

# ANDHRA PRADESH HIGH COURT

Hiranand Ramsukh

Vs

Commissioner of Income-Tax

(Kumarayya J.)

21.12.1961

## JUDGMENT

### **Kumarayya J.**

1. The Income-tax Appellate Tribunal, Hyderabad Bench, has on the requisition of this court referred under section 66(2) the following questions for determination :

"1. Whether, on the facts and in the circumstances of the case, the Tribunal was justified in refusing to recognise Venugopal as a genuine partner of the firm ? and

2. Whether, on the facts and in the circumstances of the case, the department was justified in law in refusing to register the firm under section 26A of the Indian Income-tax Act ?"

These questions arise out of the order refusing registration under section 26A of the Act for the five assessment years beginning from 1951-52 and ending with 1955-56. The assessee's firm originally consisted of two partners, Ramprasad and Bhagwandas, with equal shares. But later on Ramprasad took in Mrs. Chandrabai, his aunt, as partner with Rs. 0-4-0 share by splitting up his own share of Rs. 0-8-0. These two shares were further split up and Ramprasad's minor son, Venugopal, was given Rs. 0-6-0 share. The application for registration on that basis was made to the Income-tax Officer at the time of 1950-51 assessment. But the income-tax Officer found that Chandrabai and the minor, Venugopal, were not genuine partners in the firm and on that basis refused to register the firm showing them as partners. Again when for the assessment years in question renewal of registration was sought for, the Income-tax Officer refused to register on the ground that Chandrabai and Venugopal are not real partners but have been merely shown as such in order to reduce the incident of tax of Ramprasad who had Rs. 0-8-0 share but had collusively made over Rs. 0-7-0 out of it in favor of Chandrabai and Venugopal. This order was upheld eventually by the Income-tax Appellate Tribunal. The question then is whether the order of refusal to registration is justified by the provisions of section 26A of the Income-tax Act. At the very outset, we may notice the fact that this court, at the time when the application under section 66(2) was made, upheld the view that whatever may be the case with Venugopal, Mrs. Chandrabai

was not a genuine partner. The Tribunal Nevertheless was required to state the case as there was a questions law arising out of its order which, on the application of the party, ought to had been referred by the Tribunal. So, then, the only question that is material is whether the income-tax authorities could not, in law, refuse registration, even though at least one of the partners was not a genuine partner. If that is decided against the assessee, the first question need not be answered at all. Mr. Ranganathachari, the learned counsel for the petitioner, contends that under section 26A it is not open to the income-tax authority to refuse registration of the firm on the mere ground that a partner have dealt with the beneficial ownership in respect of his share in any particular manner. He argues further that when the partners of a firm have, in their application for registration stated truly the position of the partners qua the firm, the firm ought to be registered. In support of his argument, he has relied on Commissioner of Income-tax v. A. Abdul Rahim & Co. Before we deal with this contention, we may notice the relevant statutory provision in this behalf. Section 26A reads thus :

"26. (1) Application may be made to the Income-tax Officer on behalf of any firm, constituted under an instrument of partnership specifying the individual shares of the partners, for registration for the purposes of this Act and of any other enactment for the time being in force relating to income-tax or super-tax.

(2) The application shall be made by such person or persons, and at such times and shall contain such particulars and shall be in such form, and be verified in such manner, as may be verified in such manner, as may be prescribed and it shall be dealt with by the Income-tax Officer in such manner as may be prescribed."

It would appear from the provision that in order that a firm may be entitled to registration, it is necessary (i) that the application for registration must be made on behalf of a firm; (ii) that the firm must have been constituted under an instrument of partnership; (iii) that the instrument of partnership must specify individual shares of the partners; and (iv) the said application should comply with all requirement contemplated by sub-section (2). Sub-section (2) leaves all the details as to who should make the application, what should be its contents and in what form or manner it should be presented only to the Rules. Of the relevant Rules framed under the statute, rule 2 requires that such an application should be signed by all the partner, not being minors, personally, and also refers to the item in which the application should be made in each case. Rule 3 prescribes the forms of the application and enjoins, inter alia, that it should be normally accompanied by the original instrument of partnership under which the firm is constituted. The form prescribed is set out in detail. In paragraph 3 of the form, it has to be certified that the profit or loss if any of the relevant period were divided or credited as shown in section B of the Schedule and that the information given in the form and the Schedule in correct. Section 3 of the Schedule, it must be remembered, requires the particulars of apportionment of the income, profits or loss of the business in the previous year between the partner who in that previous year were entitled to share in such income profits or gains. Rule 4 says that if, on receipt of the

application referred to in rule 3, the Income-tax Officer is satisfied that there is or was a firm in existence, constituted as shown in the instrument of partnership, and that the application has been properly made, he shall enter in writing at the foot of the instrument or certified copy, a certificate stating that the instrument has been registered with him and it will have effect from the assessment year in question. Sub-clause (2) of rule 4 provides that, if the Income-tax Officer is not so satisfied, he shall pass an order in writing refusing to recognise the instrument of partnership or the certified copy thereof and furnish a copy of such order to the applicants. So, then, under the provisions referred to above on receipt of an application for registration of a firm, the Income-tax Officer has to be satisfied whether there is or was a firm constituted as shown in the instrument and whether the application has been properly made. He is entitled in that connection to examine whether the partnership is true, whether each of the partners mentioned therein is a real partner, whether the shares are properly specified and are real ones and whether the profits which are to be distributed under the deed will truly be the profits of those particular individuals. If he is not satisfied as to the genuineness with regard to any of these things, it is open to him to reject the application on the ground that there was no genuine partnership brought into existence by the deed. It is clear that the above mentioned section, rules and the particulars required in the particulars required in the form have been carefully designed to enable the assessment of the registered firm to be done in the manner provided under sub-section (5) (a) of section 23 of the income-tax Act. That is that reason why care has been taken to see that the partners and the precise shares of each of the partners with necessary particulars are correctly brought to the notice of the authorities. It should be borne in mind that the provision in section 26A is only a sort of privilege conferred on the firms so that they may get the benefit of lower rates of assessment applicable to the individual partners whenever such rates are lower than the rates applicable to the computed income of the firm as a whole. The firm, therefore, must conform strictly and rigidly to the requirements provided by law. In other words, if the application is not properly made or does not contain the true state of affairs, if the individual shares of the partners specified in the instrument of partnership or in the application are not the true shares of the partners, the income-tax authority is perfectly justified in refusing registration. That is also what has been observed in Central Talkies Circuit, Matunga, In re. In that case Beaumont C.J. observed thus :

"Under rule 2 the only person who can apply for registration is a firm constituted under an instrument of partnership specifying the individual share of the partners, which must, of course, mean specifying correctly the individual shares of the partners. I think it is open whether under the old rule or the new rule, to the Income-tax Officer of the partners and, therefore, there is no proper application by the requisite firm."

At another stage, he observed :

"I think it must specify correctly the individual and beneficial shares, because that is a matter which is relevant from the point of view of the income-tax authorities."

Kania J. (as he then was) observed thus :

"It appears to me that if it is conceded that the Commissioner has the power to inquire whether the partnership deed as put forth by the applicants is genuine or not, it does not involve a consideration whether the share of an individual partner as mentioned therein is also correctly stated or not. For example, if the share of a partner were stated to be 5 annas, and on an open inquiry and taking evidence the Commissioner definitely came to the conclusion that the share was 4 annas, the partnership agreement as put forth by the applicants would not be correct, and there appears to be little doubt that the Commissioner would be entitled to hold that the deed executed by the applicants was not a correct partnership deed."

In the present case it would appear that though Srimathi Chandrabai has been shown as a partner and her share have been specified as Rs. 0-1-0, she is neither a genuine partner nor has she got a beneficial interest in the share entered in her name in the instrument of partnership. In these circumstances, on the proper construction of the relevant provision and rules, it is obvious that the Income-tax Officer was perfectly within his powers in refusing to register this firm. In *Raju Chettiar & Brother v. Commissioner of Income-tax*, the Madras High Court elaborately dealt with this question and came to the conclusion that if registration has to be obtained under section 26A of the Indian Income-tax Act it can only be by a genuine firm which specified the actual share of each partner and when that is not done, the Income-tax Officer is competent, if not bound, to refuse registration. It was a case where the Income-tax Officer refused registration of the firm on the ground that there was no genuine partnership and the shares shown as belonging to the widow therein did not belong to her and the deed thus did not specify the real partners and their shares. The learned judges after elaborate discussion on the subject and purpose of section 26A and the rules framed in that behalf observed :

"It must be remembered that registration of firms under the Income-tax Act is not a general or common law right, but it is a privilege given to the firms in order to enable them to get the benefit of the lower rates of assessment applicable to the individual partners wherever such rates are lower than the rate applicable to the computed income of the firm as a whole. If a firm desires to have this privilege it must conform strictly and rigidly to the requirements provided by the law."

They further observed that :

"There can be no doubt upon the authorities that the Income-tax Officer is entitled to examine when an application for registration of a firm is made whether the partnership is genuine, whether each of the partners mentioned therein is a real partner, whether the shares are specified properly, whether the shares specified are real ones and whether the profits which are to be distributed under the deed will truly be the profits of those

particular individuals. If he finds that there is no genuineness with regard to any of these things it is open to him to reject the application on the ground that there is no genuine partnership brought into existence by the deed."

With respect, we find ourselves in complete agreement with the observations made. This case does not appear to have been cited before the learned judges of the Gujarat High Court in Commissioner of Income-tax v. A. Abdul Rahim & Co. Of course the Bombay case was brought to their notice. Their statement of law on the point is contained in the following observations :

"While applying the provisions of law to the facts of the present case, what we have to consider is, whether the deed of partnership in case, question correctly sets out the names of the partners and correctly such agreement in this respect amongst the partner, then that deed of partnership is not liable to be registered. If there is an arrangement arrived at between two out of the four partners of the firm binding on those two partners alone and not binding on the partnership, the same cannot be taken into consideration for the purpose of considering whether the instrument of partnership is one which is capable of being registered under the provisions of the Act. If there is an arrangement amongst all the partners that the share standing in the name of the partner. Abdulrehman Kalubhai, was not to belong to him but to the partner. Abdul Rahim Valibhai, then the deed of partnership would no represent the true position amongst the partners and their true shares in the firm and the instrument would not be liable to be registered under the Act. In the present case there is no finding given by the Appellate Tribunal to the effect that an agreement was arrived at amongst all the partners that the share of Abdulrehman Kalubhai should be treated as the share of his uncle, Abdul, Rahim Valibhai. In the Circumstances, it is not possible for us to hold that the firm had not made a true disclosure in the deed of partnership about the names of the partners and their respective shares and was disentitled to have itself registered under the provisions of section 26A of the Income-tax Act."

With deference we cannot wholly agree with this proposition. It cannot be said that even though the form attached to rule 3 contemplates correct statement of information and the Income-tax Officer comes to the conclusion that any one or more of the partners shown as partner or partners is a mere name-lender and has no beneficial interest in the share specified in the instrument and the application and thus the information given in the application is incorrect, the fact that some of the partners may not be aware of this or that it was a term of the agreement of partnership, would not affect the power of the Income-tax Officer to refuse the instrument of partnership or the application does not reflect the true state of affair. We however prefer to follow the view taken by the Madras and Bombay High Courts as the correct view. We therefore answer question No. 2 in the affirmative. In this view it is necessary to answer question No 1. The assessee will pay the cost of the department. The advocate fee is fixed at Rs. 200. Questions answered in the affirmative.

