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Income Tax- capital Gain Rulings on conversion:

In decision of the Bombay High Court in CIT v Texspin Engineering and Manufacturing Co. (2003) 263 ITR 345 (Bom) has held that such conversion of firm into company by following the route under Part-IX of the Companies Act, 1956, does not occasion capital gains, since there is no transfer involved in such a case. The High Court after considering the provisions of Companies Act, provisions of income tax relating to capital gains and relying on the ratio of Malbar Fisheries Company v CIT (1979) 120 ITR 49 (SC), CIT Vs. George Henderson & Co Ltd (1967) 66 ITR 622 (SC), CIT Vs. Gillanders Arbuthnot & Co (1973) 87 ITR 407 (SC), held that, when a firm is registered as a company, as per the procedure prescribed under Part IX of the Companies Act, no capital gains arise to the firm. When a partnership firm is treated as limited company, under Part IX of the Companies Act, the properties of the erstwhile firm vests in the limited company as they exist. There is no dissolution of the firm. Hence section 45 (1) of the Income Tax Act is not applicable. When shares of the Company are allotted to partners in consideration of capital standing in their accounts in the firm, there is no transfer of capital assets as contemplated under section 2(47)(iii) of the Income Tax Act (i.e. compulsory acquisition, thereof under any law), as partners are getting their own right to share Capital.

In Well Pack Packaging Vs. Dy. CIT (2003) 78 TTJ (Ahd.) 448, also the same view was taken that, corporatisation of the firm under the part IX route did not attract liability to Capital Gains in the hands of the firm.

In Vali Pattabhiram Roa v Shri Ramanuja Ginning & Rice Factory (P) Ltd. (1986) 60 Comp cas 568 (AP), the Court has held that there is no transfer under general law if the constitution of the firm is changed to that of a company by registering it under Part IX of the Companies Act, as there shall be statutory vesting of title of all the properties of the firm in the newly incorporated company without any need for a separate conveyance.

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