(1961) 12 MAD CK 0011

In the Madras High Court

Aruna Group of Estates APPELLANT

Vs

The State of Madras RESPONDENT

Date of Decision : 06-12-1961

Acts Referred:
Tamil Nadu Agricultural Income Tax Act, 1955 — Section 27

Citation : (1962) ILR (Mad) 990 : (1962) 75 LW 799 : (1962) 2 MLJ 294

Hon'ble Judges : Jagadisan, J

Bench : Division Bench

Judgement

Jagadisan, J.—The Agricultural Income Tax Officer, Batlagundu, refused registration of a firm u/s 27 of the Madras Agricultural Income Tax

Act for the Agricultural Income Tax year 1957-1958 in respect of a firm alleged to consist of 15 partners, of whom one was a minor entitled only

to the benefits of partnership. This decision was affirmed both by the Assistant Commissioner of Agricultural Income Tax, Madurai, and the

Agricultural Income Tax Appellate Tribunal, Madras. In this Tax Revision Case the correctness of the said decision is challenged.

2. The facts that led to the application for registration are quite simple and are not in controversy. Anina Group Estates, Bodinaickanur, is the name

of a firm and the firm was originally constituted with five partners who had entered into a partnership agreement, dated 13th April, 1950. The firm

owned plantations of cardamom and other agricultural and horticultural products. The names of the partners and their respective shares were as

detailed below:

I. A.S. Subbaraj .. 7/12. 2. A. Narayanan .. 1/12. (3) A.S.R. Kanakaraj .. 1/12. 4. A.S. Suppan Chettiar .. 1/12. 5 K. M. S. Mallayyan Chettiar

... 2/12.

The capital of the partnership was Rs. 4 lakhs, which was contributed mainly by A.S. Subbaraj, who was the major sharer. This partnership was

accepted by the Agricultural Income Tax Department and was registered for the assessment years, 1955-56 and 1956-197. On 23rd November,

1955 a fresh partnership was entered into, the terms whereof were embodied in a written instrument. The names of the partners under this new

partnership and their respective shares are as detailed below:

1. A.S. Subbaraj .. 7/48.

2. S. Srinivasan .. 7/48

3. S. Baskaran .. 7/48 ....

4. A. Narayanan .. 1/12

5. A.S. R. Kanakaraj .. 1/12

6. S. Kasiraj .. 1/48

7. S. Dorairaj .. 1/48

8. S. Natarajan .. 1/48

9. S. Mohan .. 1/48

10. K.M.S. Mallayyan Chettiar .. 1/30

11. K.M.S. Surulinathan Chettiar .. 1/30

12. K.M.S. Subbiah Chettiar .. 1/30

13. K.M.S. Narayanaswami Chettiar.. 1/30

14. S. Sethuram .. 1/30

15. S. Subbiah .. 7/48)(minor admited to the benefits of partnership).

Numbers 2, 3 and 15 are the sons of A.S. Subbaraj. The original share of A.S. Subbaraj, namely, 7/12 was claimed to have been divided equally

in a family partition between Subbaraj and his three sons. Numbers 4 and 5 were already partners and they retained their previous shares of 1/12

each. Numbers 6 to 9 are the sons of A.S. Suppan Chettiar, partner No. 4 in the previous partnership, and they claimed to have obtained the

share of Suppan Chettiar equally amongst themselves by reason of Suppan Chettiar having renounced his share in the partnership. No. 10 was one

of the original partners and numbers 11 to 14 are the brothers and nephew of

No. 10 Mallayyan Chettiar. Numbers 10 to 14 were members of a

Hindu undivided family and they claimed to have acquired 1/30 share each as a result of family division of the 2/12th share of Mallayyan Chettiar in

the original partnership.

3. The partition arrangement in Mallayyan Chettiar''s family is evidenced by a document dated 14th November, 1950, which provides that the

income accruing from the 2/12th share in the Aruna Group'' Estates shall be divided into five shares among the five sharers. The Tribunal has

accepted this partition arrangement as true and valid.

4. Admittedly there was a partition between A.S. Subbaraj and his three sons. The partition deed, dated 14th January, 1955, between the

members of the family of Subbaraj undoubtedly establishes a division amongst them. The 7/12th share of Subbaraj in the Aruna Group Estates is

described in the H Schedule attached to that partition deed. Clause 9 of that deed dealing with Aruna Group Estates reads thus:

The H Schedule property (Aruna Group Estates) which is worth Rs. 3,18,500 is not in a position to be divided and is being enjoyed in co-

ownership with others. As has been done upto the present that property will be kept undivided and the share of the profits that will accrue to my

family will be enjoyed by myself and my male issue. When necessity arises in the future, the share that belongs to my family in this property will be

divided between myself and Such of my male issue as exist at that time.

It is to be noted that this partition deed expressly provides for the continuation and preservation of the 7/12th share in Aruna Group Estates as an

undivided family asset.

5. In the partnership deed, dated 23rd November, 1955, of which registration was sought there is definite declaration that Subbaraj and his three

sons are each entitled only to a 7/48th share. The preamble to that document recites:

Whereas No. 1. A.S. Subbaraj as a member of the joint family consisting of Nos. 1 to 3 and 15 having acquired the estate known as Aruna Group

Estates....at a cost of Rs. 4,00,000.... and having effected subsequently a partition of the family effects (No. 15 being minor is admitted to the

benefits of the partnership).

It is quite obvious that though A.S. Subbaraj and his sons kept the 7/12th share undivided in the partition arrangement dated 14th January, 1955,

they divided it at or about the time when the new partnership was constituted on 23rd November, 1955.

6. A.S. Suppan Chettiar, partner No. 4 in the first partnership, retired from the partnership and is not a partner in the newly constituted firm. His

place and his share have been taken by his four sons each taking 1/48th share. Suppan Chettiar wrote a letter dated 1st July, 1955, to A.S.

Subbaraj, the managing partner of the firm in these terms:

I have given my share in the Aruna Group Estates (1/12 share) to my four sons, viz., Messrs. S. Kasiraj, S. Dorairaj, S. Nataraj and S. Mohan

with effect from 1st July, 1955 in equal proportion, I shall be thankful if you please transfer my share to them equally and admit them as partners in

the above firm in my place.

7. We shall now refer to the reasoning adopted by the Tribunal in negativing the relief of registration sought for by the partners of the new firm. The

application was in substance one for registration and not for renewal of the pre-existing registration of the original firm. Though the business of the

old partnership was continued the old firm has been reconstituted and the structure of the newly constituted firm being different from that of the old

firm, there can be no question of renewal of registration. The Tribunal relied upon the terms of the partition deed dated 14th January, 1955

between Subbaraj and his sons as affording conclusive evidence of Subbaraj and his family owning the 7/48 share as only an undivided family

asset. In that view the Tribunal refused to accept the existence of a genuine partnership as constituted by the deed, dated 23rd November, 1955.

This is what the Tribunal observes in dealing with the division between Subbaraj and his sons:

It is incongruous that the Aruna Group Estates is kept undivided for the purpose of family division, but a division is alleged for the purpose of

admitting new partners into the partnership. The recital in the partnership deed about the specific shares of A.S. Subbaraj and his sons, is

inconsistent with the recital in the partition deed that the share of Subbaraj''s family in the Aruna Group Estates, was not divided and that the

income was to be enjoyed in common. This makes us hold that the recital in the partition deed was a make-believe affair alleged with a view to get

the income split up into smaller shares, either to secure a lower rate of Income Tax or make the income of particular shares fall below the taxable

minimum and therefore escape the assessment altogether....the recital in the partnership deed about the share of A.S. Subbaraj being redistributed

in particular shares among his sons, is not bona fide and consequently has to be rejected for the purpose of assessment.

In regard to the claim of Suppan Chettiar''s four sons being partners holding 1/48 share each, the Tribunal took the view that the transfer from

Suppan Chettiar to his sons was a device lacking in bona fides resorted to for obtaining the benefit of a lower rate of tax or to get exemption

altogether from assessment. We have now to examine the soundness of these reasons given by the Tribunal for not affording relief of registration

prayed for by the partners of the firm.

8. It will now be convenient to refer to the provision'' of the Statute (Madras Agricultural Income Tax Act, 1955). Section 27 provides for

registration of a firm. That section reads as follows:

1. Application maybe made to the Agricultural 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 purposes of this Act and of any other enactment for the time being in force relating to

agricultural Income 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 Agricultural Income Tax Officer in such manner as may be

prescribed.''

''Prescribed '' means '' prescribed by rules under the Act.'' The relevant rules are Rules 16, 17 and 18. It is not necessary to set out Rules 16 and

17. Rule 18 reads as follows:

(a) ""On receipt of an application under Rule 16, the Agricultural Income Tax Officer shall, if he is satisfied that the application is in order, and that

there is or there was a firm in existence Constituted as shown in the instrument of partnership, grant to the assessee a certificate signed and dated by him and also bearing his official seal in the following form at the foot of the instrument or certified copy.

(b) If the Agricultural Income Tax Officer is not satisfied, he shall pass an order in writing refusing to recognise the instrument of partnership or the

certified copy thereof and furnish a copy of such order to the applicants.

Section 27 provides for the following requisites to be complied with : 1. There must be an application made on behalf of the firm sought to be

registered. 2, The firm must be constituted under an instrument of partnership. 3. The instrument must specify the individual shares of the partners.

Rule 18 requires that the Agricultural Income Tax Officer should be satisfied that the application is in order, and that there is or there was a firm in

existence constituted as shown in the instrument of partnership. The vital question, and perhaps the only question, which has to be decided by the

Officer is the existence or otherwise of a firm in accordance with the tenor and the terms of a written instrument of partnership. If there is no firm in

existence and the deed is a mere make-believe and a fiction, or if there is a firm but not in accordance with the terms of the deed, the application

for registration must fail.

9. In the present case there is no finding by the subordinate Tribunals that the firm as constituted under the written instrument dated 23rd

November, 1955, is not genuine, or that the parties to that document never agreed or intended to constitute themselves into a firm. The original

partnership consisting of five members was accepted as a genuine partnership, and was registered as such by the Agricultural Income Tax Officer

for the two previous years preceding 1957-58. In the new partnership, which was sought to be registered there was only a re-distribution and re-

allocation of the shares of the original partners. The taxing authorities and the Appellate Tribunal did not find any difficulty in the matter of re-

distribution of the 2/12 share of K.M.S. Mallayyan Chettiar. In regard to the share of A.S. Subbaraj, the view that has been taken by the

Subordinate Tribunals is that there was no partition between him and his sons regarding the 7/12 share. We have no doubt that the plea of division

between Subbaraj and his sons ought not to be repelled merely on the ground that the deed of partition kept it as a joint asset. Members of a joint

family can bring about a division even without an instrument of partition. Every member of a Hindu undivided family has the indefeasible birthright

of becoming divided and he can exercise that right by an unequivocal declaration of his intention to do so. This is purely a matter of volition on the

part of any member and the personal law, the Hindu Law, does not prescribe the time, place, manner or form for its exercise. If the members of

the family sever their joint status the severance is complete and valid, and it cannot be ignored on grounds of lack of bona fides. We are unable to

see why the very declaration contained in the partnership deed by which Subbaraj and his three sons unequivocally declared that each is entitled

only to 7/48 share should not itself be regarded as having brought about a division amongst themselves of the quondam 7/12 undivided share.

10. The Tribunal seems to have been considerably obsessed by the supposed motive of Subbaraj and his sons of lessening the incidence of

taxation in holding that there was no partition between them. A partition cannot be vitiated by a bad motive or a mala fide object. It may be an

obstacle to a creditor seeking remedies in the execution of a decree or to a taxing authority levying a tax but nonetheless it is effective and cannot

be put aside. Let us assume that Subbaraj and his sons desired to lighten their tax burden by exercising their undoubted right to disrupt the joint

family, and let us also assume that the giving effect to the partition will reduce their tax liability. But there is nothing wrong or illegal about it.

Avoidance of tax is not tax evasion and it carries no ignominy with it for it is sound law and, certainly, not bad morality for anybody to so arrange

his affairs as to : educe the brunt of taxation to a minimum. On the materials on record, we are clearly of opinion that there is sufficient proof of

Subbaraj and his sons having become divided, though not under the terms of the written partition deed but by reason of their subsequent

declaration and conduct, and that each of them is entitled to a share of 7/48 and that there is no impediment to recognise them as partners holding

the shares specified in the instrument of partnership.

11. The next question for consideration is whether registration can be refused on the ground that Suppan Chettiar''s sons have not validly derived

their respective shares by any transfer of title from Suppan Chettiar. It is true that the only evidence on record which enables the sons of Suppan

Chettiar to claim his share is the letter already referred to. It is always open to any partner to retire from the firm yielding his place to his nominee

or nominees. If all the other partners of the firm agree to this retirement and substitution of the new partner or partners, a new partnership springs

into existence. The absence of any valid document of transfer from Suppan Chettiar to his sons, we do not say that the letter of Suppan Chettiar is

not enough, cannot really affect the question whether the sons of Suppan Chettiar became partners of the new partnership each holding 1/48 share.

The terms of the partnership deed dated 23rd November, 1955 do not indicate that the sons of Suppan Chettiar were mere dummies either for the

other partners or for Suppan Chettiar, who was not eo nomine a partner.

12. The formation and constitution of a partnership can in no way be affected by the fact that one of the partners is a benamindar for a stranger or

that a partner holds his share as a manager of his joint family, or that a partner has agreed to give a portion of his share to another by constituting a

sub-partnership with him. These are incidents which are outside the scope of partnership arrangement and have no bearing on the truth or reality of

the partnership as such.

13. In the decision reported in Bagyalakshmi and Co. Vs. Commissioner of Income Tax, Madras, , which arose u/s 26-A of the Indian Income

Tax Act, a provision in pari materia with Section 27 of the Madras Agricultural Income Tax Act, it was held that a division in the family of two of

the partners of a firm whereby the shares of the partners became divided between the members of the family, cannot affect the position of the

partners in the firm, and give room for cancellation of the registration of the firm. One of us was a party to that decision, and we wish to quote the

following observation at page 741:

... where the partition arrangement is a make-believe affair with a view to avoid the incident of heaver taxation, the Department is entitled to look at

the real state of things. For instance, if in a partnership composed of A, B and C it is found as a fact that B and C are mere name lenders and that

A alone is the real owner of the shares nominally shown against B and C, it would obviously be only a device to avoid the incident of heavier

taxation. In such a case, there would be no partnership in existence. In other cases of a similar nature it might turn out that one member is entitled

to a larger share than what he is shown to possess.

We are of opinion that this decision does not lay down the proposition of law that where A, B, and C are partners of a firm truly and genuinely the

registration of that firm can be refused on the ground that one of the partners is a mere benamidar for a stranger to the partnership. If any partner is

only a benamidar for another, it can only mean that he is accountable to the real owner for the profits earned by him from and out of the

partnership. But his benami character does not affect his capacity as partner or his final relationship with the other members of the partnership.

14. We wish to refer to the decision of the Gujarat High Court in Commissioner of Income Tax, Bombay North Vs. A. Abdul Rahim and Co., , as

we are of opinion that the ratio of that decision will govern the present case. In that case there were three partners, V, R and M, in a firm. The firm

was registered u/s 26-A of the Indian Income Tax Act. A new deed of partnership was. executed by these three partners V, R and M and a newly

added partner, A who was the nephew of V. Under this deed the shares of V and A were 7 annas and 2 annas and these of R and M, the original

partners were as before 5 annas and 2 annas. The original share of 9 annas belonging to V was split up into 7 annas for V and two annas for his

nephew A, who joined the firm as a partner. An application was made for registration of the newly constituted firm. The Income Tax Officer held

that the new partner was only a benamidar for V and that the bringing in of a new partner was a mere device to defeat the taxable income of V. He

refused registration. On appeal the Appellate Tribunal held that one of the partners had given a small portion of his share to his nephew without

disturbing the main structure of the firm but, that that was not believed, and that fact could not affect the structure of the firm which continued as

before and that registration ought not to have been refused. The Gujarat High Court held that the firm constituted under the new deed of

partnership could be registered u/s 26-A of the Act. At page 2,0 the learned Chief Justice observed as follows:

If the deed correctly records what is agreed upon amongst all the partners, it cannot be said that the deed is in any sense incorrect and if an

application for registration of the firm is made which correctly sets forth what is stated in the instrument of partnership, then it cannot be said that

any of the particulars given in the application are incorrect and that the firm is not entitled to. have itself registered by reason thereof. There might be arrangements secret or otherwise arrived at between some of the partners, as regards the shares held by them in connection with the business of

the partnership. A partner might be holding his share as a member of a joint and undivided Hindu family. A partner might be a benamidar for an

outsider in connection with the whole or part of his share in the partnership. A partner may have a sub-partner in connection with the share held by

him. A partner may not hold the whole beneficial interest in the profits coming to his share. There might be a divergence between the legal

ownership and the beneficial ownership in respect of the amount of profit which may come to the share of a partner. . . It is not possible to refuse

registration to a firm merely because a partner may have dealt with the beneficial ownership in respect of his share in any particular manner.

With respect, we agree that this principle of law, should govern the application for registration of a firm either under the Indian Income Tax Act Or

under the Madras Agricultural Income Tax Act. In our opinion the application for registration preferred by the partners of the deed dated 23rd

November, 1955, ought to have been granted u/s 27 of the Act.

15. The last question that has to be considered is whether the deed dated 23rd November, 1955, should have retrospective operation from 1st

July, 1955. The Tribunal has observed that there is no evidence of the partnership having come into existence even on 1st July, 1955. It is true that

a partnership can be constituted orally and then the agreed terms can be embodied subsequent to the formation of the partnership in a deed. In

such a case the rights of the partners accrue from the date of the formation of the partnership, and need not be deferred to the date of the written

instrument. R.C. Mitter & Sons v. Commissioner of Income Tax, Calcutta (1959) 2 M.L.J. 192 : 1959. S.C.J. 194. : (1959) 2 An.W.R : : 36 ITR

We accept the finding of the Tribunal that the partnership began to function only from the date of the written instrument in the absence of any

evidence of its formation at any time anterior to it. We are therefore of opinion that the partnership cannot be given retrospective operation as and

from 1st July, 1955.

16. The Revision Petition is allowed and the order of the Subordinate Tribunals is set aside. The Agricultural Income Tax Officer is hereby directed

to restore the application for registration to his file and dispose it of in accordance with law and in the light of the observations herein contained.

There will be no order as to costs in this petition.

