

Kalu Ram and Co. (HUF) and Kalu Ram and Co. (FIRM) Vs Commissioner of Income Tax

Court: Delhi High Court

Date of Decision: Dec. 21, 2000

Citation: (2002) 254 ITR 307 : (2001) 115 TAXMAN 499

Hon'ble Judges: Dr. Arijit Pasayat, C.J; D.K. Jain, J

Bench: Division Bench

Advocate: R.P. Bansal and Bharati Pawar, for the Appellant; R.C. Pandey, Ajay Jha and Prem Lata Bansal, for the Respondent

Judgement

D. K. Jain J.

1. On being moved by the assessed u/s 256(1) of the Income Tax Act, 1961 (for short "the Act"), the Income Tax Appellate Tribunal, Delhi

Bench-A (in short "the Tribunal"), has referred the following questions for the opinion of this court:

1. Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was justified in upholding the order of the

Income Tax Officer refusing to grant registration to the firm of Kalu Ram and Co. ?

2. Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was justified in holding that the income arising

from contract was rightly assessed in the hands of the Hindu undivided family of Kalu Ram and Co. ?

2. The two references, pertaining to the assessment year 1972-73, arise out of two appeals filed by Kalu Ram and Co. (Firm) (hereinafter referred

to as "the firm") and Kalu Ram and Co. (HUF) (hereinafter referred as "the HUF"). The previous year relevant to the said assessment year ended

on March 31, 1972, in both the cases. The business was originally carried on by the Hindu undivided family. There were three members in the

Hindu undivided family, namely, Bal Kishan (karta), his brother, Bharat Singh and their mother, Smt. Kishan Pyari. The income from the business

was assessed in the hands of the Hindu undivided family up to the assessment year 1971-72. On March 22, 1972, a deed of partnership was

drawn up Constituting the firm, consisting of all the above three persons as its partners. In the said deed, Bal Kishan was described as party of the

first part, Bharat Singh as party of the second part and Smt. Kishan Pyari as party of the third part. The preamble to the deed read as under :

Whereas the party hereto of the first part took the works of contract, namely, (i) supply of 18000 cu.m. of 1 1/2" gauge stone ballast (3.8 cm)

and 1500 cu.m. of 1" gauge stone ballast (2.5 cm.) duly stacked and loaded into rail borne trucks at Tughlakabad (Zone No. 1) approximate

contractor value Rs. 4,74,405 only, and (ii) supply of 18000 cu.m. of 1 1/2" gauge stone ballast (3.8 cm.) and 1500 cu.m. of 1" gauge stone

ballast (2.5 cm.) duly stacked and loaded into rail borne trucks at Tughlakabad (Zone No. 3) approximate contractor value of Rs. 4,86,300 only.

And whereas party hereto of the first part took the aforesaid works of contract in his name in his capacity as a karta of the Hindu undivided family,

known as Kalu Ram and Co., and started carrying on the same with the funds of the said Hindu undivided family.

And whereas the party hereto of the first part has been carrying on the said business.

And whereas on 1st of April, 1971, the party hereto of the first part agreed to take the parties hereto of the second and third parts as partners and

continued to carry on the said business in partnership with them subject to certain terms and conditions which will regulate their rights, relations and

mutual obligations.

3. The profit-sharing ratio of the above three persons in the said partnership deed was shown as under :

(1) Bal Kishan 30 per cent.

(2) Bharat Singh 30 per cent.

(3) Smt. Kishan Pyari 40 per cent

4. Clause 6 of the deed stipulated that the capital required by the partnership shall be provided for by the parties hereto as and when required and

in such proportion as may be actually agreed upon from time to time. As a matter of fact, the entire capital of the business, formerly run by the

Hindu undivided family, amounting to Rs. 38,538, became the capital of Bal Kishan. A deposit of Rs. 2,000 in the books of the Hindu undivided

family in the name of Bharat Singh was treated as the capital of Bharat Singh. He made a further deposit of Rs. 4,000 on March 2, 1972, but the

entire amount of Rs. 6,000 was withdrawn by him on March 26, 1972, i.e., before the end of the relevant previous year. Smt. Kishan Pyari did

not contribute any capital. On the contrary, her account showed that she had withdrawn Rs. 3,000 on April 1, 1971, and another sum of Rs.

10,000 on February 9, 1972. Thus, she had a debit balance in her account.

5. The firm submitted an application in Form No. 11 for grant of registration u/s 184 of the Act on March 25, 1972, along with a certified copy of

the said partnership deed dated March 22, 1972. The Income Tax Officer (in short "the ITO") was of the view that the firm was not genuine and

the entire income of the business was required to be assessed in the hands of the Hindu undivided family as it was the real owner of the business.

He was of the view that the karta of the Hindu undivided family was not competent to enter into partnership with other members of the family to

carry on the joint family business and that any such agreement was void ab initio. On the facts the Income Tax Officer found that the alleged firm

had not opened any new bank account; it had been carrying on business on the old bank account standing in the name of the Hindu undivided

family ; no separate books of account had been maintained for the business of the firm ; even the refund of security deposit with the railways with

respect to the contract undertaken by the Hindu undivided family for the previous two assessment years had been deposited in the books of the

firm. Observing that once a business had been assessed to tax as belonging to the Hindu undivided family, it would continue to be assessed as such

until it was shown that a partition had taken place with reference to that business and an order to that effect had been recorded by the Income Tax

Officer u/s 171(3) of the Act, the Income Tax Officer came to the conclusion that no genuine firm had come into existence. He, accordingly,

refused to allow the benefit of registration to the firm. Since the return had been filed in the status of a firm, the Income Tax Officer made a

protective assessment on it in the status of an unregistered firm and made a separate assessment on the Hindu undivided family including therein the

income declared by the firm.

6. Both the Hindu undivided family and the firm took the matter in appeals to the Appellate Assistant Commissioner (in short "the AAC"). The

Appellate Assistant Commissioner found that all the formalities necessary for seeking registration had been complied with by the firm. He observed

that the income tax Officer had expressed no doubt about the genuineness of the firm on the merits. Finding that the said persons had been

assessed separately with reference to the share income derived by them from the firm, he held that the firm was entitled to the status of a registered

firm.

7. Being aggrieved by the order of the Appellate Assistant Commissioner, the Revenue took the matter in further appeals to the Tribunal. Dealing

with the first question as to whether the karta of the Hindu undivided family could validly enter into partnership with other members of the family,

the Tribunal held that in the light of the principle of law laid down by the Supreme Court in the case of Firm of Bhagat Ram Mohanlal Vs. The

Commissioner of Excess Profits Tax, Madhya Pradesh, Nagpur and Another, , the Income Tax Officer had taken the correct view of law that Bal

Kishan could not enter into partnership with Bharat Singh and Smt. Kishan Pyari with reference to the property belonging to the Hindu undivided

family and, Therefore, the alleged partnership was clearly illegal and invalid and could not be allowed the benefit of registration. Regarding the

genuineness of the firm, the Tribunal recorded the following findings :

Although, our above finding is sufficient to dispose of the present appeal, but in deference to the parties, we may give our finding on the other

issues also. We do not agree with the observations of the Appellate Assistant Commissioner that the Income Tax Officer had raised no doubt

about the genuineness of the firm. The Income Tax Officer clearly stated in his orders under Sections 143(3) and 185 of the Act that the firm had

not opened a new bank account and that it had carried on the bank account originally standing in the name of the family and that the receipts from

the contract undertaking were all deposited in this bank account. He also observed that no separate books of account for the firm's business had

been maintained and that the refund of the security deposit with respect to the contract undertaken by the family for the previous two assessment

years had been deposited in the books of the alleged firm. Similarly, he pointed out that the contract originally taken in the name of the karta as

representing the family had been carried on as the business of the alleged firm. In our opinion, on these facts also, it cannot be said that a genuine

firm had come into existence. Smt. Kishan Pyari had been allowed 40% share in the business without contributing any capital as in fact her account

showed a debit balance. There is no consideration for allowing her such a heavy share except that the assessed wanted to divert a part of the

income to her, to save incidence of tax. We cannot persuade ourselves to hold that the assessed was a genuine firm only on the ground that all

other legal formalities had been duly complied with as they are not conclusive in the matter.

8. Accordingly, the Tribunal set aside the order of the Appellate Assistant Commissioner and restored the order of the Income Tax Officer

disallowing registration to the firm. As a consequence, the order of the Appellate Assistant Commissioner in the Hindu undivided family's appeal

quashing the assessment in the hands of the Hindu undivided family was also reversed.

9. As noticed above, on the motion of the assessed, the aforementioned questions have been referred for our opinion.

10. We have heard Mr. R. P. Bansal, the learned senior counsel for the assessed, and Mr. R. C. Pandey for the Revenue.

11. It is submitted by the learned senior counsel for the assessed that there was no disability for the karta of the Hindu undivided family to enter

into partnership with other members of the family or even with a stranger. It is also asserted that the Income Tax Officer had not brought any

material on record to hold that the firm was not genuine. Merely because the firm had used the bank account of the Hindu undivided family, it did

not mean that a genuine firm had not come into existence. The learned counsel for the Revenue, on the other hand, contended that the view taken

in this behalf by the Tribunal was correct.

12. The special provisions applicable to firms, as they existed prior to April 1, 1993, i. e., up to the assessment year 1992-93, are contained in

Part B of Chapter XVI of the Act. The procedure for grant of registration to firms is contained in sections 184 and 185 of the Act. In order to

obtain registration for the purposes of the Act an application is to be filed on behalf of the firm if the partnership is evidenced by an instrument and

that instrument specifies the individual shares of the partners and the application is to be signed by all the partners, (not being minors personally).

On receipt of such application, the Assessing Officer is obliged to enquire into the genuineness of the firm and its constitution as specified in the

instrument of partnership. If, on such enquiry, he is satisfied that there is in existence a genuine firm with the constitution so specified, he is obliged

to pass an order in writing u/s 185 of the Act, registering the firm. If, however, he is not satisfied, he has to pass an order in writing refusing

registration to the firm. In other words, in order to obtain registration of a firm it is not only mandatory for the assessed to file an application and

declaration on behalf of and signed by all the partners along with an instrument of partnership, specifying the individual shares of the partners, it is

equally obligatory for the Assessing Officer to enquire into the genuineness of the firm. Whether a firm is genuine or not is a pure question of fact. It

is for the Assessing Officer in the first instance and the Tribunal, as a final fact-finding authority, to reach a final finding on this question (see

Ratanchand Darbarilal Vs. Commissioner of Income Tax, M.P.,).

13. In the instant case, although the partnership was evidenced by an instrument of so-called partnership specifying the individual shares of the

three parties but the truth of actual partnership coming into existence was seriously disputed by the Assessing Officer. As noted above, the

Tribunal, while noticing the factual aspects, highlighted by the Income Tax Officer, viz., the non- maintenance of any independent bank account by

the firm; the nature and the extent of capital contribution by the parties, etc., has recorded a categorical finding that no genuine firm had come into

existence. The Tribunal had observed that Smt Kishan Pyari had been allotted 40 per cent, share in the business without contributing any capital

and there was no consideration for allowing her such a heavy share except that the firm wanted to divert a part of its income to her to save

incidence of tax. In our view, these are pure findings of fact recorded by the Tribunal, which, as is evident from the format of the questions

referred, have not been challenged by the assessed by raising a specific question in that behalf. Since the questions referred speak of ""on the facts

and in the circumstances of the case"" , this court, in the exercise of advisory jurisdiction u/s 256 of the Act cannot go behind or question the

statement of facts drawn by the Tribunal (see Karnani Properties Ltd. Vs. The Commissioner of Income Tax, West Bengal,). The aforementioned

findings of fact arrived at by the Tribunal are binding on both the parties and the question referred has to be answered on the facts so found by the

Tribunal. In the light of the facts found by the Tribunal, the irresistible conclusion is that since no genuine firm had come into existence, registration

to the firm for the purposes of the Act was rightly declined by the Income Tax Officer.

14. In view of our conclusion on the question of genuineness of the firm, we feel that it is not necessary to go deeper into the other issues raised by

the Income Tax Officer, namely, whether Bal Kishan, as karta of the Hindu undivided family, was competent to enter into partnership with other

members of the family to carry on the same joint family business as a firm, constituted of all the members of the Hindu undivided family.

Nevertheless, there is substance in the stand of the Revenue to the extent that in the present case for converting the Hindu undivided family

business into a partnership there had to be a division between the coparceners qua the joint family business, although it was not necessary to

disrupt the Hindu undivided family as a whole. It is true that the Hindu law or the Act does not impose any disability upon the members of a Hindu

undivided family in the matter of entering into a contract inter se, as is pleaded by learned counsel for the assessed. They can enter into a valid

partnership, provided they put into the partnership by way of their capital their separate property or the property which they might have obtained

as a result of a partition, complete or partial, of the joint property. That was the view taken by the Privy Council in (1948) 16 ITR 35 (Privy

Council) , wherein it was held that the karta of a joint family could enter into partnership with an individual member of the coparcenary qua his

separate property. This view was approved by the apex court in Firm of Bhagat Ram Mohanlal Vs. The Commissioner of Excess Profits Tax,

Madhya Pradesh, Nagpur and Another, and in other cases. But it is well settled that before entering into such partnership, the prerequisite is the

partition of that joint family asset, which is sought to be introduced as capital of the partnership so that it acquires the character of a separate

property. Admittedly, in the present case, there was no such partition. As noticed above, the entire capital of the business of the Hindu undivided

family was treated as the capital of Bal Kishan and none of the other partners contributed any capital in the firm. The capital asset invested in the

business of the firm was joint family property and was not partitioned. In the circumstances, we feel that the business of Government contract

awarded to the Hindu undivided family continued to be the business of the Hindu undivided family and it did not transform itself into a partnership

business of the firm. We are in agreement with the Tribunal that no partnership came into existence in law.

15. In the light of our answer to the first question, the necessary corollary is that the view of the Tribunal to the effect that the income arising from

the contract was to be assessed in the hands of the Hindu undivided family, is also correct.

16. For the foregoing reasons, our answer to both the questions referred to us is in the affirmative, i. e., in favor of the Revenue and against the

assessed. There will, however, be no order as to costs.