
(1984) 01 AP CK 0004

In the Andhra Pradesh High Court

Case No : Referred Case No. 93 of 1978

Choudry Brothers

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 17-01-1984

Acts Referred:

Income Tax Act, 1922 — Section 32

Income Tax Act, 1961 — Section 183, 184, 2, 2(31), 4

Citation : (1986) 158 ITR 224

Hon'ble Judges : P.A. Choudhary, J;K. Punnayya, J

Bench : Division Bench

Advocate : K.L. Rathi, for the Appellant; M.S.N. Murthy, for the Respondent

Judgement

P.A. Choudary, J.—The following three questions are referred by the Income Tax Appellate Tribunal for obtaining the opinion of this court :

"(1) Whether, on the facts and in the circumstances of the case, the assessment in the status of association of persons is valid ?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal can direct the assessee to file Form No. 11 and comply with conditions u/s 184 and directing the Income Tax Officer to pass orders thereon ?

(3) Whether, on the facts and in the circumstances of the case, the assessee is entitled to benefits of registration ?"

2. In order to be able to answer these questions, a few facts as they appear from the statement of case are stated.

3. The assessee is a partnership firm constituted under a deed of partnership dated July 5, 1962, consisting of four partners of which Sushilchand Choudary was a minor represented by his mother.

4. For the assessment year 1966-67, the assessee filed an application for registration of the firm before the Income Tax Officer. But the Income Tax Officer

rejected the application and refused to register the firm under the Income Tax Act on the ground that the partnership deed dated July 5, 1962, was an invalid instrument. u/s 30 of the Partnership Act, a minor can only be admitted to the benefits of a partnership and cannot be made a partner. The partnership deed on the basis of which registration was sought had one minor by name Sushilchand Choudary as a full partner. The Income Tax Officer, therefore, sought to make an assessment as association of persons. The assessee carried the matter in appeal before the Appellate Assistant Commissioner who confirmed the order of the Income Tax Officer. The assessee made a further appeal to the Income Tax Appellate Tribunal.

5. Before the Income Tax Appellate Tribunal, it was urged that the above mentioned Sushilchand Choudary had on attaining majority elected to continue as a partner and had intimated that fact to the Registrar of Firms on March 25, 1964, and that for the assessment year 1966-67, the assessee had filed on that basis an application in Form No.12 for continuation of registration. However, the Income Tax Officer refused to register the firm in view of his order for the earlier year.

6. The Tribunal considered the question whether in the matter of continuation of registration, a fresh partnership deed is necessary after Sushilchand Choudary attained majority. The Tribunal held that since Sushilchand Choudary became major and had elected to continue to be a partner of the firm constituted by the partnership deed dated July 5, 1962, the partnership was perfectly valid. The Tribunal held that the said Sushilchand Choudary signed the application in Form No. 11 for the assessment year 1965-66 and also Form No. 12 for 1966-67 clearly undertaking that he agreed to be a partner of the firm. The Tribunal opined that this conduct of the said Sushilchand Choudary cured the invalidity attached to the partnership deed. Accordingly, the Tribunal concluded that the invalidity hitherto attached to the partnership deed was removed and that the assessee was entitled to registration u/s 184 of the Income Tax Act. Accordingly, the Tribunal directed the assessee to file an application in Form No. 11 complying with the conditions u/s 184 of the Income Tax Act and also directed the Income Tax Officer to pass orders thereon.

7. Thereupon the above questions Nos. (2) and (3) have been framed and referred to at the instance of the Revenue and question No. (1) at the instance of the assessee.

8. It appears to us that both questions Nos. (2) and (3) should be answered in favour of the Revenue and against the assessee on the basis of the facts appearing in the statement of case. In this case, the partnership was constituted under a partnership deed dated July 5, 1962. The partnership deed is clearly contrary to the provisions of section 30, clause (1), of the Partnership Act inasmuch as it is admitted that the abovementioned Sushilchand Choudary was a minor at the time of constitution of the partnership. The partnership can only be brought into existence in accordance with the provisions of the Indian

Partnership Act. Section 4 of the Indian Partnership Act defines "partnership". "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. Section 30 of the Partnership Act declares that a person who is a minor may not be a full partner of the firm. In the partnership deed dated July 5, 1962, it is admitted that the abovementioned Sushilchand Choudary is a minor. The partnership deed dated July 5, 1962, is, therefore, incapable of constituting a relationship of a partnership among the persons mentioned in that deed. And that deed is void.

9. Now, for the purpose of earning the benefit of tax under the Income Tax Act, a firm has to be registered u/s 184 of the Income Tax Act. or that purpose, an application has to be made to the Income Tax Officer accompanied by the instrument evidencing partnership. If a partnership is legally recognised, the Income Tax Officer cannot decline registration of the firm u/s 184 of the Income Tax Act. On the other hand if the partnership is void, no registration can be granted. Prima facie no registration can be granted in this case. But the learned counsel for the assessee argues that by the time Sushilchand Choudary had come to file Form No. 12, he had become a major and elected to be a partner of the firm.

10. It appears to us that his election to be a partner alone is not sufficient to obtain registration u/s 184 of the Income Tax Act. He made no application to the Income Tax Officer as required by section 184 of the Income Tax Act. According to the requirements of section 184 of the Income Tax Act, he ought to have made an application in Form No. 11 for the grant of registration. Instead, he made an application in Form No. 12 which deals not with the granting of registration but with the renewal of registration. The assessee had not produced the instrument of partnership deed along with his application filed in Form No. 12. All this could possibly have been ignored if there was, in fact, a valid partnership. In fact, there was no instrument evidencing a legal partnership firm except the one constituting an unlawful firm on July 5, 1962. On the basis of such an instrument which is void in law, no registration could be claimed under the Income Tax Act. But the argument of the learned counsel for the assessee is that after Sushilchand Choudary had become major, his election to be a partner of the firm cured the invalidity, if any, attached to the partnership deed dated July 5, 1962. We cannot accept this argument. The deed of partnership dated July 5, 1962, which described Sushilchand Choudary as a minor and admitted him as a minor, is a void document as being hit by section 30 of the Partnership Act. Such a void document cannot be revalidated by the subsequent act of ratification by Sushilchand Choudary. It follows that no registration can be granted on the basis of such a void document.

11. The learned counsel for the assessee relied upon the judgment of the Bombay High Court in Commissioner of Income Tax Vs. R. Dwarkadas and Co., . But there the assessee derived support not from an illegal and void document of a partnership but a fresh document which had been executed on November 7,

1953, after the expiry of the earlier document which was void. The Division Bench in that case held that the assessee was entitled for the grant of registration on the basis of a fresh agreement of partnership which was found to have been executed on November 7, 1953. That case, therefore, has no application to the facts of this case. We accordingly answer questions Nos. (2) and (3) in favour of the Revenue and against the assessee.

12. Then remains the first question referred to this court to be answered. This question is referred to this court at the instance of the assessee.

13. The assessee argues that on the facts and circumstances of the case, the assessee cannot be assessed in the status of association of persons and that the assessment should take place only as an individual person. The argument of the assessee goes directly contrary to our answers which we have already given to questions Nos. (2) and (3). Our answers in favour of the Revenue on questions Nos. (2) and (3) are based on the finding of a fact that no firm was constituted by the partnership deed dated July 5, 1962, nor could any firm be so constituted by that deed. The partnership constituted either by word of mouth or a written document brings into existence a particular relationship between the persons called partners. Such a relationship called partnership cannot be brought into existence contrary to the applicable legal provisions of the Partnership Act. Section 30 of the Partnership Act forbids the constitution of a partnership with a minor as a full member. Admittance of Sushilchand Choudary who was a minor on July 5, 1962, as a full member of partnership renders it legally impossible to constitute an association of four persons into a partnership. The result is that there can be no partnership in the eye of law. The question of such a body of persons being registered as a partnership for the purpose of the Income Tax Act cannot, therefore, arise. The association of persons in this case can neither be treated as a registered partnership nor as an unregistered partnership. It follows that this association of persons cannot be assessed to Income Tax either as a registered firm or as an unregistered firm. Nor can the assessee be assessed on the basis of individual member's income and through the association of persons because a body of individuals constituted an association of persons. A group of persons came together and acted together for doing business and earning profits. They, therefore, constitute an association of persons only. u/s 4 of the Income Tax Act, 1961, the unit for the purpose of assessment in this case can only be an association of persons. Section 4 of the Income Tax Act, 1961, charges the income earned by such an association of persons called "person" within the meaning of the definition clause of section 2(31), with liability to suffer Income Tax. It is no doubt true that an association of persons is a body of persons. But from this, it does not necessarily follow that in the matter of assessing the income earned by an association of persons, the Income Tax Officer has an option either to assess that body of persons called the association of persons or its individual members. u/s 4 of the Income Tax Act, 1961, the Income Tax Officer is left with no choice to assess the association of persons or alternatively the individual persons comprising that association of persons. u/s 4

of the Act, he has to levy tax only on the appropriate unit of Income Tax. It, therefore, becomes necessary to find out which is the appropriate unit of Income Tax in this case. The income was earned in this case not by the individuals but by an association of persons. Willy-nilly the Income Tax Officer had to levy tax on the association of persons which is the only appropriate unit of Income Tax assessment in this case. In fact, the Income Tax Officer in a case of this nature would be acting contrary to law if he assesses as the assessee suggests before us on the facts of individual personal income.

14. But the argument of the assessee before us is that two different Income Tax Officers, one of Hyderabad in the year 1966, and the other of Delhi in 1967, had already assessed two of the members of the association of persons on the basis of share of income from the firm and that thereafter it would not be open to the taxing authority to tax their income as that of the association of persons. In support of this argument, the assessee placed reliance upon the following decisions :

(1966) 60 ITR 95 (SC) , Ch. Atchiaiah Vs. Income Tax Officer, "B" Ward, , Deccan Bharat Khandsari Sugar Factory Vs. Commissioner of Income Tax, , Laxmichand Hirjibhai v. CIT [1981] 128 ITR 747, COMMISSIONER OF Income Tax, MADRAS Vs. R. DHANDAYUTHAM AND OTHERS., Bhola Nath Kesari v. Director of State Lotteries, U.P. [1971] 95 ITR 171 (sic) and Universal Commercial Company Vs. Commissioner of Income Tax, .

15. A close reading of these judgments would show that a large number of them are inapplicable to the facts of the present case and that the argument of the assessee largely suffers from a failure to make a distinction between the scope and meaning of section 3 of the Indian Income Tax Act of 1922 and section 4 of the Income Tax Act of 1961. Section 3 of the Indian Income Tax Act of 1922 declares in part that Income Tax shall be charged in accordance with the rates of the Finance Act in respect of the total income of the previous year of every individual, Hindu undivided family, company and local authority and of every firm and other association of persons or the partners of the firm or the members of the association individually. Thus, u/s 3 of the Indian Income Tax Act, 1922, the units of assessment are : (i) individual, (ii) Hindu undivided family, (iii) company, (iv) local authority, (v) every firm, and (vi) other association of persons or the partners of the firm or the members of the association individually. Now u/s 4 of the Income Tax Act, 1961, this enumeration of units of assessment is covered by the use of the single word "person" which is defined by section 2(31) as including an individual, a Hindu undivided family, a company, a firm, an association of persons, or a body of individuals, whether incorporated or not, a local authority, and every artificial juridical person. The difference between section 3 of the old Act and section 2 of the present Act, with which we are now concerned, consists in the fact that on the total income earned by a firm or other association of persons, the Income Tax authority had under the old Act the choice to assess either that firm or other association of persons or the partners of the firm or the

members of the association individually. Now this choice which section 3 of the old Income Tax Act conferred upon the Income Tax Officer had been completely removed so far as an association of individuals is concerned, although u/s 183 of the present Act, the Income Tax Officer is still left with a discretion to assess the Income Tax in the hands of an unregistered firm or its individual partners. But as we have found above that there was no legal firm in this case, we may not consider any further the question of an unregistered firm or its individual members, being assessed. The question with which we are now concerned is whether the Income Tax Officer has discretion under the new Act to assess the individual members of an association of persons instead of the association of persons. A perusal of section 4 of the 1961 Act would clearly show that the Income Tax Officer under the new Act has been left with no such discretion. The discretion which he was hitherto enjoying u/s 3 of the 1922 Act was withdrawn by the Income Tax Act, 1961. It would, therefore, not be permissible today for the Income Tax Officer under the Income Tax Act, 1961, to assess the income of the association of persons individually in the hands of that association any more than it would have been permissible for the Income Tax Officer to assess the Income Tax of the Hindu undivided family in the hands of its individual members.

16. In *Income Tax Officer, A-ward, Lucknow Vs. Bachulal Kapoor*, , at page 80, the Supreme Court observed :

"That apart, u/s 3 of the Act, in the matter of assessment, there is no question of any election between a Hindu undivided family and a member thereof in respect of the income of the family. If a Hindu undivided family exists, u/s 3 of the Act, the Income Tax Officer has to assess it in respect of its income... While section 3 confers a option on the Income Tax Officer to assess either the association of persons or the members of the association individually, no such option is conferred on him thereunder in the case of a Hindu undivided family."

17. In *Mahendra Kumar Agrawalla Vs. Income Tax Officer and Others*, , a Division Bench of the Patna High Court observed (headnote) :

"Under section 3 of the Indian Income Tax Act, 1922, once the income of the "association of persons " was charged to Income Tax in the hands of the members individually, there could be no fresh assessment of the income in the hand, of the association because that would amount to double taxation of the income. u/s 3 of that Act, the Income Tax Officer had the option to assess either of the two units of assessment and once having exercised the option to assess one unit it would not be open to him to assess the other unit. But u/s 4 of the Income Tax Act, 1961, no such option of election between the two taxable units has been given to the Income Tax Officer."

18. In *RODAMAL LALCHAND Vs. COMMISSIONER OF Income Tax, PATIALA-II*, , a Division Bench of the Punjab and Haryana High Court also took a similar view noting the difference between the scheme of section 3 of the Indian Income Tax Act, 1922, and section 4 of the Income Tax Act, 1961. The headnote reads :

"The description of "person" in section 2(31) of the Income Tax Act, 1961, makes no distinction between a firm or its partners, association of persons or body of individuals, whether incorporated or not, or the members of the association or the body of individuals in their individual capacity. The charging section of the Act, i.e., section 4, views each category of the taxable entities alike as a distinct and different unit. In the case of a firm it would mean a firm or a partner. Similarly, in the case of an association of person or body of individuals, it would mean the association of persons or the body of individuals or the members. The option given by the word "or" to the assessing authority in the charging section 3 of the Indian Income Tax Act, 1922, to proceed against any out of these has now been withdrawn in the 1961 Act. In taxation matters, it is a rule that the charging section guides the machinery sections of the Act.

Therefore, there is no prohibition in section 4 of the 1961 Act restraining the assessing authority from proceeding against the firm which is a taxable entity even though two of its partners had been separately assessed in respect of their share of the income from the partnership business. The position, that once the income of an entity has been assessed and taxed in the hands of other taxable entities mentioned in section 3 of the 1922 Act, no tax could be levied on the first entity, cannot prevail under the 1961 Act."

19. In (1966) 60 ITR 95 (SC) , the Supreme Court held that where the Income Tax Officer had exercised his option, that would be final and binding. Similarly, Commissioner of Income Tax, U.P., Lucknow Vs. Kanpur Coal Syndicate, , is also a case dealing with the option of the Income Tax Officer falling under the old section 3. The judgment of the Gujarat High Court in Laxmichand Hirjibhai v. CIT [1981] 128 ITR 747, and the judgment of the Madras High Court in Universal Commercial Company Vs. Commissioner of Income Tax, would not support the argument of the assessee, because in both the cases the question which was considered was one which fell u/s 183(b) of the Income Tax Act. Under that section, a regulated option has been given to the Income Tax Officer to assess the income of an unregistered firm either in the hands of the individual members or in the hands of the unregistered firm. These cases held that once that option has been exercised, it is final and binding on the Revenue, of course, subject to alteration and variation in the regular procedure of all appeals and revisions. But those cases would not be of any use to us where section 4 had taken away that option. The really important cases which support the argument of the assessee are those in Ch. Atchiaiah Vs. Income Tax Officer, "B" Ward, , COMMISSIONER OF Income Tax, MADRAS Vs. R. DHANDAYUTHAM AND OTHERS., and Commissioner of Income Tax Vs. Pure Nichitpur Colliery Company, . In Ch. Atchiaiah Vs. Income Tax Officer, "B" Ward, , the distinction between section 3 of the Indian Income Tax Act, 1922, and section 4 of the Income Tax Act, 1961, was brought to the notice of the learned judges and it was urged on behalf of the Revenue that under the Income Tax Act, 1961, there was no option left with the Income Tax Officer to assess the tax either on the members of the association as individuals or the association of persons. But the learned judges summarily dismissed this

contention by failing to notice that the last part of section 3 of the old Act contemplates exercise of an option by the Income Tax Officer between the association of persons or the members of the association individually. A bare comparison of the last words of section 3 would make this clear. But u/s 4 of the 1961 Act, no such option has been given to the assessing authority ; but he has to assess the appropriate taxable unit called, the person. Unfortunately, this vital difference between the old section 3 and the new section 4 had been missed by the learned judges. It is true that by using the word "person", section 4 refers to all categories of assessable units. But from this, it cannot be said that the option which section 3 confers on the assessing authority is retained even in section 4. We have already seen that by omitting the words "or the members of the association individually", section 4 has approximated the position of association of persons to that of assessable units like Hindu undivided family. The learned judges merely stated (p. 677) :

"Under section 3 of the old Act, instead of stating that the tax shall be charged on every person, the categories of assesseees were enumerated in the section itself and one of the categories was an association of persons. Under the present Act, instead of enumerating the categories in the body of the section, it is stated that the income will be charged on every person and in the definition of "person" in section 2(31), the various categories of persons are enumerated. In our view, this change in the wording of the section does not affect the legal position."

20. We are unable to agree with this reasoning of the learned Judges which is previously based upon the fact that it had not noticed the significant changes the charging section 3 had undergone by the omission of the words "or the members of the association individually". We, therefore, consider the judgment in Ch. Atchiaiah v. ITO [1979] 116 ITR 615 , as one made per incurium and would not be a binding precedent. The judgment in Deccan Bharat Khandsari Sugar Factory Vs. Commissioner of Income Tax, , dealt with a case where the income of an unregistered firm would be assessed in the hands of the firm after first having assessed provisionally on protective basis in the hands of the individual partners. Section 183, as we have already noted above, grants the assessing authority a regulated discretion to choose to assess either the unregistered firm or its partners depending upon his assessment as which course of action would best promote the interests of the Revenue. Earlier, the option of the Income Tax Officer to assess the individuals was not based on a full view of the facts as to the income of the firm and, therefore, it would be open for the Income Tax Officer to assess the firm u/s 183(b). That case may not be of any direct relevance to the controversy before us. The decision in COMMISSIONER OF Income Tax, MADRAS Vs. R. DHANDAYUTHAM AND OTHERS., , no doubt supports the contention of the assessee. But it has not considered the change that has been brought about by section 4 of the Income Tax Act, 1961, in the matter of exercise of option by the Income Tax Officer. The Madras decision had upheld the claim of the association that an assessment having been made on one of its members on his share of the profits, no assessment of association as such can

be made subsequently, but without considering the question whether the Income Tax Officer would have made such an assessment u/s 4 of the Income Tax Act of 1961. We cannot, therefore, consider that to be a correct view of section 4. The decision in Commissioner of Income Tax Vs. Pure Nichitpur Colliery Company, , no doubt supports the contention of the assessee. But that decision was not followed by a Bench of the Patna High Court in Mahendra Kumar Agrawalla Vs. Income Tax Officer and Others, and was expressly dissented from in RODAMAL LALCHAND Vs. COMMISSIONER OF Income Tax, PATIALA-II., .

21. For the reasons which we have mentioned above, we prefer to follow the decision taken in Mahendra Kumar Agrawalla Vs. Income Tax Officer and Others, , and (not in ?) Commissioner of Income Tax Vs. Pure Nichitpur Colliery Company, .

22. We accordingly answer the first question also in favour of the Revenue and against the assessee. No costs.