

PATNA HIGH COURT

Commissioner of Income-Tax

Vs

Prakash Ram Gupta

(U.N Sinha and Kanhaiyaji, JJ.)

08.11.1968

JUDGMENT

U.N. Sinha, J.

1. These two references under Section 66(1) of the Indian Income-tax Act, 1922, have been heard together and this judgment will govern both the cases. The question of law, which has been referred to this court covering both the cases, is as follows :

" Whether, on the facts and circumstances of the case, the assessee-firm was legally entitled to registration under Section 26A of the Indian Income-tax Act for the assessment years 1959-60 and 1960-61 ? "

2. The relevant facts are as follows :

3. One Prakash Ram Gupta used to carry on business in country liquor and Pachwai at Jharia, Bararee, Bhagatdin and Rourkella and by an agreement in writing dated the 1st April, 1959, he agreed to take one Mahadeo Ram as a partner in the Bararee country liquor shop and in the Pachwai shop at Bhagatdin, on certain terms, and thereafter these two persons entered into a partnership by a registered deed executed on the 21st November, 1959. In due course, the firm named Prakash Ram Gupta applied under Section 26A of the Income-tax Act, 1922, for registration of the firm for the assessment year 1959-60. This application was rejected by the Income-tax Officer by an order dated the 29th February, 1960, It was held that by the partnership deed Sri Prakash Ram Gupta sought to transfer the business of the firm and as the excise law prohibited such a transfer of licence the firm did not have any legal existence and it cannot be recognised. For the assessment year 1960-61 the firm named Prakash Ram Gupta had again applied for registration under the same provision of law and this was also refused by the Income-tax Officer by his order dated the 24th January, 1961. By this order it was held that the licensee was Sri Prakash Ram Gupta and, as the excise law prohibited transfer of a licence from one

person to another, the transfer by Sri Gupta to a firm consisting of himself and Sri Mahadeo Ram was illegal. The assessee-firm went up in appeal with respect to the assessment year 1959-60 and by order dated the 19th July, 1960, the appeal was dismissed. It was held by the Appellate Assistant Commissioner that the transfer of licence by Sri Prakash Ram Gupta was illegal and, therefore, there was no legal firm in existence during the accounting year under consideration. It may be stated here that the assessee-firm had also filed an appeal against the order of the Income-tax Officer dated the 24th January, 1961, with respect to the assessment year 1960-61. From the order of the Appellate Assistant Commissioner with respect to the assessment year 1959-60, the assessee-firm went up in appeal before the Income-tax Appellate Tribunal, and by the order dated the 14th December, 1961, the Patna Bench of the Tribunal allowed the appeal and remanded the case to the Appellate Assistant Commissioner. The relevant portion of the order may be quoted here :

" Therefore, before deciding whether a valid partnership exists or not there has to be a finding of fact as to whether the excise licence obtained by Prakash Ram Gupta has been transferred to the partnership. This is a matter on which the fact has to be found with reference to the account books of the firm. Since neither the Income-tax Officer nor the Appellate Assistant Commissioner have adverted their mind to this aspect of the matter, we would set aside the order of the Appellate Assistant Commissioner and direct him to dispose of the appeal de novo after recording a finding as to whether the excise licence obtained by Prakash Ram Gupta has in fact been transferred to the partnership."

4. In view of the directions given in the order of remand, a report was called for by the Appellate Assistant Commissioner regarding the alleged transfer of licence and a report dated the 30th May, 1963, was sent by the Income-tax Officer stating that the licence obtained by Sri Prakash Ram Gupta had not been transferred at any time during the years 1959-60 to 1961-62. Thereafter, the Appellate Assistant Commissioner by his order dated the 5th July, 1963, decided the two appeals with respect to the assessment years 1959 60 and 1960 61. He dismissed the appeals by the assessee-firm although he came to the conclusion that the objection that had been raised by the Income-tax Officer for refusing registration for these two years was no longer valid. He, however, held that, on the facts of the case, the alleged partnership between Sri Prakash Ram Gupta and Sri Mahadeo Ram was not a genuine and valid one. Two appeals were preferred by the assessee-firm, and the Income-tax Appellate Tribunal, Patna Bench, allowed them by a consolidated judgment dated the 10th July, 1964, directing that the appellant-firm should be registered for both the years 1959-60 and 1960-61. The reasons given by the Appellate Assistant Commissioner for refusing registration were not accepted to be valid reasons, Thereafter, the Commissioner of Income-tax, Bihar and Orissa, Patna, applied under Section 66(1) of the Indian Income-tax Act, 1922, in these two cases for referring the questions of law arising on the facts

and circumstances of the two cases to this court and the reference has thus arisen.

5. In order to appreciate the contentions raised by the parties in these two cases, the following clauses of the deed of partnership dated the 21st November, 1959, are quoted : (The first party refers to Sri Prakash Ram Gupta and the second party refers to Sri Mahadeo Ram), " 1. The first party abovenamed has obtained the necessary excise licence in his name to carry on the business of sale of country liquor at Bararee and Pachwai at Bhagatdin.

2. The said business will be carried on under the name of the first party from its head office at Jharia with shops or branches at Bararee and Bhagatdin within the District of Dhanbad.

3. The working and management of the said liquor shop business shall be under the supervision of the 2nd party who will remain in sole charge of the business as a working partner.

4. The first party shall invest the entire capital for carrying on the said business properly and the 2nd party will not have to contribute any money for the said purpose.

5. The 2nd party shall devote the whole of his time and attention to the proper management of the said liquor shops and shall attend diligently to the business and shall not be entitled to work elsewhere during the period of this partnership.....

7. The second party shall carry on the liquor shop business in a profitable and businesslike way and shall duly observe all rules and regulations of the Excise Act in force or to be in force during the continuance of the partnership.....

9. Further investments required from time to time for purchase of liquor and other necessary articles for carrying on the liquor shop business shall be made by the first party alone.

10. The second party shall have no right to the assets of the liquor shop business and shall make over charge of all such assets to the first party on the termination of this partnership.....

14. A general account of the assets, liabilities and transactions of the liquor shop business mentioned above shall be taken at the end of each English financial year and the net profit of the business shall be divided between the parties according to the following shares :

(1) Shri Prakash Ram Gupta (1st party) 3/4th (three-fourth).

(2) Mahadeo Ram (2nd party) 1/4th (one-fourth) and if there be any loss, the entire loss will be borne by the first party and the 2nd party will not be liable to bear any part of such loss nor the 2nd party will be required to refund the monthly advance withdrawn by him ; the same will be treated as a remuneration for his work and labour. "

6. Learned counsel appearing for the Commissioner of Income-tax has referred to Sections 22 and 23 of the Bihar and Orissa Excise Act, 1915 (Act No. II of 1915) and they are reproduced below :

" 22. Grant of exclusive privilege of manufacture and sale of country liquor or intoxicating drugs.--(1) The State Government may grant to any person, on such conditions and for such period as it may think fit, the exclusive privilege--

(a) of manufacturing, or supplying wholesale, or

(b) of manufacturing and supplying wholesale, or

(c) of selling wholesale or retail, or

(d) of manufacturing or supplying wholesale and selling retail, or

(e) of manufacturing and supplying wholesale and selling retail any country liquor or intoxicating drug within any specified local area :

Provided that such public notice shall be given of the intention to grant any such exclusive privilege, and that any objection made by any person residing within the area affected shall be considered before an exclusive privilege is granted.

(2) No grantee of any privilege under Sub-section (1) shall exercise the same unless or until he has received a licence in that behalf from the Collector or the Excise Commissioner. "

" 23. Transfer of exclusive privilege.--(1) A grantee of an exclusive privilege under Section 22 shall not let or assign the same or any portion thereof unless he is expressly authorized, by a condition made under that section, to do so.

(2) Such letting or assignment shall be made only to a person approved by the Collector or (if the letting or assignment extends to more than one district) the Excise Commissioner.

(3) The lessee or assignee shall not exercise any rights as such unless and until the Collector has, upon his application, granted him a licence to do so. "

7. It is contended by the learned counsel for the Commissioner of Income-tax that the formation of the partnership in question amounted to a transfer of the privilege given to Sri Prakash Ram Gupta under Section 22 of the Excise Act, that is to say, the excise licence, and secondly, the

business of the two shops mentioned in the partnership deed having been transferred by Sri Prakash Ram Gupta to the firm, there has been a contravention of Section 23 of the Excise Act. The first question raised by the learned counsel is fully answered by the Supreme Court decision of Umacharan Shaw & Bros. v. Commissioner of Income-tax, [1959] 37 I.T.R. 271 (S.C.). The following observations of their Lordships at page 276 may be noted :

" Though the Tribunal stated that it had not proceeded on the ground that the partnership was illegal being against the Bengal Excise Act, 1911, the argument was referred to as supporting the conclusion that the firm was not genuine. Section 42(1)(a) of the Bengal Excise Act reads :

'42. (1) Subject to such restrictions as the State Government may prescribe, the authority who granted any licence, permit or pass under this Act may cancel or suspend it...

(a) if it is transferred or sub-let by the holder thereof without the permission of the said authority.'

There was no evidence that the excise licences were transferred or sub-let."

8. If the mere formation of a partnership in which the licensee is a partner amounts to a transfer or sub-lease of the licence, their Lordships of the Supreme Court would not have stated that there was no evidence that the excise licences were transferred or sub-let. Therefore, the real question in these two cases for consideration is whether Sri Prakash Ram Gupta had sub-let or assigned the licence obtained by him to the firm. This point is really the second point raised by the learned counsel for the Commissioner of Income-tax, although he has put his argument in the manner mentioned above, that is to say, he has referred to the transfer of the business of the two shops to the firm as constituting a transfer of the licence. On this point, the principal case on which reliance has been placed by the learned counsel is a case of the Orissa High Court, namely, Mohapatra Bhandar v. Commissioner of Income-tax, [1965] 58 I.T.R. 671, 674. In my opinion, Mohapatra Bhandar's case: is distinguishable on facts and the principle applied by the learned judges of the Orissa High Court will not apply on the terms of the partnership deed of these cases. The learned judges stated as follows : "This finding clearly shows that the firm did not merely takeover the financial part of the business but the entire business including its management. The business here consists merely in storing and selling excisable goods like opium and ganja and when the income-tax authorities have categorically held that this business was handed over by the licensee to the firm and the firm managed this business during the year in question, it must be held that there was a complete transfer of the business against the provisions of the excise rules prevailing in the State."

9. Then the learned judges, after distinguishing a decision of this court in the case of Commissioner of Income-tax v. K. C. S. Reddy, [1960] 38 I.T.R. 560 stated that the partnership deed of Mohapatra Bhandar's case showed that the firm carried on " business ", which would necessarily mean securing, possessing and selling of excisable articles in question. The distinction between Mohapatra Bhandar's case and the instant cases are these :

(a) The licensee of the Orissa case was unable to finance the excise business individually and he had made over the business to the firm in lieu of finance. It was agreed that the partners would share the profit or loss according to the share of each partner in the firm. In the instant cases, the entire capital was to be invested by Sri Gupta, and Sri Ram was not called upon to contribute any money for carrying on the business. Sri Ram had no right to the assets of the liquor shop business. He was entitled only to the one-fourth of the profit, if any, and he was not liable for any loss.

(b) The learned judges held in Mohapatra Bhandar's case that the work of securing, possessing and selling of excisable articles had been transferred to the firm. In the instant cases, it was stated in the partnership deed that the working and management of the liquor shop business was under the supervision of Sri Ram and he had to observe all rules and regulations of the Excise Act in force or to be in force during the continuance of the partnership. Therefore, it is not possible to hold that Sri Ram could actually conduct the sale of the country liquor and Pachwai covered by the licence, in contravention of Section 22 of the Excise Act. It is clear that under the partnership deed Sri Ram was entitled to the supervision of the working and the management of the business only.

(c) In Mohapatra Bhandar's case the licensee was Sri U. N. Mohapatra, whereas the firm was described as Mohapatra Bhandar and that firm had applied for registration under Section 26A of the Income-tax Act. In the instant cases, Clause (2) of the partnership deed states that the business will be carried on under the name of Sri Prakash Ram Gupta. In the circumstances, it is difficult to hold that by the partnership deed there was contravention of Section 23 of the Excise Act in the sense that the excise licence had been let or assigned to the firm by Sri Gupta.

10. Learned counsel for the Commissioner of Income-tax has relied upon a decision of the Madras High Court in *D. Mohideen Sahib & Co. v. Commissioner of Income-tax*¹, which was based on an earlier Full Bench decision of the same High Court in the case of *Velu Padayachi v. Sivasooriam Pillai*², Sri A. K. Sen, appearing for the firm, has argued that the principle followed by the learned judges of the Madras High Court is obliterated by the decision of their Lordships of the Supreme Court in Umacharam Shaw's case. In *D. Mohideen*'s case the learned judges of the Madras High Court referred to the Full Bench decision and stated that the Full Bench decision of that court held that a partnership entered into for the purpose of conducting a business

in arrack or toddy on a licence granted to only one or some of the partners was void ab initio, because such a partnership arrangement involved a transfer of the licence or was a breach of the Abkari Act punishable under that Act, because the unlicensed partner, by himself, or through his agent, the other partner, sells without a licence. The argument of Sri Sen is based on the decision of their Lordships of the Supreme Court. Challenging the correctness of the decisions of the Madras High Court cannot be said to be without force and Sri Sen has drawn our attention to a decision of the Andhra Pradesh High Court in the case of *Chandaji Sukhraj & Co. v. Lal and Co*³, where the Full Bench decision of the Madras High Court was not accepted as correct. Sri Sen has also relied upon a decision of the Bombay High Court in the case of *Champsey Dossa v. Gordhandas Kessowji*⁴, --on appeal A.I.R. 1921 P.C. 137 affirmed by the Privy Council, and the decision of this court in the case, *Commissioner of Income-tax v. K. C. S. Reddy*, for contending that Section 23 of the Excise Act has not been contravened by the partnership deed entered into by Sri Gupta and Sri Ram. In my opinion, the contentions raised by Sri Sen are valid. I shall first deal with the decision of the Andhra Pradesh High Court in *Chandaji Sukhraj & Co. v. Lal and Co.*, A.I.R. 1960 A.P. 444(Supra) Under the law that was involved in Chandaji Sukhraj's case every licence shall be deemed to have been granted or renewed personally to the licensee and no licence could be sold or transferred. On transfer of the business of the licensee to another person, the transferee had to take a fresh licence. If the holder of a licence entered into partnership in regard to the business covered by the licence, he had to report the fact to the licensing authority and get his licence suitably amended. The appeal in the Andhra Pradesh High Court arose out of a suit instituted by the plaintiff-firm for settlement of account of his partnership entered into with the first defendant-firm for a period of one year or, in the alternative, for dissolution of the partnership and for settlement of account. The first defendant had licence from the Government for dealing in tobacco. The trial court, dealing with the question of illegality of the partnership, decided the matter against the plaintiff in view of a fresh licence not having been obtained after the formation of the partnership, and the suit was dismissed. The High Court had to deal with the question as to whether the plaintiff's participation in the tobacco business as a partner was illegal or not. In that context, the learned judges of the Andhra Pradesh High Court were not inclined to follow the principle laid down in the Madras Full Bench decision and an earlier decision of that court in *Nalam Padmanabham v. Sait Badrinadh Sarda*⁵, No doubt, in Chandaji Shukhraj's case, the learned judges of the Andhra Pradesh High Court had put some stress on the fact that liberty had been given to the licensee to enter into partnership but reference was made to the case, *Champsey Dossa v. Gordhandas Kessowji*, and the affirming decision of the Privy Council reported in A.I.R. 1921 P.C. 137, mentioned above, and it is clear that the learned judges of the Andhra Pradesh High Court went on the broad principle as to the significance of the prohibition of the transfer of licences. In *Champsey Dossa's* case a licensee was not authorised to sub-let, sell, mortgage or otherwise alienate, in whole or in part, the privilege granted under a licence,

without the written permission of the Collector; nevertheless, some members of the family and others were taken in partnership and the Bombay High Court held that the admission of the partner to a share in the profit cannot be considered as sub-letting or alienation unless there was a document directly transferring to the partners or attempting to transfer to the partners a part of the right to manufacture or vend. In the instant cases, as stated earlier, Clause (7) of the partnership deed compelled Sri Ram to observe the rules and regulations of the Excise Act and, therefore, he cannot possibly claim to sell licensed commodity, as he himself was not a licensee, and, therefore, on the broad principle, I am inclined to agree with the principle laid down by the learned judges of the Andhra Pradesh High Court. In Champsey Dossa's case the learned judges of the Bombay High Court stated thus :

"The admission of partners to a share in the profits cannot be considered as sub-letting or alienation of a part of the privilege, unless there has been a document directly transferring to the partners or attempting to transfer to the partners a part of the right to manufacture or vend."

11. This decision was affirmed by their Lordships of the Privy Council. The next case to which our attention has been drawn by Sri Sen is the case of *Dayabhai & Co. v. Commissioner of Income-tax*⁶, a decision of the Madhya Pradesh High Court. That was a case under the Motor Vehicles Act of 1939, and, in substance, it was held that where a statute does not prohibit a licensee or permit-holder from taking a partner, but simply prohibits a transfer or sub-lease of the licence or the permit, then the licensee or the permit-holder by merely admitting a partner or partners in the business to which the licence or the permit relates, does not transgress the prohibition against transfer or sub-lease and the partnership is valid. That was also a case of registration under Section 26A of the Indian Income-tax Act. The case was decided on the principles laid down by the Supreme Court in Umacharan Shaw's case and those laid down by the Bombay High Court and affirmed by the Privy Council in *Gordhandas Kessowji v. Champsey Dossa*⁷, and on the decision of this court in the case of *Commissioner of Income-tax v. K. C. S. Reddy*. The principles laid down in *Velu Padayachi v. Sivasooriam Pillai* and *D. Mohideen Sahib & Co. v. Commissioner of Income-tax* and other cases of the same nature were dissented from. It now remains for me to consider this court's decision in *Commissioner of Income-tax v. K. C. S. Reddy*. That was also a case of an application for registration under Section 26A of the Indian Income-tax Act. I must state at this stage that there is a slight distinction between this earlier decision of this court and the instant cases, inasmuch as, under the partnership deed of the earlier case, one K. C. S. Reddy had obtained a licence under the Bihar Mica Act of 1947 and, thereafter, a partnership had been formed with him and others, under the terms of which K. C. S. Reddy was the managing partner. But, it would not make any difference in principle, because, as stated earlier, under Clause (7) of the partnership deed in question, the rules and regulations of the Excise Act had to be observed and the working and the management

of the liquor shop business had only been put under the supervision of Sri Ram. Therefore, it was in the contemplation of the two partners that the law regarding sale of liquor had to be observed as provided by Section 22 of the Excise Act. Hence registration under Section 26A was rightly ordered on the principle laid down by this decision.

12. On a consideration of the facts and circumstances of the case, I am of the opinion that the judgment of the Income-tax Appellate Tribunal dated the 10th July, 1964, was correct. As the assessee-firm was legally entitled to registration under Section 26A of the Indian Income-tax Act, 1922, for the years 1959-60 and 1960-61, the reference is answered against the Commissioner of Income-tax. The opposite party, the applicant for registration, will be entitled to costs, which I assess at Rs. 250.

Kanhaiyaji, J.

13. I agree.

Cases Referred.

1[1950] 18 I.T.R. 200

2A.I.R. 1950 Mad. 444 (F.B.)

3A.I.R. 1960 A.P. 444

4A.I.R. 1917 Bom. 250; 40 I.C. 805

5[1911] I.L.R. 35 Mad. 582; 21 M.L.J. 425

6[1966] 59 I.T.R. 364

7A.I.R. 1921 P.C. 137

