

(1986) 07 MP CK 0012

In the Madhya Pradesh High Court

Case No : Miscellaneous Civil Case No. 326 of 1984 & Miscellaneous Civil Case No. 344 of 1984

Commissioner of Income Tax

APPELLANT

Vs

Smt. Nirmala Devi

RESPONDENT

Date of Decision : 16-07-1986

Acts Referred:

Income Tax Act, 1961 — Section 64(1)

Citation : (1987) 60 CTR 38 : (1987) 166 ITR 253 : (1987) 32 TAXMAN 245

Hon'ble Judges : G.G. Sohani, J;B.B.L. Shrivastava, J

Bench : Division Bench

Advocate : R.C. Mukati, for the Appellant; Chaphekar, for the Respondent

Judgement

G.G. Sohani, J.—The order in this case will also govern the disposal of MCC No. 326 of 1984 (Commissioner of Income Tax Vs. Smt. Nirmala Devi,).

2. By these references u/s 256(1) of the Income Tax Act, 1961 (hereinafter referred to as "the Act"), the Income Tax Appellate Tribunal, Indore Bench, has referred the following question of law to this court for its opinion:

"Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that interest earned by a minor on his capital investment in the firm to the benefits of which he has been admitted, could not be clubbed along with the share income and taxed in the hands of the parent u/s 64(1)(iii) of the Income Tax Act, 1961 ?"

3. The facts giving rise to these cases, as set out in the statement of the case, briefly, are as follows :

4. The assessee is a partner in a firm known as M/s Nirmal Paper Mart, Ratlam. Her minor children are admitted to the benefits of the partnership in a number of firms. Certain funds were invested in these firms on behalf of the minors as their capital and the firms paid interest to the minors on the capital so invested. The assessee's contention before the Income Tax Officer was that so far as the

amount of interest on the capital invested in the aforesaid firms by the minors was concerned, that could not be taxed in the hands of the assessee under the provisions of Section 64(1)(iii) of the Act. This contention was not upheld by the Income Tax Officer, while framing the assessment for the years 1976-77, 1977-78, 1978-79 and 1979-80. On appeal, the Appellate Assistant Commissioner upheld the finding of the Income Tax Officer in this behalf. On further appeal before the Tribunal, the Tribunal held that if there was independent investment of capital by the minor, which had not come to him from the assessee directly or indirectly, Section 64(1)(iii) of the Act would not render it liable to be taxed in the hands of the assessee. The Tribunal, therefore, remanded the matter to the Income Tax Officer to ascertain if there was independent investment by the minors, which had not come to them from the assessee directly or indirectly. The Tribunal further directed that if it was found that the amount of capital invested by the minors had not been provided by the assessee, the interest paid thereon by the firms should not be clubbed with the income of the assessee. Aggrieved by that order, the Revenue sought a reference and it is at the instance of the Revenue that the aforesaid question of law has been referred to this court for its opinion. The reference made in respect of the assessment years 1976-77, 1978-79 and 1979-80 has been registered as Miscellaneous Civil Case No. 326 of 1984 (Commissioner of Income Tax Vs. Smt. Nirmala Devi,), while the reference in respect of the assessment year 1977-78 has been registered as Miscellaneous Civil Case No. 344 of 1984.

5. Learned counsel for the Revenue contended that the Tribunal erred in holding that the question of source of investment of capital by a minor was not relevant in determining the question as to whether the amount of interest could be taxed in the hands of the assessee. In reply, it was contended on behalf of the assessee that the source of investment was the decisive factor for determining whether the income in question was or was not includible in the total income of the assessee.

6. Before we proceed to appreciate the contentions advanced on behalf of the parties, we find that the question referred to this court by the Tribunal does not bring out the real issue between the parties. The Tribunal was of the opinion that if the capital invested in the firms by the minors had not come to the minors from the assessee directly or indirectly, then interest on such capital could not be taxed in the hands of the assessee by virtue of the provisions of Section 64(1)(iii) of the Act. It was for ascertaining this fact that the Tribunal had remanded the case to the Income Tax Officer. The real issue between the parties, therefore, is whether the source of the capital invested in the firms by the minors is decisive of the question as to whether interest on such capital can be taxed in the hands of the assessee by virtue of the provisions of Section 64(1)(iii) of the Act. To bring out this real issue between the parties, we, therefore, reframe the question as follows :

"Whether, on the facts and in the circumstances of the case, the Tribunal was

justified in holding that if there was independent investment of capital by the minor, which had not come to him from the assessee directly or indirectly, interest on such capital would not be liable to be taxed in the hands of the assessee by virtue of the provisions of Section 64(1)(iii) of the Act and whether the Tribunal was justified in remanding the case to the Income Tax Officer for ascertaining the source of capital invested by the minors in the partnership firms ?"

7. Now, the answer to the aforesaid question turns on Clause (iii) of Sub-section (1) of Section 64 of the Act, which reads as under :

"64. Income of individual to include income of spouse, minor child, etc.-

(1) In computing the total income of any individual, there shall be included all such income as arises directly or indirectly--...

(iii) to a minor child of such individual from the admission of the minor to the benefits of partnership in a firm."

8. The aforesaid provision is clear enough. It says that in computing the total income of an individual, the income of a minor arising directly or indirectly "from the admission of the minor to the benefits of partnership in a firm" shall be included in the total income of the assessee for the purpose of assessment. If the income arising to the minor child has direct or indirect connection with the fact of its admission to the benefits of the partnership, then the minor's income has to be included in the total income of the individual. That is the mandate of Clause (iii) of Sub-section (1) of Section 64 of the Act. Therefore, what is material for the purpose of applicability of the provisions of Section 64(1)(iii) of the Act is the nexus between the income derived by a minor child from a partnership firm and the admission of such minor child to the benefits of that partnership firm. In this connection, we may usefully refer to the following observations of a Division Bench of this court in COMMISSIONER OF Income Tax, M. P. Vs. BADRILAL BHOLARAM., :

"For the inclusion of the minor child's income in the total income of an individual u/s 16(3)(a)(ii), there must be a direct or indirect connection between the minor's admission to the benefits of partnership and the receipt of the income. It follows, therefore, that if the minor child gets interest on any capital contributed by him to the firm, then the interest earned by him on the capital amount is an income which he derives from his association to the benefits of the partnership. It is because of his admission to the benefits of the partnership that he can contribute to or maintain any capital in the firm. If, on the other hand, the minor makes a deposit with the firm or advances a loan to the partnership firm, then the interest paid to him on the loan or deposit amount has no connection whatsoever with the fact of his admission to the benefits of the partnership. The minor child could have made the deposit or advanced the loan and earned interest thereon even if he had not been admitted to the benefits of the partnership firm."

9. We respectfully agree with the aforesaid observations.

10. Learned counsel for the assessee contended that under the terms of partnership, the minor admitted to the benefits of the partnership was not under any obligation to contribute any capital. But as observed in COMMISSIONER OF Income Tax, M. P. Vs. BADRILAL BHOLARAM., , the amount contributed by a partner as capital does not become an advance merely because under the partnership deed, there is no compulsion on the partner to contribute any capital. It was also contended by learned counsel for the assessee that there was no material on record for finding as to whether the amount invested by the minor was towards the capital of the firm or whether it was a loan or any advance by the minor to the firm. But from the statement of the case drawn by the Tribunal, it does not appear that the assessee had at any time raised the contention before the Tribunal that the amount invested by the minor was a loan or advance to the firm and was not the contribution of the minor to the capital of the firm. In this behalf, what the Tribunal has stated in the statement of the case is as follows:

"Certain funds were invested in the firms on behalf of the minors as their capital and the firms allowed interest to the minors on the said capital."

11. It is, therefore, clear that what was urged before the Tribunal on behalf of the assessee was that for the applicability of the provisions of Section 64(1)(iii) of the Act, what was material was a finding on the question as to whether the amount invested by the minor had or had not come from the assessee directly or indirectly and that if there was independent investment of capital by the minor, interest earned thereon could not be taxed in the hands of the assessee. This contention was upheld by the Tribunal. In our opinion, however, in upholding the aforesaid contention of the assessee, the Tribunal did not take into account the import of the language used in Section 64(1)(iii) of the Act. That language is clear and whatever might have been the object of introducing that clause, the clause does not leave any room for doubt that it has been made obligatory that if the income arising to a minor child from a partnership firm is referable to the fact of admission of that child to the benefits of the said partnership firm, then such income is includible in the total income of the assessee. The question of source of investment in the firm by the minor is not relevant or decisive for making the income of the minor includible in the total income of the assessee. In the instant case, what is invested in the firms on behalf of the minors is capital and not a loan or advance to the firm. Under these circumstances, the Tribunal, in our opinion, was not justified in holding that if there was independent investment of capital by the minor, which had not come to him from the assessee directly or indirectly, interest on such capital would not be liable to be taxed in the hands of the assessee, by virtue of the provisions of Section 64(1)(iii) of the Act. The Tribunal was, therefore, not justified in remanding the case to the Income Tax Officer for ascertaining the source of investment.

12. For all these reasons, our answer to the question reframed by us is, therefore, in the negative and against the assessee. In the circumstances of the

case, parties shall bear their own costs of these references.