of the A.O that as a "firm" is not an entity or a "person" in law but is merely an association of individuals, therefore, as per the clearly worded Section 4 of the Indian Partnership Act, 1932, it is not entitled to enter into a partnership with another firm or an individual. Considering the aforesaid position of law, I shall herein deal with the sustainability of the view taken by the A.O in the backdrop of the facts involved in the case of present assessee.

16. On a careful perusal of the "Partnership Deed" of the assessee firm, Page 37 to 43 of APB, it transpires that the same comprises of four partners who represented their respective firms. Nothing is

discernible from the “Partnership Deed” which would reveal that the respective partnership firms were taken up as partners in the assessee firm. For the sake of clarity and in order to dispel all doubts, the relevant extract of the “Partnership Deed” wherein the respective profit sharing ratios of the partners is stated is culled out as under:

	<u>Share in Profit or Loss</u>
a. Shri Suresh Chandra Dayabhai Manik (Representative of Manik Brothers)	25%
b. Shri Hemendra Kumar Dayabhai Manik (Representative of Thackers H.P & Co.)	25%
c. Shri Paresh Kumar Dayabhai Manik (Representative of Everest Leaves Co.)	25%
d. Shri Yogesh Kumar Dayabhai Manik (Representative of Manik & Co.)	25%

Apart from that, I find that at clause 6 of the “Partnership Deed”, it is specifically provided that the partners were representing their respective firms. On the basis of the aforesaid facts, I am of the considered view that it can safely be concluded that the assessee firm was comprised of the aforesaid four individual partners, who, though, were representing their respective firms. The observation of the A.O that the respective partnership firms had been taken as partners in the assessee firm is found to be absolutely misconceived and misplaced.

17. I shall in the backdrop of the aforesaid factual position deal with the issue in hand. As observed by me hereinabove, the assessee firm was comprised of four individual partners who were representing their respective firms. It is, thus, in the backdrop of the aforesaid factual matrix that I shall herein deal with the proposition that as to whether or not such an arrangement is as per the mandate of law. It would be apposite to refer to the judgment of the Hon'ble Apex Court in the case of Ram Laxman Sugar Mills Vs. CIT (1967) 66 ITR 613 (SC). The Hon'ble Apex Court in the aforesaid case, had observed, that the mere fact that the manager of a HUF describing himself as a representative of the family had entered into an agreement of partnership with other persons could not form a basis to infer that an agreement of partnership was intended contrary to law between the HUF and other partners. For the sake of clarity, the relevant observations of the Hon'ble Apex Court are culled out as under:

“7. In ascertaining the legal effect of a transaction the court seeks in the first instance to determine the intention of the parties, and when ambiguous expressions are used the court may normally adopt that interpretation which upholds the deed, if the parties thereto have acted on the assumption of its validity. From the mere fact that the manager of a Hindu undivided family describing himself as representing the family entered into an agreement of partnership with other persons, it cannot be inferred that an agreement of partnership was intended contrary to law between a Hindu undivided family consisting of all adult members, females, minors and even unborn persons and strangers to the family.

8. A partnership under section 4 of the Indian partnership Act is "the relation between person who have agreed to share the profits of a business carried on by all or any of them acting for all." Under an agreement of partnership

there must arise the relation of principal and agent inter se between the members of the partnership for the purpose of carrying on the business. The intention disclosed by the deed was that Lala Suraj Bhan was to be a partner, and he was described as manager and he signed the document in that capacity; it did not thereby seek to bring into existence a relationship of partners between the Hindu undivided family and the other members described as the second party. Nor can it be said that by this agreement it was intended to make all the adult members of the Hindu undivided family of Dina Nath Nanak Chand partners of the assessee- firm. None of the clauses of the deed of partnership evidences an intention that the members of the partnership were to be agents inter se or agents of the members of the second party for the purpose of carrying on the business of the assessee-firm. In our view, the true interpretation of this clause is that Lala Suraj Bhan was the first party under the deed. He was merely described as the manager of the joint Hindu trading firm known and styled as Messrs. Dina Nath Nanak Chand, but thereby there was no attempt to make the family a partner of the firm.”

The facts involved in the case of Ram Laxman Sugar Mills Vs. CIT (supra) supports my conviction that an individual in his representative capacity can be taken up as partner in a firm.

18. Similar view had been taken by the Hon'ble Supreme Court in the case of Rashik Lal & CO. Vs. CIT (1998) 229 ITR 458 (SC). In the aforesaid case, the Hon'ble Apex Court reiterating its earlier judgment in the case of Dulichand Laxminarayan Vs. Commissioner of Income Tax (1956) 29 ITR 535 (SC), had observed, that as a firm is a compendious way of describing the individuals constituting the firm, therefore, neither HUF nor a firm can become a partner of a firm because a firm is an association of individuals. Carrying its observation further, it was held by the Hon'ble Apex Court that even if a person nominated by the HUF joins a partnership, then the

partnership will be between the nominated person and the other partners of the firm. It was further observed by the Hon'ble Court that where the Karta of an HUF enters into a partnership agreement with a stranger, the Karta alone in the eyes of law is the partner. For the sake of clarity the relevant observations of the Hon'ble Apex Court, are culled out, as under:

"8. An HUF cannot be in a better position than a firm in the scheme of the Partnership Act. The reasons that led this Court to hold that a firm cannot join a partnership with another "individual" will apply with equal force to an HUF. In law, an HUF can never be a partner of a partnership firm. Even if a person nominated by the HUF joins a partnership, the partnership will be between the nominated person and the other partners of the firm. Having regard to the definition of "partnership" and "partners" and in view of the principle laid down in Dulichand's case (supra), it is not possible to hold that an HUF being a fluctuating body of individuals, can enter into a partnership with other individual partners. It cannot do indirectly what it cannot do directly. If a Karta or any other member of the HUF joins a partnership, he can do so only as an individual. His rights and obligations vis-a-vis other partners are determined by the Partnership Act and not by Hindu law. Whatever may be the relationship between an HUF and its nominee partner, in a partnership, neither the HUF nor any member of the HUF can claim to be a partner or connected with the partnership through a nominee. Where the Karta of an HUF enters into a partnership agreement with a stranger, the Karta alone in the eye of law is the partner. If any payment by the firm to a partner is prohibited by law, the Karta cannot be heard to say that the payment was received by him not as a partner but in some other capacity. Within the partnership, the Karta is a partner like any other partner with whom he has entered into a partnership agreement individually. It is essential to have an agreement between the partners to form a partnership. An HUF not being a "person" cannot enter into an agreement of partnership. If the Karta of an HUF enters into partnership with a stranger, upon the death of the Karta, the partnership will stand dissolved. In the absence of a contract to the contrary, another member of the family cannot step into the shoes of the Karta claiming that the Karta was merely representing the HUF and the real partner was the HUF. A Karta who enters into a contract of partnership with a stranger may be accountable to the other members of the HUF for the profits received from the partnership business. But that is something between the Karta and the HUF. But so far as the partnership firm is

concerned, the Karta is a partner like any other partner. If a commission is paid to a partner who happens to be a nominee of an HUF, the commission is not paid to the HUF. It is paid by the firm to one of its individual partners. The partner may have to account for the monies received from the firm to another person or another firm or an association of persons or an HUF. But that will not alter the fact that commission was paid by the firm to one of its partners.”

On the basis of the facts involved in the aforesaid respective cases before the Hon'ble Supreme Court and the first principle therein laid down, it can safely; or in fact inescapably, be concluded, that there is no bar on an individual to join a partnership firm in his representative capacity of a firm being represented by him.

19. On the basis of the facts involved in the case before me read with settled position of law, I am of the considered view that there was no justification on the part of the lower authorities to have recharacterized the assessee firm i.e. a firm comprising of individual partners (representing their respective firms) as an “AOP”. I, thus, in terms of my aforesaid observations set-aside the order of the CIT(Appeals) and direct the A.O to assess the assessee firm in the status as that of a firm as therein claimed. Thus, the **Ground of appeal No.1** raised by the assessee is allowed in terms of my aforesaid observations.

20. I shall now deal with the grievance of the assessee that the A.O had wrongly disallowed its claim for deduction of donation of Rs.28,600/-.

21. As the assessee in the course of the assessment proceedings could not substantiate as to how its aforesaid claim for deduction of expense incurred was related to its business, therefore, the same was disallowed by the A.O in view of provisions of Section 37 of the Act. Although the assessee specifically assailed the aforesaid disallowance before the CIT(Appeals), however, I find that the same had not been addressed by the said appellate authority while disposing off the appeal. Considering the fact that the CIT(Appeals) had failed to adjudicate the Ground of appeal No.4, wherein the assessee had assailed the disallowance of its claim for deduction of donation of Rs.28,600/-, therefore, I restore the said issue to his file for adjudicating the same. Needless to say, the CIT(Appeals) shall grant a reasonable opportunity of being heard to the assessee while adjudicating the aforesaid issue. Thus, the **Ground of appeal No.3** raised by the assessee is allowed for statistical purposes in terms of my aforesaid observation.

22. **Ground of appeal No.4** being general in nature is dismissed as not pressed.

23. In the result, appeal of the assessee is partly allowed for statistical purposes in terms of my aforesaid observations.

Order pronounced in open court on 22nd day of February, 2023.

Sd/-

(रवीश सूद / RAVISH SOOD)

न्यायिक सदस्य/JUDICIAL MEMBER

रायपुर / Raipur; दिनांक / Dated : 22nd February, 2023

*****SB

आदेश की प्रतिलिपि अग्रेषित / Copy of the Order forwarded to :

1. अपीलार्थी / The Appellant.
2. प्रत्यर्थी / The Respondent.
3. The CIT(Appeals)-II, Raipur (C.G.)
4. The Pr. CIT-II, Raipur (C.G.)
5. विभागीय प्रतिनिधि, आयकर अपीलीय अधिकरण, “एक-सदस्य” बेंच, रायपुर / DR, ITAT, “SMC” Bench, Raipur.
6. गार्ड फ़ाइल / Guard File.

आदेशानुसार / BY ORDER,

// True Copy //

निजी सचिव /Private Secretary

आयकर अपीलीय अधिकरण, रायपुर / ITAT, Raipur