

Calcutta High Court

Dawjee Dadabhoy And Co. vs Commissioner Of Income-Tax, ... on 20 March, 1962

Equivalent citations: 1963 49 ITR 698 Cal

JUDGMENT G. K. MITTER J. - This reference under section 66(1) of the Act is at the instance of the assessee, a firm which was denied registration under section 26A for the period January 1, 1953, to July 1, 1953.

Dawjee Dadabhoy & Co. was a firm composed of eight partners under a written agreement of November 14, 1949. There was a change in the constitution of the partnership in the year 1953, when two of the partners retired and a new partner was taken in. This was recorded in writing by a document styled "supplementary deed of partnership" bearing date July 2, 1953, executed by six out of eight partners who did not retire and the new partner who taken in. As the rights of the parties are regulated by these two documents it is necessary to note the relevant provisions thereof. The following are the relevant clauses of the deed of 1949 :

"Clause 2 :- The partnership business shall be carried on as long as the senior partners or a majority of them so desire provided that if any partner shall be desirous of retiring from the partnership at any time during the continuance of the partnership he shall be at liberty to do so only on the 30th day of June or the 31st day of December in any calendar year, and only on giving at least two months previous notice in writing ending with the 30th day of June or the 31st day of December, as the case may be, to the managing partners.... and immediately after the 30th day of June or the 31st day of December, as the case may be the partner giving such notice shall cease to be a partner and subject thereto the business of the partnership shall be continued by the remaining partners.

Clause 3 :- At the end of every year, that is to say, on the 31st day of December (or at the end of every period of six months, namely, on the 30th day of June and the 31st day of December if the partners or a majority of them so decide) a general account and balance-sheet shall be made by the partners who shall be at the head-office of the firm and also at each branch of the firm of all sales, purchases, receipts, etc., during the preceding year six months as the case may be."

The partners who retired were Esoof and Abdul Hamid and the new partner was one Ghulam Hossain.

The recitals in the supplementary indenture are as follows :

"Whereas the said Esoof and Abdul Hamid both desire to retire from the said partnership. Whereas it is provided in clause 2 of the deed of partnership dated November 14, 1949, that a partner shall be at liberty to retire only on the 30th day of June or the 31st day of December in any calendar year.

Whereas by mutual agreement of all concerned it is deemed expedient that Esoof and Abdul Hamid shall both be considered to have retired with effect from December 31, 1952.

Whereas the remaining parties of the partnership formed by the deed of partnership dated November 14, 1949, have agreed to take in and admit as a new partner in the said partnership

business the party, viz., Gulam Hossain, as and from January 1, 1953.

Whereas the parties have agreed to carry on the business on the same terms and conditions, stipulations as laid down in the deed of partnership dated November 14, 1949, and they hereby agree, accept and abide by all the articles numbered 1 to 40 as set out therein and whereas all the parties hereto including the newly admitted partner have agreed (as they hereby do) to admit and acknowledge correctness of the accounts and balance-sheet of the partnership business up to and including the 31st day of December, 1952, and each of them hereby agree not to raise any objection to the accounts as to correctness thereof or about any matter connected with the said business prior to January 1, 1953."

The operative portion of the supplementary deed shows that in pursuance of the above, the parties agreed to carry on the said business in the Union of the firm of Dawjee Dadabhoy & Co., under the supplementary deed of partnership, upon the same terms and conditions, stipulations, as are set out in the deed of partnership dated November 14, 1949.

The firm applied for registration under section 26A which was refused by the Income-tax Officer and the Appellate Assistant Commissioner. The Tribunal also rejected the appeal of the assessee holding that there was no proper distribution of profits in accordance with the deed dated July 2, 1953. The Tribunal further held that the firm was only entitled to registration with effect from the last-mentioned date, there being no partnership deed in operation from January 1, 1953, to July 1, 1953.

It appears that before the Tribunal the assessee prayed for production of two documents, viz., one dated December 31, 1952, and the other dated January 1, 1953. It is claimed that by the first of these documents the retirement of two partners which effect from December 31, 1952, was recorded and by the latter executed by the six continuing partners and the new partner it was provided that these seven partners would carry on the business of the firm with effect from January 1, 1953, and that a new instrument of partnership would be drawn up as quickly as possible and until execution of such an instrument the partnership would be covered by the agreement dated January 1, 1953.

The Tribunal declined to entertain or admit these documents at the hearing before it. If these documents were in existence the recitals in the supplementary deed are wholly inexplicable. Not only is there no mention of any document of the kind which the assessee wanted to place before the Tribunal, but the supplementary deed of partnership against the execution of any such document for the following reasons :

"(a) The first recital in the supplementary document is inconsistent with the desire of Esoof and Abdul Hamid to retire from the partnership before July, 1953.

(b) In view of the term in the deed of partnership of 1949 that a partner could only retire on the 30th day of June or the 31st day of December in any calendar year the parties concerned though it expedient that Esoof and Abdul Hamid should be considered to have retired with effect from December 31, 1952. In plain words it means that although no retirement had actually taken place on

December 31, 1952, the agreement was that their retirement should be taken to have occurred on that date.

(c) The fourth recital shows that the remaining partners agreement to take in and admit Gulam Hossain as a new partner was coeval with the supplementary deed."

The operative portion of the supplementary deed shows that the agreement to carry on the business of the partnership under the new constitution was arrived at the time of the execution of the document and excludes the possibility of the parties having agreed to constitute the new partnership on a date prior to July 2, 1953.

Section 26A provides as follows :

"26A. (1) Application may be made to the Income-tax Officer on behalf of any firm, constituted under and instrument of partnership specifying the individual shares of the partners, for registration for the purposes of this Act 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".

Formerly there was some difference of opinion as to whether "constituted under an instrument of partnership" in sub-section (1) meant "created by a deed of partnership". That has now been set at rest by the decision of the Supreme Court in R C Mitter & Sons v. Commissioner of Income-tax, holding that the word "constituted" did not necessarily mean "created" or "set up" but it might also mean "given legal or official form or shape" and that an application for registration under section 26A might be made not only by a firm which came into existence as from the date of a written agreement but also one created by word of mouth but subsequently clothed in legal form by reduction of the terms and conditions of the partnership to writing. By a majority the Supreme Court further held that "unless the partnership business was carried on in accordance with the terms of an instrument of partnership, which was operative during the accounting year, it cannot be registered in respect of the following assessment year." But at the same time the court made it clear that they were "not concerned with the further question whether the document should be in existence at the very inception of the accounting year, or before the year is out."

In the case before us the accounting year ended on December 31, 1953, the assessment year being 1954-55. We are not concerned with the question whether registration under section 26A could be had for the whole of the said accounting year as the reference is directed to the period of six months from January 1, 1953, to July 1, 1953, and our attention must be confined to that period only.

Under the Income-tax Act "firm", "partners" and "partnership" have the same attributes as they have under the partnership Act. Under section 4 of the partnership Act "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." In order, therefore, to constitute a partnership there must be an agreement to the effect by the several persons who want to unite for that purpose. Further, their agreement must be to carry on a business by all of them working together or by any them acting for all. From this latter proportion it follows that the partnership business can only spring into existence after the partners have agreed to unite. It may be open to them to adopt a business already in existence and carried on by any or all of them or even one carried on by strangers to the partnership who sever their connection with the business as from the date on which the partnership takes it over. In any of these cases, however the partnership business can only date from the moment the parties agree to unite. Although they can take over assets and liabilities of others in respect of a business carried on before the agreement of partnership is entered into, in the eye of law and specially income-tax law, the partnership business will be that carried on from the moment of the agreement. It is not open to the partners to extend the life of the partnership by saying that they will be considered to have been carrying on a business as from a date then past. The essence of partnership is an agreement to carry on business in partnership. It must necessarily follow that the life of the partnership cannot go beyond the date of this agreement.

It was, however, argued on behalf of the assessee that under the rules framed under the Indian Income-tax Act it was open to a body of persons to agree that the partnership business should be taken to have commenced from a date anterior to the agreement and that this proposition is supported by some decisions. Prima facie this seems opposed to reason and common sense and we have therefore got to examine the rules and decisions to find out whether that is so.

The Indian Income-tax Rules were framed by the Board of Inland Revenue in exercise of the powers conferred by section 59 of the Indian Income-tax Act. Under section 59(1), "The central Board of Revenue may, subject to the control of the Central Government make rules for carrying out the purposes of this Act and for the ascertainment and determination of any class of income." Under sub-section (5) of section 59, "rules made under this section shall be published in the official Gazette and shall thereupon have effect as if enacted in this Act". Rule 2 provides that "any firm constituted under an instrument of partnership specifying the individual shares of the partners may, under the provisions of section 26A of the Indian Income-tax Act 1922, ... register with the Income-tax officer, the particulars contained in the said instrument on application made in this behalf".

The rule further provides that "such application shall be signed by all the partners.... personally, or in the case of a dissolved firm by all persons... who were partners in the firm immediately before the dissolution and by the legal representative of any such partner who is deceased and shall for any year of assessment up to and including the assessment for the year ending on the 31st day of March 1953, be made before the 28th February, 1953, and for any year of assessment subsequent thereto be made -

(a) where the firm is not registered under the Indian Partnership Act 1932 (IX of 1932), or where the deed of partnership is not registered under the Indian Registration Act 1908 (XVI of 1908) and the application for registration is being made for the first time under the Act -

(i) within a period of six months of the constitution of the firm or before the end of the previous year of the firm whichever is earlier, if the firm was constituted in that previous year;

(ii) before the end of the previous year in any other case;

(b) whether the firm is registered under the Indian partnership Act 193 (IX of 1932), or where the deed or partnership is registered under the Indian Registration Act 1908 (XVI of 1908) before the end of the previous year of the firm and

(c) where the application is for renewal of registration under rule 6 for any year, before the 30th day of June of that year :

Provided that the income-tax Officer may entertain an application made after the expiry of the time-limit specified in this rule if he is satisfied that the firm was prevented by sufficient cause from making the application within the specified time."

Under rule 3 the application referred to in rule 2 has to be made in the form annexed to the rule. Under clause 3 of the specimen form of application it was open to the partners to say that the profits or loss, if any, of the previous year "will be divided or credited" as shown in section Of the Schedule. From this it was argued that the form contemplated the partnership having been in existence long before the date of application as also before the execution of the deed of partnership. I do not think that the use of the words "will be divided or credited" in paragraph 3 of the specimen form has any such effect. It is no doubt open to the partners to enter into an oral agreement of partnership first and to have the same recorded in writing later on. The schedule to the form itself shows that the date of admittance to partnership of each partner has to be given. It would not be open to any partner to say that he had been admitted to the partnership before a date on which all the partners including himself agreed to enter into partnership.

A partnership like any other contract can be entered into by means of correspondence so long as the letters spell out a concluded bargain sufficient for the purpose of section 26A of the Indian Income-tax Act; *Haridas Premji v. Commissioner of Income-tax*. more often however persons desiring to unite carry on oral negotiation which are then reduced to writing in the form of a deed of partnership. It may well happen that even when the parties have settled all the terms by which they are to be bound and have agreed to carry on business in pursuance thereof the drawing up of the formal document takes place some time afterwards. In such a case the partners may claim registration as from the date when they enter into the agreement to carry of the partnership orally and can have the firm registered under section 26A if the rules mentioned above are complied with but unless it is established to the satisfaction of the Income-tax Officer that there was an oral agreement which preceded the formal document the Income-tax Officer can only go by the document.

In *Dwarkadas Khetan & Co v. Commissioner of Income-tax*, an instrument of partnership was executed by four persons on March 27, 1946. Clause 3 of the deed of partnership recorded that "the partnership shall be deemed to have commenced from January 1, 1946, and shall continue until the

partners hereto decide unanimously in writing to terminate the same. "One of the partners who also executed this document was a minor. The learned judges of the Bombay High Court held, *inter alia*, that the instrument created a valid partnership between the three adult partners, the minor having been admitted to the benefits of the partnership. This was upset by the Supreme Court, the judgment being reported as *Commissioner of Income-tax v. Dwarkadas Khetan & Co.* With regard to the date from which registration was to have effect the learned judges of the Bombay High Court held that it should be "not by reason of the date of the instrument but in point of Act. If it came into existence on January 1, 1946, then it should be registered from that date. If it came into existence at a later date, then from such date." The learned judges did not hold that the registration should have effect from January 1, 1946, in terms of clause (3) of the deed of partnership. The Supreme Court however did not come to any finding on this question as in their opinion the answer to the first question was sufficient to dispose of the appeal. In delivering the judgment of the Bombay High Court, Chagla C.J. observed : "What must not be overlooked is that what is sought to be registered is not the instrument of partnership but the firm, and the firm is seeking registration for the purpose of certain indulgence which is shown to a registered firm and if the firm can satisfy the authorities that it was carrying on business during the accounting period, then the fact that the partnership deed was executed subsequently can have no bearing on the question of registration." With respect, I agree with the first part of the observation but the second part must be subject to the qualification that the execution of the deed must not be beyond the period prescribed under the rules.

Reliance was placed by the learned advocate for the assessee on the case of *K. Acharya v. Commissioner of Income-tax*. In this case one A who was carrying on business as the sole proprietor of it took in some of his employees as partners and had a deed of partnership drawn up on December 27, 1945, to record the said fact. One of these persons described as partners was Rabindra Nath Prodhan, a minor. The shares of the partners were specified in the document. Subsequently, on July 25, 1951, the same persons including the minor purported to execute another deed of partnership. By yet another document dated February 28, 1952, described as a deed of rectification of the deed of partnership dated July 25, 1951, it was declared by the four major partners that Rabindra Nath Prodhan was only "a minor admitted to the benefits of the partnership till he attains majority." An application was then made for registration of the partnership business. The Income-tax Officer rejected it on the ground that the minor had not merely been admitted to the benefits of partnership. The Income-tax Tribunal upheld this order. One of the question framed for decision by the court was whether, on the facts and in the circumstances of the case, registration under section 26A should have been granted to the firm as constituted by the deed dated July 25, 1951, and the deed rectification dated February 28, 1952, for any one or more of the assessment years 1951-52, 1952-53 and 1953-54. The Orissa High Court held that the Tribunal had failed to consider the effect of the deed of rectification. It found that the assessee could not claim registration for the year 1951-52 as the Appellate Assistant Commissioner had found that the partnership was created only from July 25, 1951, several months after the expiry of the financial year 1950-51. On the view that the partnership came into existence on July 25, 1951, the court held that the assessee was entitled to registration for the year 1952-53 as the instrument of partnership had been in existence in the accounting year in respect of which the assessment was being made. This conclusion was based on this reading of the judgment of the Supreme Court in *R. C. Mitter v. Commissioner of Income-tax*. The court also relied on the departmental instructions issued by the Central Board of

Revenue which indicated that "so long as the partnership was genuine, registration should not be refused merely on the ground that the instrument of partnership was drawn up after the commencement of the year." The court also held that the firm was entitled to registration for the year 1953-54. So far as registration for the assessment year 1952-53 is concerned the judgment seems to be against the decision of the Supreme Court in N. T. Patel & Co. v. Commissioner of Income-tax.

I do not see how these judgments help the assessee before us. So far as the Orissa case is concerned if the deed of rectification dated February 28, 1952, cured the defect in the deed of partnership dated July 25, 1951, as held by the High Court, there was a partnership constituted under the deed. The court treated the firm as having been in existence from the commencement of the year previous to the assessment year 1952-53.

In the present case if it had been shown before the income-tax authorities including the Tribunal that the seven persons had entered into an agreement of partnership and carried on business together as a firm from January 1, 1953, to July 1, 1953, we would have answered the question in favour of the assessee. But unfortunately on the material before us we cannot possibly take that view.

In the result the question framed : "Whether on the facts and in the circumstances of the case the assessee was entitled to registration for the period from January 1, 1953, to July 1, 1953 ?" must be answered in the negative. The assessee must pay the costs of this reference.

RAY J. - I agree.

Question answered in the negative.