N. V. Shanmugham And Co vs Commissioner Of Income-Tax, Madras on 23 April, 1970

Equivalent citations: 1970 AIR 1707, 1971 SCR (1) 340

Author: K.S. Hegde

Bench: K.S. Hegde, J.C. Shah, A.N. Grover

PETITIONER:
N. V. SHANMUGHAM AND CO.

Vs.

RESPONDENT:
COMMISSIONER OF INCOME-TAX, MADRAS

DATE OF JUDGMENT:
23/04/1970

BENCH:
HEGDE, K.S.
BENCH:
HEGDE, K.S.
SHAH, J.C.
GROVER, A.N.

CITATION:
1970 AIR 1707 1971 SCR (1) 340
1970 SCC (2) 139
CITATOR INFO :
R 1973 SC2369 (10)
R 1977 SC2103 (15)

ACT:
Income-tax Act, 1922, s. 41(1)-Receivers appointed by Court to ,carry on business of dissolved firm-Erstwhile partners acquiescing in carrying on of business by receivers and receiving from them their shares of the profits earned-Assessment of income of business whether to be on erstwhile partners as in individuals or as constituting an association of individuals-Receivers whether an association of persons Nature of liability of receivers under s. 41(1).

HEADNOTE:
The appellant was a partnership firm constituted under a deed April '20, 1955. On a suit for dissolution being filed

by one of the partners and an application being made for the appointment of a receiver, the Court appointed three 'receivers two of whom were the erstwhile partners of the firm and the third an advocate. The Court-ordered the receivers to continue the business for the purpose of winding up with the power to realise the out standings and discharge the dues of the firm. The profits were to be divided among the parties according to terms of the partnership deed dated April 20, 1955. The business yielded profits in the assessment years 1958-59 and'1959-60. In response to notices issued to the Income-tax Officer the receivers filed returns for these years showing 'nit' income. They showed the profits in section D of the return. They claimed that the income should be assessed in the hands of the beneficiaries as they were already assessees having other sources of income. The Income-tax officer rejected the contention and held that the business was carried on by an 'association of persons' and, as such no question of assessing the individual partners on their share of income at the rates applicable to them would arise. The Appellate Assistant Commissioner confirmed the order ,of the Income-tax Officer. The Tribunal took the opposite view but the High Court in reference answered the question referred to it, namely whether the income "could be assessed on the receivers as a association ,.of persons under s. 10 or under s. 41 of the Act", in favour of the revenue. In appeals to this Court by certificate,

HELD : (i) The fact that there were three receivers was wholly irrelevant for the purpose of assessment and did not make them an association of receivers. In respect of business profits, all assessments of tax is done under s. 3 read with s. 10 of the Act. Section 3 imposes the charge and s. 10 provides for determining the profits and gains of business. Section 41 does not impose any separate charge but only empower the Revenue to levy and collect tax due from a person or persons, from his or their representative. The primary liability to pay the tax in the present case was that of the real owners of the business i.e. the erstwhile partners of the firm. There was thus no question of assessing the receivers as an association of persons. The receivers were not liable "under s. 10 or s. 41 ,of the Act"; their liability arose under s. 41 read with s. 10. [343 E-H; 344 A-B]

(ii) The control and management of the receivers was a unified one. The receivers had joined in a common purpose and they acted jointly. When they did so they acted on behalf of the persons who were the owners of the, business. The receivers did not and could not have represented the individual interest of the various owners of the business; that

341

would have resulted in chaos. The profits Were earned on behalf of the persons who had a common interest created by

the order of the court and were on that account an "association of persons". [345 B-C]
The fact that one of the erstwhile partners bad objected to the continuance of the partnership could not lead to a contrary conclusion. All the owners of the business including the person who objected to the continuance of the business were given month by month some amounts from the proceeds of the business and none of them had declined to receive the same. They were therefore an "association of persons" within the meaning of s. 3 of the Act having joined together for the purpose of producing income, profits or gains. [345 G-H; 347 F]
Commissioner of Income-tax, Ahmedabad, v. Balwantrai Jethalal Vaidya Qrs. 34 I.T.R. 187, C.R. Nagappa v. Commissioner of Income-tax 73 I.T.R. 626, In re B. N. Elias
JUDGMENT:

42 I.T.R. 115, referred to.

Commissioner of Income-tax, Bombay v. Indira Balkrishna 39 I.T.R. 546 and Commissioner of Income-tax, Poona v. Buldana Distt. Main Cloth Importers Group, 42 I.T.R. 172, applied.

& CIVIL APPELLATE JURISDICTION : Civil Appeals Nos. 294 and 295 of 1967.

Appeal from the judgment and order dated November 30, 1965 of the Madras High Court in Tax Case No. 215 of 1962 (Reference No. 120 of 1962).

M. C. Chagla, K. Srinivasan and T. A. Ramachandran, for the appell it (in both the appeals).

B. Sen, G. C. Sharma and B. D. Sharma, for the respondent (in both the appeals).

The Judgment of the Court was delivered by Hegde, J. These companion appeals by certificate under s. 66A(2) of the Indian Income Tax Act, 1922 (in short 'the Act') are directed against the decision of the Madras High Court in a tax reference under S. 66 (1) of the Act, relating to the assessment years 1958-59 and 1959-60. Messrs. N. V. Shanmugam and Co., a firm, was carrying on business in the manufacture and sale of snuff under a deed of partnership dated April 20, 1955. Its partners were S. P. Ramiah Nadar, Murugavel Nagar and Shanmughavel Nadar. S. P. Mohan, a minor had been admitted to the benefits of the partnership, his share in the net profits being 1/6th. The deed of partnership provided that the partnership could not be dissolved before August 3 1, 1955. But it was open to the partners to continue the partnership or enter into a fresh partnership on fresh terms and conditions. On September 17, 1956, Ramiah Nadar filed a suit in the city Civil Court, Madras for the dissolution of the partnership 2Sup. Cl/70 8 with effect from August 31, 1956 and for taking of accounts. He also applied for the appointment of a receiver to take charge of the business. On September 21, 1956, the Court appointed three receivers two of whom were the partners of the firm namely Ramiah Nadar and Murugavel Nadar and the third was an Advocate by name Ram Mohan. The business of the firm had been stopped from September 1, 1956 to September 21, 1956. The Court directed the receivers "to reopen and conduct the snuff business for the purpose of

winding up, with powers to realise the outstandings and discharge the dues of the firm" subject to the following among other terms.

Clause 4 : The receivers can carry on the business of the partnership normally.

Clause 6 : All parties to have access to the books of the firm and to the business premises.

Clause 7 : All parties are entitled to get information relating to the conduct of the business from the receivers.

Clause 8 : The profits if any earned from 1-9- 1956 will be treated as an asset of the firm subject to be divided between the parties in the manner set out in paragraph 10 of the deed dated 20-4-1955. The receiver or receivers shall not be entitled to any share in the pro- fits for the management.

Clause 9 : The receivers will pay every month Rs. 1,5001' to plaintiff, Rs. 1,5001- to the 1st defendant, Rs. 750/- to 2nd defendant and Rs. 750/- to 3rd defedant by his guardian from November 1, 1956 (owners of the dissolved firm).

Sometime later the court appointed a Commissioner for taking the accounts of the' firm and for arranging the sale of the business as a going concern; but no sale took place. In the assessment year 1958-59, the business yielded a profit of Rs. 93,739/-. in the assessment year, 1959-60, there was a profit of Rs. 1,54,393/In response to a notice from the Income-tax Officer, the receivers filed "nil" returns but showed the profits earned in the businezs in Section D of the return. But they asserted that the income should be assessed in the hands of the beneficiaries as they are already assessees having other sources of income. The Income-tax Officer rejected that contention. He came to the conclusion that the business was carried on by an 'association of persons' and as such no question of assessing the individual partners on their share of income at tile rate applicable to them would arise, as contended by the receivers. The Appellate Assistant Commissioner rejected the appeal of the assessees and confirmed the order of the Incometax Officer; but on a further appeal, the Tribunal came to the conclusion that the profits earned should be assessed to tax in the hands of the individual partners at the rates applicable to, them. At the instance of the Commissioner of Income-tax, Madras, the Tribunal submitted the following question under s. 66(1) of the Act for the opinion of the High- Court :

> "Whether the incomes of the business in snuff could be assessed on the receivers as an association of peisons under s. 10 or under s. 41 of the Act."

The High Court answered that question in favour of the Revenue.

The real point in controversy between the Revenue and the assessees is whether the profits earned in the business should be considered as profits earned by an "association of persons'," or whether it should be considered as having been earned by individuals. The receivers appointed by the court were merely the representatives of the real owners of the business i.e. the erstwhile partners of the firm. The primary liability to pay the tax due was, that of the real owners. The tax may be levied and

recovered from the Receivers under s. 41 (1) of the Act. To borrow the expression from the Income-tax Act, 1961, they are only representative assessees. The fact that there were three receivers did not makethere an association of receivers. The three receivers jointly represented the real owners. The circumstance that there were three receivers was wholly irrelevant for the purpose of the assessment. There was no question of assessing the receivers as an "association of persons". The real question is whether the Persons whom the receivers represented constituted an "association of persons". Further in respect of business profits,-,all assessment of tax is done under s. 3 read with s. 10 of the Act. Section 3 imposes the charge and s. 10 to the extent relevant for our present purpose provides that tax shall be payable by the assessee under the head "Profits and gains of business" in respect of the profits or gains of business carried on by him subject to the allowances allowed under sub-s. (2) of that section. Section 41 empowers the Revenue to levy the tax that could-have been levied on the person who earned the profits on one or the other of his representatives mentioned in that section and recover the same from that representative "in the like manner and to the same amount as it would be leviable upon and recoverable"

> from the person on whose, behalf such profits are. recoverable and all the provisions of the Act shall apply accordingly. Section 41 of the Act does not impose any separate charge. It only empowers the Revenue to levy and collect a tax due from a person or persons, from his or their representative. Hence there-.
>
> is no question of either the receivers being an "association of persons" or their being liable "under s. 10 or s. 41 of the Act". The liability of the receivers arose under S. 41 read with S. 10. The Tribunal wanted the opinion of the High Court on the question whether the profits in question should be considered to have been earned by an "association of persons" or by individuals. We shall proceed to answer that question.
>
> Mr. M. C. Chagla, learned Counsel for the assessee contended that the liability of receivers is co-extensive with that of the beneficiaries and cannot in any case be a larger or wider liability. If the assessment is made on a receiver whatever the nature of the profit, whatever the mode of compuation, his liability to pay tax must be determined in accordance with s.41 of the Act; that section is mandatory; the tax payable by him on the profits earned can only be ascertained in accordance with the special provisions laid down in that section; it is not open to the department to ignore the provisions of s.41 and levy tax on receivers in the same way as on assessee who does not fulfil the character of a receiver. According to the Counsel when an assessment is made under s.41 of the Act, it must be done under one of the heads mentioned in Chap. III of the Act and the provisions laid down with regard to computation of the income-tax must be carried out; Section 41. will come into play after the incomes has been so computed. In support of this contention, he relied on the decision of the Bombay High Court in Commissioner of Income-tax, Ahmedabad v. Balwantrai Jethalal Vaidya and ors.(1) which decision has been approved by this Court in C. R. Nagappa v. Commissioner of Income Tax. (2) Proceeding further the Counsel urged that the assessment of the receivers should have been on the same basis as the erstwhile partners of the firm would have been assessed in respect of the

profits in question. According to him, the business in question could not have been conducted by the erstwhile partners as an "association of persons". He urged that the erstwhile partners of the firm were fighting amongst themselves; some of them wanted to carry on the business while one of them wanted to close down the same. Hence they could not have carried on the business as an "association of persons". He urged that an "association of persons" as used in s.3 of the Act means an association in which two or more persons voluntarily join in a 41 common purpose" or "common action". He further urged that in a business said to be carried on by an "association of persons", there must be unity of control and unity of management; as no such unity existed amongst the erstwhile partners of the firm, it cannot be said that the receivers represented an "association of persons".

(1) 34, I.T.R. 187. (2) 73, I.T.R., 626.

We are unable to accede to the contentions of the learned Counsel for the assessee. It is not denied that the business was carried on by the receivers on behalf of erstwhile partners of the firm and that considerable profits were earned from the business. The control and the management of the business was in the hands of, the receivers. That control and management was a unified one. The receivers had joined in a common purpose and they actd jointly. When they did so they acted on behalf of the persons who were the owners of the business. The receivers did not and could not have represented the individual interest of the various owners of the business. If they had done so there would have been chaos in the business. The profits to which those owners lay claim and which they were not averse to pocket, were earned on behalf of an "association of persons". The profits were earned on behalf of the persons who had a common interest creatd by the order of the Court and were on that account of an "association of persons". The existence of specific or defined interest in the profits did not make the earning any the less by an 'association of persons'. Liability to tax depends upon the earning of profits by a unit and not upon the ultimate division of the profits. The expression "association of persons" is not defined in the Act. At one stage, there was conflict of judicial opinion about the true meaning of that expression. That conflict can now be said to have been settled by some of the decisions of this Court to which we shall refer presently.

In Commissioner of Income-tax, Bombay v. Indira Bal krishna(1) this Court accepted the observations of Sir Harold Derbyshire C.J. in In re B. N. Elias and ors. (2). that the words " associate" means "to join in common purpose or to join in an action". Therefore "association of persons" as used in s. 3 of the Act means an association in which two or more persons join in a common purpose or common action, and as the words occur in a section which imposes a tax on income, the association must be one, the object of which is to produce income, profits or gains. It is true that in the instant case before the receivers were appointed,. one of the erstwhile partners objected to the continuance of the partnership. But there is nothing in the record to show that he objected to the continuance of the business. All the same we shall assume that he did not want at that stage that the business should be continued. But in fact business was continued in pursuance of the orders of the Court. All the owners of the business including the person who objected to the continuance of the business were given, month by month, some amounts from the proceeds of the business. It was not said that any of them declined to receive the same. That means all of them

acquiesced in the continuance of (1) 39, I.T.R. 546.

(2) 3, I.T.R. 408.

the business. Each one of the assessees wants to share the profits earned on behalf of all of them but when it comes to the question of paying tax, they want to deny that the business was conducted on behalf of all of them. It is true considerations of equity are irrelevant in interpreting taxing provisions but while considering the question who carried on a business, the course of conduct of the concerned parties is relevant. On the facts proved, it must' be held that in law the erstwhile partners of the firm carried on the business through their representatives. In Mohamad Noorullah v. C.I.T. Madras(1) this Court had to consider whether the assessment in that case was rightly made on an "association of persons". Therein, 0, a Mohamaden who was carrying on the business of manufacture and sale of beedies of a particular brand, died intestate on December 17, 1942 leaving as his heirs, N, a son by his predeceased wife, L his widow and his four children by L. The widow L and one D carried on the business after the death of O.N, through his next friend, applied for leave to sue for partition in forma pauperis and pending these proceedings on March 17, 1943, two advocates were appointed as joint receivers of all the properties of 0, by consent of all the parties. The consent on behalf of the minor was given by his next friend. The widow L filed another suit for partition on May 10, 1943 but applied for the continuance of the joint receivers. N opposed the application on the ground that h.-. wanted different persons to be appointed as receivers. By an order dated May 25, 1943, the Court ordered the continuance of the joint receivers. The receivers continued in charge of the business till November, 1946 when the business was put up for sale by auction and was purchased by N. The Income-tax Officer assessed the profits of the business for the calendar years 1943-46 in the, hands of the receivers as the income of an "association of persons" consisting of the heirs of O. The Appellate Assistant Commissioner as well as the Tribunal upheld the finding of the Income-tax Officer. On a reference under s.66(1) of the Act, the High Court agreed with the view taken by the authorities under the Act. This Court upheld the view taken by the High Court. This decision was tried to be distinguished by Mr. Chagla on the ground that in that case all the parties had consented to the appointment of the receivers. None of the heirs of the deceased owner of the business wanted to break the unity of the business or its continuity and the business was of such a nature that it could not be carried on without consensus; therefore, the continuance of the business by the receivers was rightly considered as continuance of business by the heirs of the deceased. According to the Counsel such was not position in the present case. For the reasons already stated, we (1) 42, I.T.R. 115.

see no merit in that contention. We have earlier come to the conclusion that the business was continued with consent of all the owners. Hence for the purpose of this case it is not necessary to go into the question as to what would have been the position it the business had been continued without the consent of all the owners. The facts of this case directly fall within the rule laid down by this Court in Commissioner of Income-Tax, Poona v. Buldana Distt. Main Cloth Importers Group(1). The facts of that case were : In 1945, the Deputy Commissioner of Buldana evolved a scheme for the distribution of cloth in his district and, with the sanction of the C.P. Government appointed a group of four persons as sole agents for the import of cloth from mills in various places in India and for its distribution to retailers. For different periods the group which imported cloth was differently

constituted. H. & Co., which was a common member maintained the books relating to the business. Every time there was a change in the constituents of the group, a separate set of books was maintained and the profits from those enterprises were divided between the various persons who formed the group at the material time. The Appellate Tribunal found that the import,and distribution of cloth was done on a joint basis, the purchasers were joint, so were the sales and the profits were ascertained on a joint basis and then distributed according to the capital contributed by each member of the group. This Court held that the group was an "association of persons" and could be assessed on its profits as such to income-tax and excess profits tax. It further held that it made no difference that the business was carried on because the Deputy Commissioner of the district had appointed the members constituting the group to import and distribute the cloth. Therein the members of the group did not voluntarily join the group. They were put together by the Deputy Commissioner and asked to act together, which they did. Similar is the position in the present case. For the reasons mentioned above, our answer to the question referred is that the profits in question were earned from a business carried on by an "association of persons". In the result these appeals fail and they are dismissed with costs. One hearing fee.

G. C. Appeals dismissed.

(1) 42 I.T.R. 172.