
(1982) 07 MAD CK 0006
In the Madras High Court
Case No : Tax Case No. 944 of 1977

Commissioner of Income Tax

APPELLANT

Vs

Dadha and Co

RESPONDENT

Date of Decision : 29-07-1982

Acts Referred:

Income Tax Act, 1961 — Section 2(47), 41(2)
Registration Act, 1908 — Section 17(b)
Stamp Act, 1899 — Section 2(15)

Citation : (1983) 14 TAXMAN 219

Hon'ble Judges : V. Balasubrahmanyam, J;G. Ramanujam, J

Bench : Division Bench

Judgement

G. Ramanujam, J.—The assessee herein is a registered firm carrying on business in Pharmaceuticals, chemicals, drugs and money-lending.

For the assessment year 1971-72, corresponding to the previous year ended 30-10-1970, it filed a return showing an income of Rs. 1,22,180.

While going through the accounts of the assessee, the ITO found that the capital account of the partners showed a credit of one-third share of sale

proceeds of the house property Nos. 161 and 162, Nyniappa Naicken Street, Madras. The said two properties had been purchased on 14-6-

1948 and 1-2-1950 by the firm and the income from these properties were being assessed in the hands of the firm until the assessment year 1964-

65. During the accounting year ended 4-11-1964, entries had been made in the books of the firm removing these properties from the partnership

assets and showing as the individual properties of the partners and for the income from the property there has also been a return filed by the

partners as individuals and that has been accepted by the revenue for some years. On 15-10-1970, these properties were sold to a third party for

Rs. 2,00,000. The said sale deed had been executed by two of the partners of the firm and the legal representative of the deceased partner by name Lalchand Dadha. The purchase price as well as the interest received from the purchaser were credited to the accounts of the two partners and the legal representative of the deceased partner. On these facts, the ITO came to the conclusion that though the sale deed executed by the individuals, it should be treated as a sale on behalf of the firm and if so treated the capital gains arising out of the transaction as well as the income from the property and the interest on unpaid purchase price were all to be assessed in the hands of the firm. He also computed the capital gains to be Rs. 1,80,500 and added the same along with the income of Rs. 9,500 and the interest of Rs. 4,390 to the profit u/s 41(2) of the income tax Act, 1961 ("the Act") and ultimately determined the total income of the year at Rs. 1,97,260. Aggrieved by the said decision of the ITO the assessee went before the AAC who accepted the contention of the assessee that these properties have been taken out of the assets of the firm by the entries in the firm's accounts in the assessment year 1964-65 which has been accepted by the department and, therefore, the assessment of the said sums in the hands of the firm was untenable. He, therefore, deleted the additions made by the ITO.

2. Aggrieved against the order of the AAC, the revenue took the matter in appeal to the Tribunal contending that the properties in question were the immovable property purchased by the firm and, therefore, they could not cease to be that of the firm without instrument in writing and relied on a decision of the Allahabad High Court in Ram Narain and Brothers Vs. Commissioner of Income Tax, The Tribunal, after considering the rival contentions of the parties, held that though the two properties were purchased on 14-6-1948 and 1-2-1950 in the name of the firm, in view of the entries made in the account books on 16-11-1963, transferred (sic) the one-third interest of each of the three partners in the two properties, it should be taken that these transferees (sic) have become their personal properties held in common as co-owners and, therefore, these properties have ceased to be the properties of the firm after the relevant book entries in the firm. The Tribunal also held that after the relevant book entries the income from these properties had been assessed in the hands of the individual partners from the assessment years 1964-65 to 1969-70 and,

therefore, these properties should be taken to have become the separate properties of the partners. Aggrieved against the order of the Tribunal,

the revenue has sought and obtained a reference to this Court on the following three questions of law:

1. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in holding that no registered document is necessary

for converting the immovable property of the firm in favour of the partners and that the mere book entries would be sufficient?

2. Whether the Appellate Tribunal's finding that the assessee-firm was not the owner of the properties Nos. 161-162, Nyniappa Naicken Street,

Madras-3, on the date of transfer is based on valid and relevant materials and is sustainable in law?

3. Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in confirming the deletion of the various additions

made by the income tax Officer consequent on the sale of the properties Nos. 161-162, Nyniappa Naicken Street, Madras-3, by the assessee-

firm?

3. Admittedly, the properties were purchased in the name of the firm and the sale consideration has proceeded from the firm. Ever since the date

of the purchase till the assessment year 1964-65, income from these properties have been regularly assessed in the hands of the firm. It is on 16-

11-1963, during the accounting year ended 4-11-1964, [that] book entries have been made removing these properties from the list of partnership

assets and putting them in the names of the individual partners with respect to their respective shares. The individual partners have been assessed

with respect to their respective shares of the income from these properties since then. There is no other document in writing evidencing the transfer

of an interest in the properties from the firm to the individual partners. According to the revenue, unless there is some document of transfer from the

firm to the individual partners, the properties should be taken to continue as the firm's properties notwithstanding the book entries and by means of

book entries there cannot be a transfer of interest in immovable properties which has to be effected only [through a] document if the value of such

interest exceeds Rs. 100. The learned counsel for the assessee, however,, contends that though the properties have been purchased in the name of

the firm, since the firm is not a legal entity and is merely a compendious name to denote the partners constituting the firm, the firm's properties

should be treated as common properties of the individual partners and, therefore, no document is necessary to transfer the properties held by the

firm to the individual partners, and once the properties are taken to be the common properties of the partners even from the date of purchase, then

it is open to the partners to divide the common properties amongst themselves even though there is no actual dissolution of the firm.

He refers to the decision in *Malabar Fisheries Co. Vs. Commissioner of Income Tax, Kerala*, wherein Tulzapurkar, J., speaking for the Bench had

expressed the view that a partnership firm under the Indian Partnership Act, 1932 is not a distinct legal entity apart from the partners constituting it,

that equally in law the firm as such has no separate rights of its own in the partnership assets and when one talks of the firm's property or the firms

assets, all that is meant is property or assets in which all partners have a joint or common interest, that, it cannot therefore, be said that upon

dissolution, the firm's rights in the partnership assets are extinguished, that it is the partners who own jointly or in common the assets of the

partnership, and that, therefore, the consequence of the distribution, division or allotment of assets to the partners which flows upon dissolution

after the discharge of liabilities is nothing but a mutual adjustment of rights between the partners and there is no question of any extinguishment of

the firm's rights in the partnership assets amounting to a transfer of assets within the meaning of section 2(47) of the Act.

In the said decision, the Supreme Court was of the view that where, in the course of the dissolution of the firm, the firm's properties that remain

after satisfying all the creditors are divided amongst the partners, it will not amount to a transfer of interest from the firm and it is only the

distribution of assets on a dissolution of the firm. In this case there is no question of dissolution. Even when there is no dissolution of the firm the

properties of the firm had been divided as between the partners by way of book entries. Even on the basis, as has been held by the Supreme

Court in the above decision that the properties of the firm should be deemed to have been held in common by all the partners constituting the firm,

as firm itself which has no legal entity cannot hold the properties, there cannot be a division of the properties purchased in the name of the firm

amongst the partners by making entries in the accounts of the firm without actual dissolution of the firm. Even if we take the firm's properties as the properties owned and enjoyed in common by the partners, still such common properties cannot be possessed and enjoyed in severalty unless there is a document in writing. In a case where the properties are owned in common by several persons each of them is entitled to every particle of those properties but when it is divided and enjoyed in severalty there is actually a transfer of interest by mutual release. When common ownership of two is transferred into two individual ownerships, then there is a clear transfer of an interest in that there is mutual release by one in favour of the other as regards the interests transferred in favour of the other. It is, no doubt, true that the release of his share in the partnership business by one partner is not a transfer of an interest in immovable property even though the partnership owned immovable property.

This is for the reason that though a partner is a co-owner of the partnership property, he has no right to ask for a share in that property but only a right to ask for a dissolution and a share in the resulting assets. However, if a partner releases his share in specified properties of the firm, it will be a transfer of an interest in immovable property. Similarly, if the partners divide amongst them, the immovable properties held by the firm, it will be an instrument of partition. This is clear from the definition in section 2(15) of the Indian Stamp Act, 1899, where an instrument of partition is defined as follows:

(15) Instrument of partition. - "Instrument of partition" means any instrument whereby co-owners of any property divide or agree to divide such property in severalty, and includes also a final order for effecting a partition passed by any revenue authority or any civil court and an award by an arbitrator directing a partition.

4. In this case the properties which were originally owned by a firm of three partners have subsequently been divided in severalty by means of book entries and this transaction by which the common enjoyment by all partners of common properties transformed into a separate enjoyment in severalty of each partner clearly falls within the definition. It is well established that instrument of partition of immovable property of the value of Rs. 100 and upwards requires registration. Section 17(b) of the Indian Registration

Act, 1908, provides that any non-testamentary instrument which purport or operate to create, declare assign, limit or extinguish any right, title or interest in the immovable property of the value of Rs. 100 and upwards shall be registered. Even if the transaction by which the common property becomes the separate property [of] each of the partners in severalty it clearly amounts to a release and counter-release of their respective interest in the common property. Even on that basis the transfer should be by a release deed. In this view, the book entries made on 16-11-1963 showing the common properties of the partner as the separate properties of each of the partners to the extent of their share cannot have any effect without there being any instrument evidencing the said transfer of a common interest into a separate and individual interest. If the book entries are not sufficient to constitute a transfer of the common interest in the properties into a separate interest of the partners, the properties will be taken as if the firm's properties and the ultimate sale by the two partners and the legal representative of the other partner should be taken to have been executed only on behalf of the firm. In this view of the matter, the assessment made in this case, -assessing the firm to capital gains and also assessing the income and interest earned on the unpaid consideration, should be sustained as correct. On the contrary the view taken by the Tribunal cannot be legally sustained,

5. The questions referred are, therefore, answered in favour of the revenue. The revenue will have its cost. Counsel fee Rs. 500 (Rupees five hundred only).

V. Balasubrahmanyam, J.

6. I wish to add a few words to the elaborate judgment of my learned brother. In this reference, it is not the assessee's case that the immovable properties in question are the joint properties of a HUF. The owners, even according to the assessee, are only co-owners and not mitakshara coparcenary. If it were the joint properties of a mitakshara coparcenary, for instance, the common properties can be divided and converted into separate interest owned respectively by the dividing members without any writing or other formalities. For Hindu law recognises a partition even of immovables under an oral partition. But the immovable properties in this case were jointly owned by persons who happened to be partners and

who acquired the properties by joint purchase. This being so, the only way the co-owners have of putting an end to commonality of ownership and of creating separate dimensions over as many separate interests as there are co-owners, would be by way of a regular deed of partition. Without a deed of partition or at any rate deed of mutual release, co-ownership of property cannot fall apart as separate individual interests. If there is need for an instrument, then such an instrument, whether it is by way of regular partition deed or a release deed, must be duly stamped. The Indian Stamp Act defines an instrument of partition as "any instrument whereby co-owners of any property divide or agree to divide such property in severalty". What is more, if the partitioned property is of the value of Rs. 100 and upwards, the instrument must be registered under the Indian Registration Act. There can be no doubt that excepting partition deed made by a revenue authority which is specifically exempt from a registration, other partition deeds involving immovable property of the value of Rs. 100 and upwards are compulsorily registerable.

7. In the face of this position in law relating to partition of immovable property as between co-owners, there can be no partition in this case. What the co-owners did in this case was merely to debit the asset account relating to the immovable properties in the books of the partnership firm and credit the co-owners, that is to say, a partner, in equal shares of the said value. It is claimed that these book entries have completely, effectively and legally brought a partition of the immovable properties in question. This cannot be accepted. In the first place, the book entries do not make a conversion of any kind known to law. They are only entries made by the book keeper. They are rightly called book entries, and those entries find place in the account books. They cannot by their own force effect any conveyance, release, partition or other transfer of immovable properties. What is more, the entries do not even evidence a partition. All the entries taken together only show two distinct positions, the original position under which the properties were under co-ownership and the subsequent position under which it is shown that separate values of the properties or figure as against the co-owners. A combined reading of these two entries will only give release of [show] what was the position devoutly wished for the parties, which has not been properly brought about by any effective transaction known to law. The law requires a degree of formality in

regard to transfers of immovable property. A partition may not technically be a full-fledged transfer of ownership, because those who receive their shares under the partition may be rightly regarded as co-owners and the partition in any case does not confer a new title on them. Still there is a transformation or metamorphosis of the co-owners' title and possession involved in the partition. This would include the mutual release of the respective interest of the co-owners. This is why partition has always been regarded as involving some degree of alteration in the title and possession of the immovable property. Partition, apart from what the Hindu law permits, is always a synellegromatic (sic) transaction and it cannot fructify by mere book entries. For these reasons as well as grounds on which my learned brother has decided the question of law, I would respectfully agree with this conclusion. I would agree with the direction as to costs also.