

COMMISSIONER OF INCOME-TAX, MADRAS

v.

BAGYALAKSHMI & CO., UDAMALPET

November 4, 1964

[K. SUBBA RAO, J. C. SHAH AND S. M. SIKRI, JJ.]

Income Tax—Registration of firm—Members of Hindu undivided family representing it as partners in firm—Partition of Hindu undivided family—Variance between the interests of the members as shown in partnership deed and as shown in partition deed—Partnership otherwise genuine—Whether registerable—Indian Income-tax Act, 1922 (11 of 1922), s. 26A.

G and his son V belonged to a Hindu undivided family, and as representatives of the family were partners in the assessee-firm holding therein shares of 7½ as. and 2½ as. respectively. The family thus held through them, an interest of 10 as. in the assessee-firm. On August 24, 1950, there was a partition in the family, and according to the partition-deed the 10 as. interest of the family in the assessee-firm was divided in such a way between seven members that the shares allotted to G and V came to 2 as. and 1 anna 4 pies respectively. On November 30, 1950, a new partnership-deed was drawn up by the partners of the assessee-firm and the shares allotted to G and V therein were again 7½ as. and 2½ as. respectively. The claim of the assessee-firm for Registration under s. 26-A of the Indian Income-tax Act, 1922, on the basis of the new deed, for the years 1952-53, 1953-54 and 1954-55 was accepted by the Income-tax authorities. G and V were duly assessed on their respective shares as shown in the partnership deed. But they contended that in respect of the first two years they were liable to pay tax only in respect of their respective shares as shown in the partition-deed of their erstwhile undivided family. Their contention was accepted by the Income-tax Appellate Tribunal. Whereupon, the Commissioner of Income-tax acting under s. 33B of the aforesaid Act cancelled the registration of the partnership for the three years on the ground that the partnership-deed did not show the correct shares of the partners in the partnership. The Tribunal, in appeal, upheld the Commissioner's action. At the assessee's instance, a reference was then made to the High Court of Judicature at Allahabad, the questions referred being whether the Commissioner's action under s. 33B was lawful, and if so, whether the firm was registerable under s. 26A for the assessment years in question. The High Court decided both the questions in favour of the assessee and against the Revenue. The Commissioner of Income-tax appealed to this court.

It was contended on behalf of the Revenue that as the partnership-deed did not specify the correct shares of G and V in that while they were entitled only to 2 as. and 1 anna 4 pies share in accordance with the partition-deed, they were shown in the partnership-deed as holding 7½ as. and 2½ as. shares respectively, and therefore, the Tribunal had rightly held that the said partnership could not be registered under s. 26A of the Act.

HELD : A contract of partnership has no concern with the obligation of the partners to others in respect of their shares of profit in the partnership. It only regulates the rights and liabilities of the partners. A partner may be the *karta* of a joint Hindu family, he may be a trustee; he may enter into sub-partnership with others; he may under an agreement express or implied, be the representative of a group of persons; he may be a *benamidar* for another. In all such cases he occupies a dual position. *Qua*

A the partnership he functions in his personal capacity; *qua* the third parties, in his representative capacity. Third parties, whom one of the partner represents, cannot enforce their rights against the other partners nor can the other partners do so against the said third parties. Their right is only to a share in the profits of their partner-representative in accordance with law or in accordance with the terms of the agreement, as the case may be. [26 E-G]

B The law of partnership and Hindu law functions in different fields. A divided member or some of the divided members of an erstwhile joint family can certainly enter into a partnership with third parties under some arrangement among the members of the divided family. Their shares in the partnership depend on the terms of the partnership; the shares of the members of the divided family in the interest of their representative in the partnership depend upon the terms of the partition deed. [28 D-E]

C The High Court had given correct answers to the questions propounded. As the partnership-deed was genuine, the shares given to G and V in the said partnership were correct in accordance with the terms of the partnership deed. [28 F]

Commissioner of Income-tax, Ahmedabad v. M/s. A. Abdul Rahim & Co. [1965] 2 S.C.R. 12, referred to.

D *Charandas Haridas v. Commissioner of Income-tax, Bombay*, [1960] 3 S.C.R. 296, relied on.

CIVIL APPELLATE JURISDICTION : Civil Appeals Nos. 1099—1101 of 1963.

Appeals by special leave from the judgment dated January 24, 1961 of the Madras High Court in R.C. No. 143 of 1956.

E *C. K. Daphtary, Attorney-General, N. D. Karkhanis and R. N. Sachthey*, for the appellant.

S. Swaminathan and R. Gopalakrishnan, for the respondent.

The Judgment of the Court was delivered by

F **Subba Rao, J.** These appeals raise, though not the same but a similar question on which we have given a decision in *The Commissioner of Income-tax, Ahmedabad v. M/s. A. Abdul Rahim & Co.*⁽¹⁾. The assessee-firm was the Managing Agents of Palani Andavar Mills Ltd., Udamalpet. It was originally constituted by a deed of partnership, dated June 1, 1934. The following 6 persons were the partners :

G	(1) G. Venkataswami Naidu	..	As. 2
	(2) G. T. Narayanaswamy Naidu	..	As. 2
	(3) G. T. Krishnaswamy Naidu	..	As. 2
	(4) M. A. Palaniappa Chettiar	..	As. 5
	(5) R. Guruswamy Naidu	..	As. 2½
H	(6) K. Venkatasubba Naidu	..	As. 2½

By subsequent transactions the share of G. Venkataswami Naidu

(1) [1965] 2 S.C.R. 12.

was transferred to his son Vidyasagar and the share of M. A. Palaniappa Chettiar was purchased by R. Guruswamy Naidu. With the result that the 5th partner, G. Guruswamy, had $7\frac{1}{2}$ annas share in the partnership instead of $2\frac{1}{2}$ annas share which he held earlier. Guruswamy Naidu and Venkatasubba Naidu, the 5th and 6th partners, belonged to a Hindu undivided family and the beneficial interest of their shares belonged to that family; indeed, during the previous years the joint family was assessed in respect of the income pertaining to the said shares. On August 24, 1950, the said Hindu undivided family was divided and a partition deed was executed between the members thereof. Under the deed the ten annas share held by the family was divided as follows :

(1) R. Guruswamy Naidu	..	As. 2
(2) Rudrappa (Minor son of No. 1)	..	Anna 1
(3) Venkataramana (Minor son of No. 1)	..	Anna 1
(4) Subba Naidu	..	As. 2
(5) Venkatasubba Naidu	..	As. 1-4
(6) Rudrappa Naidu	..	As. 1-4
(7) Jagannatha Naidu	..	As. 1-4

After the said partition, on November 30, 1950, a new partnership deed was executed between the partners of the assessee-firm. Under the said partnership deed the following shares were allotted to each of the partners :

(1) R. Guruswamy Naidu	..	As. $7\frac{1}{2}$
(2) R. Venkatasubba Naidu	..	As. $2\frac{1}{2}$
(3) G. T. Narayanaswamy Naidu	..	As. 2
(4) G. T. Krishnaswamy Naidu	..	As. 2
(5) Vidyasagar	..	As. 2

The point to be noticed is that the beneficial interest in 10 annas share originally belonged to the Hindu undivided family of which Guruswamy Naidu and Venkatasubba Naidu were members. But before and after the partition of the joint family the said two persons, namely, Guruswamy Naidu and Venkatasubba Naidu, were partners of the firm; before the partition the beneficial interest in the 10 annas share was in the undivided family, but after partition the beneficial interest in the partnership was in the divided members of the family including the said two partners. The assessee-firm presented the deed of partnership, dated November 30, 1950, before the Income-tax Officer for registration for the assessment years 1952-53, 1953-54 and 1954-55 and was duly registered under s. 26A of the Indian Income-tax Act, 1922, here-

A inafter called the Act. In due course Guruswamy Naidu and Venkatasubba Naidu were assessed as partners of the assessee-firm on their respective shares as shown in the partnership deed. But the Income-tax Appellate Tribunal, in respect of two of the assessments made on them, accepted their contention and held that they were liable only to pay tax in respect of the shares shown in the partition deed. After the decision of the Tribunal, the Commissioner of Income-tax acting under s. 33B of the Act cancelled the registration of the partnership on the ground that the partnership deed did not show the correct shares of the partners in the partnership. On appeal, the Appellate Tribunal confirmed the order of the Commissioner in respect of the 3 assessment years. At the instance of the assessee-firm the following questions of law were referred to the High Court.

(1) Whether the aforesaid order of the Commissioner under s. 33B cancelling the registration of the firm for the three years 1952-53, 1953-54 and 1954-55 is lawful.

(2) If the answer to the above question is in the affirmative, whether the firm is registrable under s. 26-A for the aforesaid assessment years.

A Division Bench of the Madras High Court, which heard the reference, came to the conclusion that the partnership was a genuine one, that the partition in the joint Hindu family allotting specific shares to the members of the family might have affected the accountability of the two partners of the firm to the other members of the family, but *qua* the partnership their relationship with the other partners had not in any way been affected and, therefore, the Tribunal went wrong in holding that the registration of the said partnership was rightly refused. In the result, it answered the first question in the negative and the second question in the affirmative. Hence the appeals.

Learned Attorney-General, appearing for the Revenue, contended that as the partnership deed did not specify the correct shares of Guruswamy Naidu and Venkatasubba Naidu in that while they were entitled only to 2 annas and 1 anna 4 pies share in accordance with the partition deed, they were shown in the partnership deed as holding $7\frac{1}{2}$ annas and $2\frac{1}{2}$ annas shares respectively and, therefore, the Tribunal rightly held that the said partnership could not be registered under s. 26A of the Act.

Mr. Swaminathan, learned counsel for the respondent contended that the partition of the family's beneficial interest in the

partnership business has no relevance to the question of registration of the partnership under the Act, for, according to him, the Income-tax authorities are only concerned with the validity and genuineness of the partnership deed executed by the partners thereof and not with the dealings of any one of the partners in respect of his share with third parties.

We have held in *The Commissioner of Income-tax, Ahmedabad v. M/s. A. Abdul Rahim & Co., Baroda*⁽¹⁾ that the Income-tax Officer can reject the registration of a firm if it is not genuine or valid and if the application for registration has not complied with the rules made under the Act. Here we have admittedly a genuine partnership. It cannot even be suggested that it is invalid. The only objection is that Guruswamy Naidu and Venkatasubba Naidu have less shares in the partition deed than those shown in the partnership deed. If the distinction between three concepts is borne in mind much of the confusion disappears. A partnership is a creature of contract. Under Hindu law a joint family is one of status and right to partition is one of its incidents. The Income-tax law gives the Income-tax Officer a power to assess the income of a person in the manner provided by the Act. Except where there is a specific provision of the Income-tax Act which derogates from any other statutory law or personal law, the provisions will have to be considered in the light of the relevant branches of law. A contract of partnership has no concern with the obligation of the partners to others in respect of their shares of profit in the partnership. It only regulates the rights and liabilities of the partners. A partner may be the *karta* of a joint Hindu family; he may be a trustee; he may enter into a sub-partnership with others; he may, under an agreement, express or implied, be the representative of a group of persons; he may be a *benámidar* for another. In all such cases he occupies a dual position. *Qua* the partnership he functions in his personal capacity; *qua* the third parties, in his representative capacity. The third parties, whom one of the partners represents, cannot enforce their rights against the other partners nor the other partners can do so against the said third parties. Their right is only to a share in the profits of their partner-representative in accordance with law or in accordance with the terms of the agreement, as the case may be. If that be so, Guruswamy Naidu could have validly entered into a genuine partnership with others taking a 10 annas share in the business, though in fact as between the members of the family he has only a 2 annas share therein. He would have been answerable for the profits per-

(1) [1965] 2 S.C.R. 12.

A taining to his share to the divided members of the family, but it would not have affected the validity or genuineness of the partnership. So much is conceded by the learned Attorney-General. If so, we do not see why a different result should flow if instead of one member of the divided family two members thereof under some arrangement between the said members of the family took 10 annas share in the partnership. If the contention of the Revenue was of no avail in the case of representation by a single member, it could not also have any validity in the case where two members represented the divided members of the family in the partnership. As the partnership deed was genuine, it must be held that the shares given to Guruswamy Naidu and Venkatasubba Naidu in the said partnership are correct in accordance with the terms of the partnership deed.

This Court in *Charandas Haridas v. Commissioner of Income-tax, Bombay*⁽¹⁾ had to consider a converse position. There a *karta* of a Hindu undivided family was a partner in 6 managing agency firms and the share of the managing agency commission received by him as such partner being assessed as the income of the family. Thereafter, there was a partial partition in the family by which he gave his daughter a one pie share of the commission from each of two of the managing agencies and the balance in those agencies and the commission in the other four managing agencies were divided into five equal shares between himself, his wife and three minor sons. The memorandum of partition recited that the parties had decided that commission which accrued from January 1, 1946, ceased to be the joint family property and that each became absolute owner of his share. Notwithstanding the partition, the Income-tax authorities assessed the said total income as the income of the joint family. The Bombay High Court agreed with that view. But this Court held that as the partition document was a genuine one, it was fully effective between the members of the family and therefore the income in respect of the divided property was not the income of the Hindu joint family. In that context Hidayatullah J., speaking for the Court, made the following observations :

“The fact of a partition in the Hindu law may have no effect upon the position of the partner, insofar as the law of partnership is concerned, but it has full effect upon the family insofar as the Hindu law is concerned. Just as the fact of a *karta* becoming a partner does not introduce the members of the undivided family into the partnership, the division of the family does not change

(1) [1960] 3 S.C.R. 296.

the position of the partner *vis-a-vis* the other partner or partners. The Income-tax law before the partition takes note, factually, of the position of the *karta*, and assesses not him *qua* partner but as representing the Hindu undivided family. In doing so, the Income-tax law looks not to the provisions of the Partnership Act, but to the provisions of Hindu law. When once the family has disrupted, the position under the partnership continues as before, but the position under the Hindu law changes. There is then no Hindu undivided family as a unit of assessment in point of fact, and the income which accrues cannot be said to be of a Hindu undivided family. There is nothing in the Indian Income-tax law or the law of partnership which prevents the members of a Hindu joint family from dividing any asset."

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These observations support the conclusion we have arrived at. The division in the joint family does not change the position of the *karta* as a partner *vis-a-vis* the other partner or partners in a pre-existing partnership, because the law of partnership and Hindu law function in different fields. If so, on the same principle a divided member or some of the divided members of an erstwhile joint family can certainly enter into a partnership with third parties under some arrangement among the members of the divided family. Their shares in the partnership depends upon the terms of the partnership; the shares of the members of the divided family in the interest of their representative in the partnership depends upon the terms of the partition deed.

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For the aforesaid reasons, we hold that the High Court has given correct answers to the question propounded.

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In the result, the appeals fail and are dismissed with costs. One hearing fee.

Appeals dismissed.