

# KERALA HIGH COURT

C.T. Palu & Sons

Vs

Commissioner of Income-Tax

(M Isaac, C.J. P N Pillai, J.)

22.10.1968

## JUDGMENT

**Isaac, J.**

1. This is a reference under Section 256(1) of the Income-tax Act, 1961, on the application of the assessee. The question referred is :

"Whether, on the facts and in the circumstances of the case, the assessee-firm is entitled to registration for the assessment year 1963-64 under Section 185 of the Income-tax Act, 1961 ?"

2. The firm Messrs. C. T. Palu & Sons was originally formed with four partners under a deed of partnership dated April 15, 1957. The partners of the firm were (1) C. T. Palu, (2) Chinnamma, the wife of Palu, (3) Thomas and (4) Joseph, parties (3) and (4) being the sons of parties (1) and (2). Joseph was then a minor; and he was represented in the execution of the deed by Palu, who was his legal guardian. Palu retired from the firm with effect from November 30, 1960; and consequently the firm was reconstituted by the three remaining partners by a deed dated December 1, 1960. Joseph, the minor, was represented in this deed by the mother as guardian. Appendix "B" to this reference is a copy of this deed. It provided, among other things, that the profit and loss of the business would be divided among the three partners in the ratio of 50 : 25 : 25, and that Chinnamma would act on behalf of the minor in all matters relating to the partnership business. A deed of clarification was executed on March 26, 1963, between Chinnamma and Thomas. Appendix "C" is a copy of this deed. It stated, among other things, that the minor, Joseph, was intended to be joined in the partnership constituted as per deed dated April 15, 1957, only as a beneficiary, that the said minor joined in the partnership re-constituted by the deed dated December 1, 1960, also only as a beneficiary, that the said deed of clarification was being executed, as it was likely to be misunderstood that the minor was also a partner, since the minor's guardian signed the deed on behalf of the minor, and that the minor would not be liable for the loss and liabilities of the firm, but he would get 25% of the profit as a beneficiary. This deed also provided that its provisions would be deemed to have come into effect on December 1, 1960, and treated as part of the partnership deed dated December 1, 1960.

3. According to the assessee, the firm had applied for registration and registration was granted for

the assessment year 1961-62. But there is no finding to that effect; and there is no material in the records before us to support it. However, on June 28, 1962, the assessee forwarded to the Income-tax Officer a declaration dated April 1, 1962, under Section 184(7) of the Income-tax Act, 1961, for continuation of the registration of the firm. This was received by the Income-tax Officer in connection with the assessment for 1962-63; but the year of assessment shown in the declaration was 1963-64. The registration for 1962-63 was refused on the ground that there was no valid partnership deed, as the partnership included the minor and the deed was also executed by the minor. The assessee claimed that the above declaration should be treated as relating to 1963-64, and the firm should be registered for the said year on the basis of this declaration. The Income-tax Officer refused registration stating that the declaration really related to the year 1962-63, and that the clarification deed dated March 26, 1963, was not valid, as the minor was not a party to that document. The assessee filed an appeal; and the Appellate Assistant Commissioner allowed it, holding that the declaration filed by the assessee should be treated as one for the assessment year 1963-64, and that, if it was defective, the Income-tax Officer should have pointed it out to the assessee and obtained a proper application. The Income-tax Officer filed an appeal from this decision; and the Appellate Tribunal allowed the appeal and restored the order of the Income-tax Officer, though for different reasons. The reasons stated by the Tribunal are :

"1. The deed of partnership dated December 1, 1960, as modified by the clarification deed dated March 26, 1963, stated that the minor shall not be liable for the loss and liabilities of the firm, and that the same shall be borne only by the two major partners. But it does not state in what proportion the loss should be shared by them. The deed states that the profit shall be shared in the ratio of 50 : 25 : 25. In the absence of a provision to the contrary, the loss is to be shared in the same proportion as the profit; and it would mean that 50% of the loss would be borne by one partner and 25% by the other. There was no legal liability for them to bear the balance 25% of the loss.

2. The clarification deed effected a change in the constitution of the firm, as it brought about a change in the shares of the profit and loss of the firm among the partners. Therefore, an application for registration was necessary."

4. The learned counsel for the assessee canvassed before us the correctness of the grounds stated by the Appellate Tribunal for refusing registration of the firm. He submitted that, if the shares of the partners in the profit of the business are specified in the deed of partnership, it is not necessary to specify the shares in the loss, as the law provides that, in the absence of a contract to the contrary, the loss shall be borne in the same proportion as the profit. In support of this position, he relied on the decision of the Mysore High Court in *R. Sannappa and Sons v. Commissioner of Income-tax*<sup>1</sup>, A different view has been taken by the Gujarat High Court in *Thacker & Co. v. Commissioner of Income-tax*<sup>2</sup>, We need not, however, examine the comparative merit of these two views because, on the facts of the instant case, the position is different. As the Appellate Tribunal has pointed out in this case, the partnership deed as amended by the deed of clarification provides that the profit is to be shared among the two major partners and the minor admitted to the benefits of the firm in the proportion of 50 : 25 : 25 and that the minor is not liable for the loss ; but no provision is made regarding the sharing of the loss. The liability of the major partners is, therefore, only to bear the loss in the proportion in which they are entitled to share the profit. This means that they are liable to bear 50% and 25% each of the loss; and the deed of partnership is blank regarding the sharing of the balance 25% of the loss. In our view, this is sufficient to disentitle the firm for registration.

5. There is also another formidable obstacle for granting registration to the assessee-firm. Admittedly, it was refused registration for the year 1962-63. The deed of partnership dated December 1, 1960, did not create a valid partnership, as by this deed the minor was made a full-fledged partner, and he was also made liable for proportionate loss of the partnership business: vide the decision of the Supreme Court in *Commissioner of Income-tax v. Dwarkadas Khetan*<sup>3</sup>. A valid partnership was constituted only by the execution of the deed of clarification on March 26, 1963. Therefore, there was no question of renewal of registration. It was open for the assessee to apply for the registration of the firm for the year 1963-64. Admittedly, it has not made any such application. All that it did was to file a declaration under Section 184(7) of the Income-tax Act, 1961, as if there was a firm which was registered for the previous assessment year.

6. In the result, we answer the question in this reference in the negative and against the assessee. The parties will bear their own costs. A copy of this judgment will be forwarded to the Income-tax Appellate Tribunal as required by Section 260(1) of the Income-tax Act.

#### Cases Referred.

1[1967] 66 I.T.R. 27

2[1966] 61 I.T.R. 540

3[1961] 41 I.T.R. 528; [1961] 2 S.C.R. 821