
(1979) 09 AP CK 0001

In the Andhra Pradesh High Court

Case No : Case Referred No. 220 of 1976

Sree Balajee Rice Working Co.

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 21-09-1979

Acts Referred:

Income Tax Act, 1961 — Section 185(1)(b), 256(2)

Citation : (1980) 3 TAXMAN 160

Hon'ble Judges : Alladi Kuppaswami, J

Bench : Single Bench

Advocate : D.V. Sastri, for the Appellant; P. Rama Rao, for the Respondent

Judgement

Alladi Kuppaswami, J.—The assessee is a firm consisting of eight partners and was constituted under an instrument of partnership dated December 11, 1967. An application for registration was filed on March 8, 1968, before the ITO who, after examining the partners and considering all the circumstances of the case, came to the conclusion that except two partners, Thunuguntla Veera Raghavaiah and Vissamsetti Lakshmikantha Rao, the other partners were not real partners and, therefore, the partnership was not genuine. On appeal, the AAC also came to the conclusion, on a careful appraisal of all the facts and circumstances of the case, that as the firm, as constituted by the instrument of partnership, dated December 11, 1967, did not really exist, it was not entitled to registration under the Act. On further appeal, the income tax Appellate Tribunal also considered the evidence and other circumstances of the case and held that the Revenue authorities were right in refusing registration. An application for reference to the court before the Tribunal having been rejected, the assessee applied to this court u/s 256(2) of the income tax Act and this court directed the Tribunal to refer the following questions: (1) Whether, in the circumstances of the case, the Tribunal is right in holding that the partnership is not genuine as six out of the eight partners are name-lenders?

(2) Whether, on the facts and in the circumstances of the case, there is any

material for the Tribunal to come to the conclusion that the partnership is not genuine and the deed of partnership is a sham document and is the firm entitled to registration u/s 185(1)(b) of the income tax Act, 1961?

(3) Whether, on the facts and in the circumstances of the case, the Tribunal is justified in concluding that the firm is not genuine and the instrument of partnership is a sham document on the ground that the partners have not withdrawn the amounts standing to their credit in the books of account by way of profits?

In the leading decision in *Sundar Singh Majithia Vs. Commissioner of Income Tax*, it was observed (p. 461): When a document purporting to be an instrument of partnership is tendered u/s 26A (under the Act of 1922) on behalf of a firm and application is made for registration of the firm as constituted under such instrument, a question may arise whether the instrument is intended by the parties to have real effect as governing their rights and liabilities inter se in relation to the business or whether it has been executed by way of pretence in order to escape liability for tax and without intention that its provisions should in truth have effect as defining the rights of the parties as between themselves.

2. The Tribunal, therefore, considered the question whether the partnership, constituted under the instrument of partnership, was genuine in the sense that it was intended to have real effect as governing the rights and liabilities, inter se, in relation to the business of the firm. The Tribunal observed that no doubt all the partners signed the partnership deed and also the application for registration before the ITO and in the intimations to various officers and banks mentioning that all the partners referred to in the partnership deed were partners. It, however, observed that a mere signing of the document will not amount to the recitals in the documents being true and it was open to the Revenue authorities to consider the question whether the partnership was genuine. In this context, the partners were examined. The Tribunal considered the depositions of all the partners and after a detailed examination of their evidence held that six of the partners were not real partners and did not have the intention of becoming partners and the so-called partnership deed was nothing but a sham document. In this connection they relied upon a number of circumstances and facts admitted by the partners. One of them, Puvvada Venkata Punnayya, stated that the partnership deed was written in English, whereas it was written in Telugu. He pleaded complete ignorance regarding sales, profit and income of the business. Another partner, Puvvada Seetharamaiah, stated that he did not withdraw any amount from the firm even though the firm was dissolved in December, 1969. He stated that the firm earned a profit of Rs. 9,000 though the assessee made a profit of Rs. 89,465. It is unnecessary to repeat what all the Tribunal had said with reference to the evidence of the various partners. It is sufficient to say that considering a number of circumstances, the Tribunal held that the partnership was not genuine and the partnership deed was a sham document which was not intended to be acted upon. It cannot, therefore, be said that the Tribunal's

finding that the partnership was not genuine is based on no material. It is also not correct to state that the Tribunal found that the partnership was not genuine merely because the partners had not withdrawn the amount standing to their credit in the books of account by way of profit. The Tribunal considered several other facts and circumstances in coming to this conclusion.

3. The learned counsel for the assessee submitted that the ITO was bound to register the partnership and he cannot refuse registration on the ground that one of the partners is a benamidar of another. In support of this contention reliance was placed upon the decision of the Supreme Court in CIT v. A. Abdul Rahim & Co. [1963] 55 ITR 651. In that case, it was held that a partner's benami character did not affect the benamidar's capacity as partner or his relationship with the other members of the partnership. If a partner is 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. A benamidar is a mere trustee of the real owner and he had no beneficial interest in the property or the business of the real owner. But, in law, just as in the case of a trustee, he can also enter into a partnership with others. This decision is of no assistance to the assessee, as in this case we are not concerned with a benamidar-partner but with a case where the partnership is not genuine and the partnership deed represents a sham transaction not intended to be acted upon. The distinction between a benami transaction and a sham transaction, not intended to be acted upon, is well settled. Reference in this connection may be made to the decision of the Supreme Court in SREE MEENAKSHI MILLS LIMITED Vs. COMMISSIONER OF Income Tax, MADRAS., In the very decision relied on by the assessee, namely, CIT v. A. Abdul Rahim & Co. [1963] 55 ITR 651, it was observed that when a firm makes an application for registration, the ITO can reject the same if he comes to the conclusion that the partnership is not genuine or the instrument of the partnership does not specify correctly the individual shares of the partners. But once he comes to the conclusion that the partnership is genuine and a valid one, he cannot refuse registration on the ground that one of the partners is a benamidar of another. It is, therefore, clear that it is the right and duty, of the ITO to refuse registration if the partnership is not genuine and the deed of partnership is a sham and nominal transaction.

4. In Madhusudana and Co. Vs. Commissioner of Income Tax, , a Division Bench of this court to which one of us (hon"ble the Chief Justice) was a party, it was held that whether a firm is genuine or not is a question of fact though the question whether there was any material for the Tribunal to find that the partnership was or was not genuine, is a question of law. In that case, it was held that there was material for the Tribunal to hold that there was no genuine firm in existence. It was observed that the Tribunal's order need not be examined, sentence by sentence, minutely. It is the totality of the material and evidence on record, but not each factor separately, that should be taken into consideration. In other words, it is the cumulative effect of all the facts relevant, germane and material for the issue, that really forms the basis for the finding of

fact, and not each factor taken independently that must be taken into consideration. Reference was also made to the decision of this court in *HIRANAND RAMSUKH Vs. COMMISSIONER OF Income Tax, HYDERABAD.*, , where it was held that the partnership was not entitled for registration as two partners constituting the alleged firm were not genuine but were mere dummies shown as partners with a view to reduce the incidence of tax. It was observed that this decision was approved by the Supreme Court even though it was also noticed that the Supreme Court did not approve some of the observations which were not relevant to the issue before them. We are, therefore, satisfied that the finding of the Tribunal that the partnership in question was not genuine and that the partnership deed was a sham transaction is based upon sufficient material. In the result, we answer the question as follows:

- (1) In the circumstances of the case, the Tribunal was right in holding that the partnership was not genuine as six out of eight partners were name- lenders.
 - (2) On the facts and in the circumstances of the case, there is material for the Tribunal to come to the conclusion that the partnership is not genuine and that the deed of partnership is a sham document and the firm was not entitled to registration u/s 185(1)(b) of the income tax Act, 1961.
 - (3) On the facts and in the circumstances of the case, the Tribunal is justified in concluding that the firm is not genuine and the instrument of partnership is a sham document on the ground that the partners have not withdrawn the amounts standing to their credit in the books of account by way of profits.
5. The assessee will pay the costs of this reference. Advocate's fee Rs. 300.