

Kylasa Sarabhiah, Bombay Cloth ... vs Commissioner Of Income-Tax, Andhra ... on 1 December, 1964

Equivalent citations: 1965 AIR 1411, 1965 SCR (2) 310, AIR 1965 SUPREME COURT 1411

Author: J.C. Shah

Bench: J.C. Shah, P.B. Gajendragadkar, M. Hidayatullah, S.M. Sikri, R.S. Bachawat

PETITIONER:

KYLASA SARABHIAH, BOMBAY CLOTH SHOP, SECUNDERABAD

Vs.

RESPONDENT:

COMMISSIONER OF INCOME-TAX, ANDHRA PRADESH

DATE OF JUDGMENT:

01/12/1964

BENCH:

SHAH, J.C.

BENCH:

SHAH, J.C.

GAJENDRAGADKAR, P.B. (CJ)

HIDAYATULLAH, M.

SIKRI, S.M.

BACHAWAT, R.S.

CITATION:

1965 AIR 1411

1965 SCR (2) 310

CITATOR INFO :

F 1967 SC 448 (5)

ACT:

Income Tax Act, 1922 (11 of 1922), s. 26-A, r. 2-Registration of firm -Partnership consisting of firm and other persons-Income Tax Officer, powers-"Specify", meaning of.

HEADNOTE:

The appellant firm applied for registration under s. 26-A of the Indian Income-tax Act. In the application the persons recited as partners were a Yam shop-another firm and four

other persons and the collective share of the Yarn shop and the shares of the other partners were set out. The Income-tax Officer rejected the application and his order was confirmed in appeal by the Appellate Assistant Commissioner and by the Income-tax Appellate Tribunal. The Tribunal held that because in the deed of partnership benefits to which certain minors were admitted and particulars "about the distribution of profits or losses in the manner in which the firm wanted the same to be distributed" were not specified, and because by the deed of partnership the yarn shop was introduced as a partner in the firm, the privilege of registration under s. 26A must be denied to the firm. The question was referred to the High Court, which too answered similarly. In appeal by special leave,

HELD: The appeal must be allowed.

(i) If the statutory conditions which qualify the firm for registration are fulfilled, an arrangement between some of the partners, which binds them to distribute the profits under a stipulation which is not a part of the partnership agreement does not effect the right to claim registration of the partnership agreement. [314 H]

Dulichand Laxminarayan v. Commissioner of Income-tax, Nagpur, [1956] S.C.R. 154, distinguished.

(ii) The word "specify" is used in s. 26A and Rule 2 as meaning mentioning, describing or defining in detail; it does not mean expressly setting out in fractional or other shares. [314 D-E]

(iii) If the conditions for registration of a firm are fulfilled, the Income-tax Officer has no power to reject the application. Undoubtedly, the application must strictly be in conformity with the Act and the Rules, but in so ascertaining, the deed of partnership must be reasonably construed. [311 G]

JUDGMENT:

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 83 of 1964. Appeal by special leave from the judgment and order dated August 18, 1960 of the Andhra Pradesh High Court in R. C. Appeal No. 34 of 1957.

A. Ranganadham Chetty, K. Venkaramaiah, A. Vedavalli and A. V. Rangam, for the appellants.

R. Ganapathy Iyer and R. N. Sachthey, for the respondent. The Judgment of the Court was delivered by Shah, J. The appellants who are a firm carrying on business in cloth at Secunderabad applied on June 30, 1955, for registration under s. 26-A of the Indian Income-tax Act, 1922, for the assessment year 1956-57. The following persons were, it was recited in the application, partners, having share in the profits and lossess in proportions specified against their names :-

1 . M/s Kylasa Sarabhiah a firm consisting of the following partners :

(a) Kylasa Veeresalingam.

(b) Kylasa Nagendrarao Rs. As. Ps.

(c) Kylasa Madhusudhanarao 069

2. Mahendrakar Narayanarao 033

3. Nune Vittayya 026

4. Pottupalli Chandrayya 026

5. Gande Ramayya 010 For facility of reference we will call No. 1 'the Yarn Shop'.

The Income-tax Officer rejected the application, and his order was confirmed in appeal by the Appellate Assistant Commissioner and by the Income-tax Appellate Tribunal. The Tribunal held that because in the deed of partnership benefits to which certain minors were admitted, and particulars "about the distribution of profits or losses in the manner in which the firm wanted the same to be distributed" were not specified, and because by the deed of partnership the Yarn Shop was introduced as a partner in the firm, the privilege of registration under s. 26-A must be denied to the firm. The High Court of Andhra Pradesh recorded on the following question referred under s. 66(1) of the Income-tax Act "Whether on the facts and circumstances of the case, the assessee is entitled to registration under s. 26-A of the Incometax Act ?", a negative answer.

Section 26-A of the Indian Income-tax Act, 1922, provides "(1) Application may be made to the Income-tax Officer on behalf of any firm, constituted under an instrument of partnership, specifying the individual shares of the partners, for registration for the purpose of this Act Sup.165--4 and of any other enactment for the time being in force relating to income-tax or super-tax.

(2)The application shall be made by such person or persons and at such times and shall contain such particulars and shall be in such form, and be verified in such manner, as may be prescribed; and it shall be dealt with by the Income-tax Officer in such manner as may be prescribed."

By securing registration under the Act, the partners of the firm obtain a benefit of lower rates of assessment and no tax is directly charged on the income of the firm. This is an important benefit to which the partners of a registered firm become entitled as a consequence of registration, and if it is intended to secure that benefit, requirements of s. 26-A and the rules framed under the Act must be strictly complied with. Rule 2 framed under s. 59 requires that the application shall be signed by the partners (not being minors) personally, and prescribes the period within which the application shall be made for the year in question. Rule 3 provides that the application shall be made in the prescribed form and shall be accompanied by the original instrument of partnership under which the firm is constituted. By Rule 4 it is provided that if on receipt of the application, the Income-tax

Officer is satisfied that there is or was a firm in existence constituted as shown in the instrument of partnership, and that the application has been properly made, he shall enter in writing at the foot of the instrument or certified copy, as the case may be, a certificate in the prescribed form. By Rule 6 of the certificate of registration may be renewed for subsequent years.

Registration of the firm may be obtained on an application to the Income-tax Officer on behalf of any firm, if the firm be lawfully constituted under an instrument of partnership which specifies the individual shares of partners and the Income-tax Officer is satisfied that there is or was a genuine firm in existence as shown in the instrument. If the conditions are fulfilled, the income-tax Officer has no power to reject the application. Undoubtedly, the application must strictly be in conformity with the Act and the Rules, but in ascertaining whether the application is in conformity with the Rules, the deed of partnership must be reasonably construed.

Under the Indian Partnership Act, 1932 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. A firm is strictly not a person : it is an association of persons, and an agreement by which a firm purports to enter into a partnership with an individual or another firm merely makes the partners of that firm individually partners of the larger partnership. The problem posed by such a partnership agreement is under the general law academic, but the right to registration under s. 26A being conditional upon specification of the individual shares of the partners, a deed of partnership between a firm and an individual, which specifies the collective share of the firm, without more, cannot be registered. It has been held by this Court in *Dulichand Laxminarayan v. Commissioner of Income-tax, Nagpur*(1) that a partnership constituted between an individual, a joint Hindu family and three firms could not be registered under s. 26-A of the Act. In *Dulichand's case*(1) the partnership deed was signed by five individuals, viz., the karta of the joint Hindu family, one partner each of the three firms and the individual. It was held that the partnership could not be admitted to registration, because a firm as such cannot enter into an agreement as partner with another firm or individual, and also because all the members of the three firms had not personally signed the application as required by Rule 2 of the Income-tax Rules. The application in the present case was rejected by the Tribunal, because in its view the benefits to which the minors were admitted and the shares of the major partners who were members of the Yarn Shop were not specified, and that the Yam Shop was introduced as a partner in the firm. But the Tribunal, in our judgment, erred in holding that the benefits to which the minors were admitted and the shares of the major members of the Yarn Shop were not specified in the deed of partnership. It is clearly recited in the preamble that K. Rajeshwarrao, K. Haranath Babu, K. Ramesh Babu and K. Shivakumar-the four minors-were admitted to the benefit of the partnership with equal shares in the profits falling to the share of the Yam Shop, and losses were to be shared in equal shares only by the major partners K. Veeresalingam, K. Nagendraro and K. Madhusudhanarao. The scheme of the deed therefore was that the Yam Shop collectively had a share of 0-6-9 in the profits and was liable in the same proportion in the losses in the appellant firm. Out of this 0-6-9 share, seven persons who constituted the Yam Shop were entitled to share the profits equally, whereas losses were to be shared by the three major members of the Yam Shop equally. It is true that in the deed of partnership, the first partner is described as "Kylasa (1)[1956] S.C.R. 154.

Sarabhiah Yam firm"-the Yam Shop-constituted under an instrument of partnership dated May 12, 1955, and in paragraphs 3 and 8 this Yam Shop is also described as the first partner. But the substance of the agreement cannot be permitted to be overshadowed merely by the use of the collective description of some of the persons who agreed to be partners. The agreement was between K. Veeresalingam, K. Nagendrarao, K. Madhusudhanarao, Mahendrakar Narayana Rao, Noone Vittayya, Pottipalli Chandrayya and Gande Ramayya to enter into partnership with the covenant that the profits and losses shall be divided in the shares specified in the instrument. The partnership agreement was signed by the major partners; the application for registration was in conformity with the rules framed under the Act, the certificate regarding the distribution of the profits in the previous year was given, the original instrument of partnership was produced and the instrument specified the individual shares of the partners. Merely because the deed of partnership set out in paragraph 8 the collective share of the Yarn Shop, registration could not be refused, for in the preamble the division of the shares of profits and losses among the three members of the Yam Shop and those admitted to the benefit of the partnership is clearly indicated. The word "specify" is used in s. 26-A and Rule 2 as meaning, mentioning, describing or defining in detail :

it does not mean expressly setting out in fractional or other shares. In the deed of partnership, the shares are clearly defined, though they are not worked out in precise fractions. Nor is it true to say that the Yam Shop is introduced as a partner. The agreement is in truth between three major members out of those who constitute the Yarn Shop and four outsiders. Each of them has signed the application and the covenants of the partnership agreement bind the partners individually. Indication in the deed of partnership that three of them held qua the Yam Shop a certain relation did not affect their status as partners of the appellant firm individually.

It was urged that in the deed dated February 20, 1952, constituting the Yarn Shop, as amended by the deed dated May 12, 1955, no profit sharing ratio was mentioned. But we are not concerned with the registration of the Yarn Shop. We are unable to appreciate how a defect (even if there be one in the agreement constituting the Yarn firm) affects the right of the appellant firm to be registered. If the statutory conditions which qualify the appellants for registration are fulfilled, an arrangement between some of the partners of the appellants which binds them to distribute the pro-fits under a stipulation which is not a part of the partnership agree-

ment does not affect the right to claim registration of the partner-ship agreement.

The answer recorded by the High Court must therefore, be discharged, and an affirmative answer must be recorded. The appeal is allowed. The appellants will be entitled to their costs in this Court and the High Court. Appeal allowed.