

M/S. Y. L. Agarwalla and Others

Vs

Commissioner of Income Tax, Central Calcutta

Civil Appeal No. 1112(Nt) of 1976

(P. N. Bhagwati, V. D. Tulzapurkar JJ)

27.07.1978

JUDGMENT

TULZAPURKAR, J. -

1. This appeal by the special leave raises an important question as to whether the sum of Rs. 3,08,187, being the share income of three minor sons from the firm of M/s. Grand Smithy Works for the period from December 19, 1967, to August 31, 1968, is liable to be assessed as the income of the Hindu undivided family - M/s. Y. L. Agarwalla & Co., for the assessment year 1969-70 ?
2. The facts giving rise to the question may briefly be stated as follows; One Yudhisthir Lal Agarwalla, since deceased, was the Karta of a Hindu Undivided Family, known as M/s. Y. L. Agarwalla & Co. (the Assessee herein). During his lifetime, in his capacity as the karta to the said Hindu Undivided Family, he carried on business in partnership with three others (Shiv Charan Laul, Ram Gopal Garodia and Tula ram Budhia) in the name and style of M/s. Grand Smithy Works. His share in that firm was 36% Under clause 13 of the partnership deed dated September 20, 1961, pursuant to which the said firm used to carry on its business, it was provided that "the death or retirement of any of the partners shall not have the effect of the dissolving this co-partnership; in such an eventuality the co-partnership business may be carried on between the surviving partner and the heirs/legal representatives of the deceased and or retiring partner or if mutually agreed upon between the surviving partners and heirs, etc, of the deceased or retiring partner with outsiders also". Yudhisthir Lal died on December 18, 1967, leaving behind him his widow, Smt. Bhagwati Devi, six daughters (three married and three unmarried out of whom two were minors) and three minor sons. By two letters both dated January 11, 1968, one addressed by the widow on behalf of herself and the Hindu Undivided Family and the other by the four major daughters, Smt. Bhagwati Devi and the four major daughters declined to exercise the option reserved to them under clause 13 of the deed and refused to join the partnership business; however, the three minor sons were admitted to the benefits of the partnership. Since Yudhisthir Lal died on December 18, 1967, i.e. before the expiry of the year of account of the firm which was from September 1, 1967, to August 31, 1968, the firm closed its accounts on December 18, 1967, and the surviving partners after admitting the three minor sons to the benefits thereof continued to carry on the business of the partnership with effect from December 19, 1967, and a new deed of the partnership was executed by the surviving partners on January 11, 1968, the terms and conditions whereof were made effective from December 19, 1967. Under this new deed each one of the three minor sons of Yudhisthir Lal was given 14% share in the profits of the firm, as also a right to become a full-fledged partner on his attaining majority. Clause 6 of the deed ensured to the firm the continued use of the capital of the Hindu undivided family standing in the account of the Yudhisthir Lal free of interest.

3. For the assessment year 1969-70 (the relevant accounting period being September 1, 1967 to August 31, 1968), Smt. Bhagwati Devi Agarwalla filed the return on behalf of the Hindu undivided family disclosing the share income from the firm of Grand Smithy Works for the period from September 1, 1967, to December 18, 1967, only i.e. up to the date when her husband was alive and was a partner in that firm. It was claimed that with effect from December 19, 1967, the Hindu undivided family of which her husband was the karta and after whose death she was managing the affairs had no interest in the said firm and that her three minor sons were admitted to the benefits of partnership in their individual and personal capacity as agreed to between the three surviving partners of that firm and, therefore, the share income of the firm received by her three minor sons for the period December, 19, 1967, to August 31, 1968, amounting to Rs. 3,08,187, could not be included in the income of the Hindu undivided family and assessed as such. The Income Tax Officer negated that contention; he noticed that in spite of the two letters of disclaimer addressed to the surviving partners, the three minor sons of late Yudhisthir Lal Agarwalla had been admitted to the benefits of the partnership with collective shares of 42% which was more than what their father was holding at the time of his death and further that the Hindu Undivided Family had not charged any interest on its capital amount which was permitted to lie with the firm for which no explanation had been offered by the assessee. He, therefore, took the view that the family of late Yudhisthir Lal continued to have interest in the business of the firm and that the share of profit allocated to the three minor sons really belonged to the Hindu Undivided Family and was accordingly assessable in its hands.

4. On appeal, the Appellate Assistant Commissioner, by his order dated March 24, 1971, confirmed the view of the Income-tax Officer. The assessee carried the matter in further appeal to the Appellate Tribunal but the Tribunal also dismissed the appeal. On a reference, the High Court following the principles and guidelines enunciated by this court in the case of Raj Kumar Singh Hukumchandji v. C. I. T. ((1970) 2 SCC 436 : (1971) 1 SCR 748 : 78 ITR 33), in substance, held that the shares that had been allocated to the three minor sons in the profits of the firm were assessable in the hands of the assessee, Hindu undivided family. The assessee has come up in appeal to this Court by special leave.

5. In support of the appeal, counsel for the assessee raised two or three contentions. In first place, he urged that when a minor was admitted to the benefits of a partnership his share of profits of the firm could be his individual income unless it was shown by the department that in the firm he was really a benamidar or nominee of the Hindu Undivided Family of which he was a member and in that behalf relying upon three undisputed circumstances it was urged that the department had failed to discharge that burden. In the first place, it was pointed out that the Department had never doubted the genuineness or bona fides of the transaction of the admission of the three minor sons of Yudhisthir Lal to the benefits of the partnership of M/s. Grand Smithy Works with effect from December 19, 1967, under the law deed of partnership dated January 11, 1968, it was further pointed out that the said three minors did not and could not in law represent the Hindu undivided family in the firm and thirdly, it was pointed out that the minors had been admitted to the benefits of the partnership after Smt. Bhagwati Devi on behalf of the Hindu undivided family the four major daughters had by their letters to disclaimer dated January 11, 1968, refused to have any connection with the partnership business. In spite of these three circumstances, the tribunal had, counsel contended, wrongly held that the minors were either the benamidars or nominees of the Hindu Undivided Family and that, therefore, the share income allocated to them was of the Hindu Undivided Family. It was further contended that there was no finding recorded by the Tribunal, that there was any agreement between the surviving partners and anyone on behalf of the heirs of the deceased, Yudhisthir Lal, to the effect that the Hindu Undivided Family was to continue to be the

real owner of the shares given to the minors nor was there any evidence to that effect and since the burden of proving any discharge, the Tribunal as well as the High Court had wrongly come to the conclusion that the shares allocated to the three minors constituted the income of the Hindu undivided family and was assessable as such in the hands of the Hindu Undivided Family.

According to him the decisions in the subject of remunerations, commission, fees or salaries, earned by a karta and others members of a Hindu undivided family such as, for instance, Dhanwatey's case (V. D. Dhanwatey v. C. I. T., (1968) 2 SCR 62 : AIR 1968 SC 683 : 68 ITR 365) and Raj Kumar's case could have no relevance to the case of a minor admitted to the benefits of partnership. He, therefore, urged that since the three minor sons could not in law represent the Hindu Undivided Family in the firm and in the absence of any finding that there was any agreement between the surviving partners and any one on behalf of the heirs of Yudhisthir Lal to the effect that the Hindu undivided family was to continue to be the real owner of the shares given to the minors, neither the tribunal nor the High Court could come to the conclusion that the share income allocated to the three minors amounting in aggregate to Rs. 3,08,187 for the period from December 19, 1967, to August 31, 1968, was liable to be assessed as the income of the Hindu Undivided Family.

6. On the other hand, on behalf of the Revenue it was urged by the learned Attorney General that where a minor had been admitted to the benefits of the partnership it was not necessary to show that he was either the benamidar or nominee of the Hindu undivided family in the partnership firm for the purposes assessing his share of profits in the partnership firm as income of the Hindu undivided family but the real test was whether such share income was earned with the aid and assistance of the Hindu Undivided Family funds and the Hindu Undivided Family had suffered any detriment in the process of realisation of such income; in fact, he urged that the question had to be viewed from the broader principle, namely, whether the share income received by the minor coparcener was by of return made to the family because of the investment of family funds of the business and if that was so it would be the income of the Hindu Undivided Family. In this behalf reliance was placed by the learned Attorney-General upon the principles enunciated by this court in its two decisions, namely, Dhanwatey's case and Raj Kumar's case (supra). He pointed out that since in the instant case, the three minor sons of Yudhisthir Lal had been admitted to the benefits of the partnership there was no question of any remunerations, commission, fees or salary being paid to any of them for rendering any services to the firm, and, therefore, having regard to Clause 6 of the new deed of partnership dated January 11, 1968, the direct nexus between the share income allocated to the minors and the utilisation of the capital amount belonging to the Hindu Undivided Family was established and, what was more such capital amount of the Hindu undivided family was permitted to be retained and utilised by the firm to the detriment of the Hindu Undivided Family since such retention or user of the said capital amount was free of interest and, therefore, the share income allocated to the three minor sons had been rightly assessed as income of the assessee. Alternatively, he urged that, though no formal finding had been recorded by the Tribunal, the facts and circumstances obtaining in the case furnished clear material leading to the only inference that the admission of the three minors to the benefits of the partnership on the terms contained in the new deed was not without the assent and agreement of the widow who was a natural guardian of the three minors though she had not formally executed the deed. Therefore, no fault could be found with the ultimate conclusion drawn by the Tribunal and the High Court.

7. Having regard to the rival contentions urged by the counsel on either side, which we have summarised above, it will be clear that the question which really falls for out determination in this case is whether the share of profits or income allocated and received from the partnership firm for the period from December 19, 1967, to August 31, 1968, by the three minor sons who were admitted to the benefits of the partnership is really the individual income of the minors or that of the

Hindu Undivided Family ?

8. Dealing with the factual aspect of the question we shall first indicate the broad and undisputed facts that emerge clearly on the record. Admittedly, deceased, Yudhisthir Lal represented the Hindu Undivided Family as its Karta in the firm of M/s. Grand Smithy Works right up to the time of his death and his share of 36% in the profits of the firm was always assessed as the income of the Hindu Undivided Family. It is not disputed that on his death on December 18, 1967, the family continued to be joint, and as per Clause 13 of the partnership deed dated September 20, 1961, the heirs of Yudhisthir Lal were given the option of joining the partnership firm but by two letters both dated January 11, 1968, the widow and the four major daughters declined the offer; instead, the three minor sons were admitted to the benefits of the partnership each one getting 14% share in the profits and a new deed of partnership dated January 11, 1968, was executed by the surviving partners having retrospective effect as from December 19, 1967. Since strong reliance was placed by counsel for the appellant on these two letters of disclaimer it would be desirable to note what exactly was disclaimed under these two letters. The four major daughters categorically stated that "we do not intend to exercise our option to become partners and decline to be partners with you in M/s. Grand Smithy Works". The widow stated : "Now I am a widow with minor sons and minor daughters. I already understand that the amount of capital lying to the credit of the H.U.F. in the firm exceeds the liability of the H.U.F. In the circumstances I am not willing to join the partnership business on my behalf and on the behalf of the H.U.F." It will thus be clear that by these two letters all that the widow and the daughters did was that they declined to become partners in the firm presumably because none wanted to take the risk of being held liable for the losses the firm might incur, but it would be significant to note that the none of the heirs disclaimed or relinquished his or her right to claim the share, right, title and interest of the deceased, Yudhisthir Lal in the partnership firm and its assets. In fact no demand for the return of the capital amount lying to the credit of Yudhisthir Lal's account, which admittedly stood at Rs. 10,00,000, was made by any of the heirs from the date of Yudhisthir Lal's death till the date of the new deed; on the other hand Clause 6 of the new deed runs thus :

6. That the capital of the partnership shall be the amount as will be found to the credit of the parties hereto of the First (Shiv Charan Laul), Second (Ram Gopal Garodia), Third, (Tola Ram Budhia), parts and the said Yudhisthir Lal Agarwall since deceased.

What is more, there is no provision for payment of interest on the respective amounts of capital lying to the credit of the three surviving partners and the deceased, Yudhisthir Lal. In our view Clause 6 is a tell-tale clauses which carries its own tale that this new partnership agreement containing such a term could not have come about without the assent and agreement on the part of the widow on behalf of the Hindu Undivided Family. Further, the factual interest-free retention and utilization of the said capital amount of the Hindu Undivided Family by the firm for the entire relevant period, i.e. from December 19, 1967, to August 31, 1968 - presumably pursuant to the said clause - clinches the said inference. It is true that the widow is not a signatory to the new deed of partnership; it is also true that the three minors sons could not in law be regarded as the nominees or benamidars of the Hindu Undivided Family in the firm, but the facts and circumstances discussed above, especially the incorporation of a term like Clause 6 in the new deed and the factual interest-free retention and utilization of the Hindu Undivided Family funds for the relevant period by the firm, clearly lead to the inference that the new partnership under the deed dated January 11, 1968, was brought about with the facit assent and agreement on the part of the widow representing the Hindu undivided family and that the quid pro quo for admitting the three minor sons of Yudhisthir Lal to the benefits of the partnership was the continued free of interest use of the capital amount

lying in Yudhisthir Lal's account for the firm which ensured to it by Clause 6. In these circumstances there was direct and substantial nexus between the share income earned by and allocated to the three minor sons and the family funds that remained with and were utilized by the firm and hence the share income would not be their individual income but the income of the Hindu Undivided Family.

9. Turning to the legal aspect of the question it is unnecessary to refer to the several decisions cited at the bar but a reference to only one decision of this court in Raj Kumar's case (supra) will suffice. It is true that the question that arose for determination before this court in that case was whether the managing director's remunerations received from the company by the Karta of a Hindu Undivided Family was assessable to tax as his individual income or as the income of Hindu Undivided Family. But this Court, after discussing the entire previous case law on the subject, laid down certain tests and guide lines which would cover the question raised in this appeal before us. From the earlier decisions this court culled out some tests which were described as subsidiary tests or subsidiary principles and then indicated a broader test or principle which would be of general application. At pages 43-44 of the report (SCC p. 444), this court has observed thus :

The others tests enumerated are -

- (1) whether the income received by a coparcener of a Hindu Undivided Family as remuneration had any real connection with the investment of the joint family funds;
- (2) whether the income received was directly related to any utilization of family assets;
- (3) whether the family had suffered any detriment in the process of realization of the income; and
- (4) whether the income was received with the aid and assistance of the family funds.

In our opinion from these subsidiary principles, the broader principle that emerges is whether the remuneration received by the coparcener in substance though not in form was but one of the modes of return made to the family because of the investment of the family funds in the business or whether it was a compensation made for the services rendered by the individual coparcener. If it is the former, it is an income of the Hindu Undivided Family but if it is the latter then it is the income of the individual coparcener. If the income was essentially earned as a result of the funds invested the fact that a coparcener has rendered some service would not change the character of the receipt. But if on the other hand it is essentially a remuneration for the services rendered by a coparcener the circumstance that his services were availed of because of the reason that he was a member of the family which had invested funds in that business or that he had obtained the qualification shares from out of the family funds would not make the receipt, the income of the Hindu Undivided Family.

10. In the instant case the question raised before us gets easily answered by applying the subsidiary principles indicated at Nos. 2, 3, and 4 above as well as by applying the broader principle indicated above. There can be no doubt the relevant period was earned with the aid and assistance of Hindu Undivided Family Funds and was directly related to the utilization of such funds by the firm and further that the Hindu Undivided Family had suffered detriment in the process of realisation of such income inasmuch as the capital amount lying to the credit of the deceased, Yudhisthir Lal was

utilized by the firm free of interest. Further, in this case, there was no question of any services being rendered by the three minors and therefore the share income received by them must, in substance, be regarded as a return made to the family because of the investment of family funds in the business. In our view, therefore, the taxing authorities as also the Tribunal and the High Court were right in assessing the said income in the hands of the Hindu Undivided Family assessee.

11. The appeal is, therefore, dismissed with costs.

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