

Krishna Flour Mills vs Commissioner Of Income-Tax, Bangalore on 1 November, 1960

Equivalent citations: [1962]44ITR501(SC)

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Bench: J.C. Shah, M. Hidayatullah, S.K. Das

JUDGMENT

S.K. Das, J.

1. These are three appeals by special leave from the judgment and order of the High Court of Mysore dated October 8, 1958. By that order the High Court dismissed three petitions made by the Krishna Flour Mills, assessee before the income-tax authorities and appellant before us, under section 66 (2) of the Indian Income-tax Act, 1922, holding that no question of law arose out of the order dated March 24, 1956, made by the Income-tax Appellate Tribunal, Madras, in Income-tax Appeals Nos. 2358, 2359 and 2360 of 1955-56.

2. M. Kasturi Ranga Setty (hereinafter referred to as K. R. Setty) was a member of a joint Hindu family. On a partition between himself and his two brothers, two flour mills belonging to the family became his separate property from June 1, 1948. These two flour mills were the Krishna Flour Mills and the Elgin Electric Flour Mills, in the latter of which K. R. Setty had only a lessee's interest. He was assessed under the Mysore Income-tax Act as karta of a joint Hindu family until the assessment year 1949-50, that is, before the Indian Income-tax Act, 1922, was brought into force in Mysore on and from April 1, 1950. Even before the disruption of the joint family Venkataramana Setty (hereinafter called V. Setty), brother-in-law of K. R. Setty, was managing the business of the two mills. He was paid a salary of about Rs. 6,000 per annum, which was increased in the account year 1948-49 to Rs. 10,000 per annum. This salary was credited in his name in the accounts of the mills. When a petition of the joint family was about to take place, K. R. Setty proposed to his brother-in-law that the latter should come in as a partner and on November 16, 1949, a partnership deed was executed, the partnership arrangement having been given effect to from July 1, 1949. This deed of partnership recited inter alia that the business of partnership would be confined to the working of the Krishna Flour Mills and the three partners were K. R. Setty, his wife, Nagaratnamma, and his brother-in-law, V. Setty. The partnership was originally for a period of five years which was later extended to March 31, 1955. Nagaratnamma contributed Rs. 50,000 as her share of the capital and V. Setty contributed Rs. 40,000; the sum of Rs. 50,000 came out of Nagaratnammas stridhanam money, which was credited to her account in the books of the Krishna Flour Mills and represented amounts given to her by her husband and the sum of Rs. 40,000 came out of the

amounts standing to the credit of V. Setty in the books of the mills representing his accumulated past salary. The partnership deed further recited that the partners had equal shares in the profits and losses, and the business would be conducted by the first partner, namely, K. R. Setty, assisted by the third partner, namely, V. Setty. The firm was duly registered with the Registrar of Firms on November 23, 1949.

3. The appellant made an application under section 26A of the Act for registration of the firm for the assessment year 1950-51 and 1951-52. The Income-tax Officer, Bangalore, rejected the application on March 18, 1954, holding that the partnership was not genuine. That order was confirmed in appeal by the Appellate Assistant Commissioner and the Income-tax Appellate Tribunal. The appellant renewed his application for the assessment years 1952-53, 1953-54 and 1954-55. These applications were heard together, and by an order dated February 26, 1955, the applications were rejected. The appellant then preferred appeals to the Appellate Assistant Commissioner who by an order dated June 30, 1955, confirmed the order of the Income-tax Officer refusing registration under section 26A of the Act. The matter was then taken up to the Income-tax Appellate Tribunal in three appeals. The Tribunal also came to the finding that the firm was not genuine and dismissed the appeals. This was on March 24, 1956. The appellant then moved the Tribunal for a reference to the High Court under section 66 (1) of the Act. The Tribunal held that no question of law arose out of its order and dismissed the applications. Thereafter, the appellant moved the High Court under section 66 (2) of the Act for directing the Tribunal to state a case on the following question of law :

"Whether on the facts and in the circumstances of the case the decision of the Tribunal that the firm is not genuine and not registerable under section 26A of the Indian Income-tax Act, is right in law ?"

4. Before the High Court the appellant contended that there were really no materials on which the assessing authorities could draw the inference that the firm was not genuine and their finding to that effect was based on suspicion, conjecture and surmises. The High Court rejected that contention, but observed : "It may be that if we were called upon to decide the question at issue we might have come to a different conclusion on the materials in the case, but that fact would not make the said question a question of law". In the result the High Court rejected the applications. The appellant then obtained special leave from this court, in pursuance whereof the present appeals have been preferred.

5. Learned counsel for the appellant has contended before us that an issue of law arises in this case, and he has put his case on the footing that on the facts found by the Tribunal, apart from mere suspicion and surmises, no such inference as has been drawn by the Tribunal reasonably follows; his argument is that the materials point only one way, and on such facts as the Tribunal has found no person acting judicially and properly instructed as to the relevant law could have come to the finding at which it arrived.

6. Learned counsel for the respondent has contested the correctness of the position taken up on behalf of the appellant, and he has pointed out that the question regarding which the appellant moved the High Court under section 66 (2) is different from the question which is now being

canvassed. It is true that by merely adding the words "right in law" to a question which is otherwise a question of fact does not make it a question of law. It is equally true that whether a firm is genuine or not is normally a question of fact. It is clear, however, that the grievance of the appellant is that the facts found by the Tribunal do not reasonably lead to the conclusion it has drawn and the conclusion is based on suspicion and surmise.

7. What are the facts which the Tribunal has found ? They may now be set out seriatim : (1) the two new partners, Nagaratnamma and V. Setty, contributed their share of the capital in the manner stated in the deed of partnership; (2) the capital account of V. Setty in the books of the partnership business showed, during the six years from 1948 to 1954, that he had accumulated profits of about 2 lakhs and had withdrawn about Rs. 3,000 a year in the two years 1950 and 1951 and Rs. 15,366, Rs. 12,864 and Rs. 12,058 respectively in the three years 1952, 1953 and 1954 respectively; (3) that the amounts withdrawn in 1950 and 1951 represented nationally the household expenses debited to his account, by reason of the fact that V. Setty lived then with his:

8. brother-in-law; (4) that the amounts withdrawn in 1952, 1953 and 1954 covered similar expenses as also expenses for improvement of a house which V. Setty had purchased in 1945; (5) that the appellant had not furnished full details of how the amounts withdrawn in those years were spent; (6) the account of Nagaratnamma showed that she had not withdrawn any part of her share of profits, which were separately shown in the account; and (7) she was an ordinary type of Hindu house- wife. The Tribunal also referred to the circumstances that K. R. Setty had been corresponding with the income-tax authorities on the footing that he was the proprietor of the business even after the commencement of the partnership; but that correspondence does not appear to have been made a part of the record, nor is there any mention of what K. R. Setty had actually stated and in what circumstances. On these facts the Tribunal stated its conclusion in the following words :

"On the above facts, we do not find it difficult to reach a conclusion that the partnership claimed on the basis of the deed dated November 16, 1949, is not genuine and that the deed is a document not intended to be acted upon. It may be so far as the outside world is concerned the three persons in question have held themselves out as partners, but that cannot by any means establish automatically the genuineness of the arrangement too. The actual conduct of the parties inter se is the essential point to bear in mind for this purpose. On the above facts, we hold that the firm is not genuine and accordingly not registerable under section 26-A."

9. Apart from the relation between the parties which is not in dispute, the Tribunal has not really referred to any conduct of the parties inter se which would indicate that the partnership was not genuine. The underlying assumption in the reasoning of the Tribunal seems to be that a partnership consisting of the wife and brother-in-law must be necessarily suspect and if the wife saves her profits and the brother- in -law does not spend his share of the profits fully, the inference must be that the partnership is a bogus partnership. On the materials placed before us, we consider that such an inference is unreasonable and not justified either by partnership law or common human experience. The books of partnership accounts were not held to be false; nor was it suggested that

there were no good reasons for taking the wife and brother-in-law as partners. It was accepted that both of them contributed their share of the capital, and it was not disputed that the brother-in-law managed the business, and at the relevant time lived with K. R. Setty. Learned counsel for the respondent suggested that the sum of Rs. 50,000 which Nagaratnamma contributed might not be her stridhanam in law. It is enough to point out that no such finding was given by the Tribunal; on the contrary, the Tribunal found that she contributed her share of the capital in the manner stated in the deed of partnership.

10. For these reasons, we think that a question of law arises out of the order of the Tribunal, namely, "whether in the facts and circumstances found by the Tribunal, there was material to come to the conclusion that the partnership firm constituted by the deed of partnership dated November 16, 1949, was not genuine ?" We would accordingly allow these appeals, set aside the order of the High Court of Mysore dated October 8, 1958, and direct that the Tribunal be required to state a case on the question indicated above and refer it to the said High Court. The appellant will be entitled to its costs of the High Court and of this court. There will be one set of costs in these appeals.

11. The appellant also filed three petitions for special leave under article 136 of the Constitution against the order of the Tribunal dated March 24, 1956, with applications for condonation of delay. These petitions were ordered to be put up with the three appeals, but no notice was given to the respondent. In view of our decision in the appeals, these petitions have become infructuous and are dismissed.

12. Appeals allowed.