

# KERALA HIGH COURT

Commissioner of Income-Tax

Vs

Ithappiri & George

(P.G Nair and T K Iyer, JJ.)

17.11.1971

## JUDGMENT

**P G Nair, J.**

1. This is a reference under Section 256(1) of the Income-tax Act 1961, at the instance of the department. The assessee is a firm. The year of assessment is 1965-66, the corresponding accounting period being that ended on March 31, 1965. The question referred is :

" Whether, on the facts and in the circumstances of the case, the Appellate Tribunal is correct in law in holding that the assessee-firm is entitled to registration under Section 185 of the Income-tax Act, 1961, for the assessment year 1965-66 ? "

2. During the accounting period a partnership deed was entered into by the assessee-firm on March 22, 1965. The partnership deed is annexure "A". The relevant paragraph of the partnership deed for the purpose of this case is paragraph 6, which is in these terms :

" 6. The net profit of the business after adjustments shall be divided among the partners as shown below.

1. M.O. Ithappiri 30 Np. in the rupee
2. T.V. George 30 Np. in the rupee
3. M.I. Leelamma 20 Np. in the rupee
4. M.I. John 20 Np. in the rupee "

3. There is no provision in the partnership deed about the manner in which the losses of the firm, if any, should be borne by the parties. There is a provision in paragraph 10 which is in these terms :

" 10. In the event of the dissolution of the partnership the accounts of the partnership including all its assets and liabilities shall be taken (and the partnership wound up), and the assets distributed in accordance with the provisions of the Partnership Act."

4. This provision is however not material for the purposes of deciding the question before us.

5. The firm applied in the prescribed form for registration of the firm for the assessment year 1965-66. This application was refused by the Income-tax Officer on the ground that the instrument did not specify the individual shares of the partners in relation to the losses that the firm may sustain. In appeal, however, the Appellate Assistant Commissioner reversed the decision of the Income-tax Officer relying on Section 4 of the Indian Partnership Act, 1932. There was a further appeal before the Tribunal and the decision of the Gujarat High Court in *Thacker & Co. v. Commissioner of Income-tax*<sup>1</sup>, was relied on by counsel on behalf of the revenue in support of the contention that registration should be refused because the instrument of partnership did not satisfy the requirements of Section 184 of the Income-tax Act, 1961, in that the proportion in which the losses should be borne had not been stated in the instrument. The Tribunal however decided against the revenue on the ground that the preponderance of authority on the subject is in favour of the assessee. It referred to the decisions of the Allahabad and Mysore High Courts in *Hiralal Jagannath Prasad v. Commissioner of Income-tax*<sup>2</sup>, and in *R. Sannappa and Sons v. Commissioner of Income-tax*<sup>3</sup>,

6. Before us counsel for the assessee also invited our attention to an earlier decision of the Allahabad High Court in *Laxmi Trading Company v. Commissioner of Income-tax*<sup>4</sup>, and the decision of the Mysore High Court in *R.B. Angaili and Sons v. Commissioner of Income-tax*<sup>5</sup>, as also the decisions of the Andhra Pradesh High Court in *Addepally Nageswara Rao and Brothers v. Commissioner of Income-tax*<sup>6</sup>, and of the Bombay High Court in *In re Parekh Wadilal Jiwanbhai*, [1961] 42 I.T.R. 266 (Bom.)(Supra). Counsel on behalf of the revenue mainly relied on the decisions of the Gujarat High Court in *Thacker & Co. v. Commissioner of Income-tax*, as well as the decision of the Supreme Court in *N. T. Patel & Co. v. Commissioner of Income-tax*<sup>7</sup> [Reference has also been made to a decision of this court in *C. T. Palu & Sons v. Commissioner of Income-tax*<sup>8</sup>

7. On a perusal of these decisions it is clear that there is a conflict of judicial opinion on the question as to whether an instrument of partnership for the purposes of Section 184 of the Income-tax Act, 1961, should specify the individual shares of the partners so far as losses of the firm are concerned. The decision in *Thacker & Co. v. Commissioner of Income-tax* has laid down that the partnership deed should specify the individual shares of the partners so far as losses are concerned. The Allahabad, Mysore, Andhra Pradesh and the Bombay High Courts have taken a contrary view. This court did not determine this question as the decision turned on the interpretation of the partnership deed before the court though it too proceeded on the basis that a specification of the share of losses is necessary to satisfy the section at least in cases where minors were partners of the firm in the sense that they were admitted to the benefits of the partnership. We do not think that the matter is open for discussion in view of the observations contained in the judgment in *N. T. Patel & Co. v. Commissioner of Income-tax*. The question that arose for decision before the Supreme Court involved the interpretation of a partnership deed in which there was no specification of the shares of the partners either regarding profits or losses. This was apparently an omission and a rectification was made after the relevant accounting period. Negating the contention that this rectification deed would have the effect of supplying the lacuna in the partnership deed drawn up, the following observation was made by the Supreme Court after a detailed examination of Clauses 9, 11, 34 and 41(a) of the partnership deed that was construed :

" But, in none of these clauses is it stated what the shares of the partners in the profits and losses of the firm were to be and that in our opinion was requisite for registration of the

partnership under Section 26A of the Act and as that was wanting, registration was rightly refused."

8. The use of the words " profits and losses " in the above sentence is significant. It is dear that the judgment proceeds on the basis that for satisfying Section 26A of the Indian Income-tax Act, 1922, there must be a specification of the shares of the profits and losses. The wording in Section 184 of the Income-tax Act, 1961, is in material respects similar to the wording of the section that was construed by the Supreme Court. We think, therefore, we are bound by the observations.

9. We may add that the expression in Section 184 " the individual shares of the partners " are wide enough to take in both shares in profits and losses. When it is borne in mind that the application for registration of a firm is " for the purposes of the Act" as is stated in Section 184(1) we must refer to the provisions of the Act to find out the purposes of the Act and in this connection Section 182(2) of the Act is relevant. We shall extract Section 182(1) and (2).

" 182. (1) Notwithstanding anything contained in Sections 143 and 144 and subject to the provisions of Sub-section (3), in the case of a registered firm, after assessing the total income of the firm,--

(i) the income-tax payable by the firm itself shall be determined; and

(ii) the share of each partner in the income of the firm shall be included in his total income and assessed to tax accordingly.

(2) If such share of any partner is a loss it shall be set off against his other income or carried forward and set off in accordance with the provisions of Sections 70 to 75."

10. It is thus clear that the assessing authorities will necessarily have to determine the share of the loss of every individual partner of a registered firm so that the loss may be set off against the other income of the partner or carried forward and set off in accordance with the provisions of Sections 70 to 75 of the Income-tax Act, 1961. The specification of the proportion in which loss is to be shared, therefore, assumes an importance almost equal to that of the specification of the shares in the profit which is necessary for assessing the individual partners on their share of the income coupled with their other income.

11. The question is not whether there is any rule of law discernible either from Section 13(b) of the Indian Partnership Act, 1932, or from any general principle from which it is possible to discern the proportion in which the losses should be shared but as to whether Section 184 insists that this should be stated in the instrument. As we said the expression used in the section must normally cover both aspects of profits and losses. There is no compelling reason to read down the expression and give it a limited meaning. Question of hardship cannot justify the adoption of such a course. The words have to be understood as including both profits and losses,

12. We answer the question referred to us in the negative, that is, in favour of the department and against the assessee.

13. A copy of this judgment under the seal of the High Court and the signature of the Registrar will be sent to the Appellate Tribunal as required by Sub-section (1) of Section 260 of the Income-tax Act, 1961.

14. There will be no orders as to costs.

Cases Referred.

- 1[1966] 61 I.T.R. 540 (Guj)
- 2[1967] 66 I.T.R. 293 (All)
- 3[1967] 66 I.T.R. 27 (Mys)
- 4[1966] 62 I.T.R. 770 (All)
- 5[1969] 73 I.T.R. 93 (Mys)
- 6[1971] 79 I.T.R. 306 (A.P)
- 7[1961] 42 I.T.R. 224 ; [1962] 1 S.C.R. 251 (S.C.)
- 8[1969] 72 I.T.R. 611 (Ker)