Privy Council Appeal No. 31 *of* 1940
Allahabad Appeal No. 25 *of* 1938

Dr. Sardar Bahadur Sir Sunder Singh Majithia (since deceased) – – – – – – – *Appellant*

v.

The Commissioner of Income Tax, United and Central Provinces – – – – – – *Respondent*

FROM

THE HIGH COURT OF JUDICATURE AT ALLAHABAD

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 4TH JUNE, 1942

Present at the Hearing:
LORD THANKERTON
LORD ROMER
LORD CLAUSON
SIR GEORGE RANKIN
SIR MADHAVAN NAIR
[*Delivered by* SIR GEORGE RANKIN]

This is an appeal by the assessees from a judgment of the High Court at Allahabad on a reference made under subsection (2) of section 66 of the Indian Income-tax Act, 1922. The question referred arises out of an assessment made for the year 1932-3 on the profits of a business carried on under the style of " The Saraiyar Sugar Factory " at Saraiyar in the district of Gorakpur in the United Provinces. The year of account is the year ending 30th September, 1931, in accordance with the accounting practice of the assessees. The matter of substance in the present dispute is whether the assessment should be made upon the footing that the business belonged to a Hindu undivided family or upon the footing that it belonged to a firm of which the father, mother and three sons were partners on the terms of a written instrument dated 12th February, 1933. The family are Sher Gill Jats of the Amritsar district of the Punjab. It is not disputed that they form a Hindu undivided family, but with them the general Hindu law is superseded by custom which provides special rules upon many points of family law. The present appeal was brought by Sir Sundar Singh Majithia as father and head of the family, but he has since died and the sons are now the appellants.

The written instrument dated 12th February, 1933, describes itself as an " agreement of partnership " and the parties to it are the father (first party), the mother (second party) and the three sons (third, fourth and fifth parties).

The recitals and clauses 2, 7 and 8 are as follows:—

> Whereas the First Party has set up machinery for manufacture of Sugar and extraction of essential oils in his estate in the Gorakhpur district at village Saraiya, *tappa* Keotali, pargana Hewali Gorakhpur, and Sugar and essential oils are manufactured there. And whereas under the personal law of the Parties who are Sher Gill Jats of Amristsar district in the Punjab, the father in his life time has a right to divide such property as aforesaid, and to give away shares, whether the nature of it is that of self-acquired or ancestral property. And whereas in exercise of the said right the First Party has given a share of three annas in the rupee to each of his sons the aforesaid Third Party, Fourth Party and Fifth Party, two of whom namely, the Third and Fourth Parties have worked hard in making the aforesaid business a success, and he has given a life interest in another share of three annas in the rupee as a special provision to his wife namely the Second Party, reserving a reversion of the said share to himself if he survives the Second Party, and if he does not then to the Third Party, the Fourth Party and the Fifth Party (or to their personal heirs in case of their

death) in equal shares, and has kept the remaining four annas in the rupee to himself. And whereas the Second, Third, Fourth and Fifth Parties having been admitted and accepted as Partners by the First Party all the parties to this deed have already entered into a Partnership to work the aforesaid Sugar and Oil manufacturing machinery and to carry on the business of manufacturing Sugar and Essential Oils, and to do any other business that all of them may agree to carry on for profit.

2. That the shares of the aforesaid Parties in the Capital, the profit and the loss of the business, are in proportion to the shares mentioned above, namely, the share of the First Party who is the Senior Partner, is four annas in the rupee, and of each of the other Parties, namely, the Second Party, the Third Party, the Fourth Party and the Fifth Party is three annas in the rupee.

7. That the liabilities, present (if any) and future of the aforesaid business are and will be the liability of all the partners and will be payable by them in proportion to their shares.

8. In future when further capital will be needed for working, improving or extending the business it will be contributed by all the parties in proportion to their shares.

By other clauses of the agreement it was provided (*inter alia*) that the partnership should not be liable to be dissolved, save with the consent of all the partners, before the 1st March, 1945; and that in case of death before that date of any of the partners the father's share should go to the sons in equal shares; the mother's to the father, and the share of a son to his legal heirs. The father and two of the sons were to manage the business, to keep and prepare proper accounts, and to have authority to raise loans (*inter alia*) for making any additions or improvements to the business. They were to draw monthly allowances—Rs. 2,000 in the case of the father, Rs. 1,500 in the case of each of the two sons. In the event of a difference of opinion between the partners the father was to have two votes and a casting vote, each other partner to have one vote.

Upon the terms of this agreement it is to be observed that it does not itself purport to effect any partition of family property or to be a transfer of any property moveable or immoveable by the father to the other parties. It recites that the father has given a share to the other parties. So, too, it does not state that the partnership came into existence on the date of the agreement, 12th February, 1933, but that the parties have already entered into a partnership. It would appear indeed to have been the assessees' case that the oral partition and commencement of the firm took place in September, 1931, and that certain entries were made in the books at that time.

Before 1932 the profits of the factory had been returned and assessed to tax as part of the income of the joint family; but on the 13th February, 1933—that is, towards the end of the year of assessment with which this appeal is concerned—the partnership agreement of the previous day was submitted to the Income-tax officer together with an application that the firm should be registered under section 26A of the Act and that the profits of the factory should be separately assessed as income of the registered firm. The Income-tax officer on the 18th April, 1933, allowed this application and made an order of assessment accordingly, but on 20th September, 1933, the Commissioner of Income-tax set aside his decision and directed that a new assessment be made. On 16th December, 1933, the Income-tax officer's successor made an assessment on Sir Sundar Singh which included the profits of the factory as his individual income. He refused to register the firm under section 26A. On appeal to the Assistant Commissioner the refusal to register the firm was upheld, but the profits of the factory were held to be assessable as income of the Hindu joint family. This order was passed on 10th April, 1935. On the 21st November, 1935, the Commissioner having been asked to review this decision in exercise of his powers under section 33 of the Act and to refer certain questions of law to the High Court, thought that it was desirable and sufficient to state a case for the opinion of the High Court on what he calls " the main question whether a genuine firm has come into existence." " The whole case for the refusal of the registration from the outset is based on the question whether or not the partnership deed has created a genuine firm such as is entitled to registration under section 26A and in the event of the assessee succeeding on this point the

registration will follow as an inevitable corollary." He formulated the question of law in the following terms:—

> In all the circumstances of the case, having regard to the personal law governing the assessee and the requirements of the Transfer of Property Act (IV of 1882) and the Stamp Act (II of 1899) has the deed of partnership dated the 12th February, 1933, brought into existence a genuine firm entitled to registration under the provisions of section 26A of the Act.

When a document purporting to be an instrument of partnership is tendered under section 26A on behalf of a firm and application is made for registration of the firm as constituted under such instrument, a question may arise whether the instrument is intended by the parties to have real effect as governing their rights and liabilities *inter se* in relation to the business or whether it has been executed by way of pretence in order to escape liability for tax and without intention that its provisions should in truth have effect as defining the rights of the parties as between themselves. To decide that an instrument is in this sense not genuine is to come to a finding of fact: whether there was evidence upon which it was open to the Income-tax authority to come to such a decision is a question of law. Their Lordships do not understand that this is the question of law which the Commissioner by the case stated has intended to refer nor do they gather that he has arrived at any such finding of fact. The Commissioner has given an elaborate account of the returns, contentions and correspondence connected with the assessments made upon the profits of this factory since the year 1918. But the substance of the case stated by him comes in the end to this, that the factory has until recently belonged to the joint family and has been assessed as such; that the members of the family now purport to have carried out an oral " partition " of this particular asset; and have executed the partnership agreement of 12th February, 1933. As to this, the assessees make an alternative case. *First*, that the factory was the father's self-acquired property and he can alienate it as he likes. Assuming that to be correct, the Commissioner says, no question of " partition " arises, but the alienation of immoveable property can only be made by a proper deed of transfer as required by the Transfer of Property Act. *Secondly*, the assessees say in the alternative that the property was joint family property; that no written instrument is necessary for a partition of joint property; and that the transaction in this case was a partition at the hands of the father. To this the Commissioner replies that the shares allotted to the members were not the shares to which they were entitled on partition: hence " the alleged transaction is not a partition in law." In this way, without deciding whether the factory was self-acquired or joint family property and without coming to any findings of fact as to the father's powers under the customary law, the Commissioner concludes that the question propounded by him should be answered in the negative. His reason is that " the sugar factory continues to occupy the same position and status in the eyes of the law as it had before and the steps taken by the assessees to bring about a change are not legally admissible."

The High Court in their judgment of 9th March, 1938, proceed as the Commissioner had done hypothetically—on the hypothesis of self-acquisition and then on the hypothesis of joint family property. The first contention of the assessees was that no immoveable property had been alienated or divided by the father, the shares of the wife and sons being shares in the machinery and other moveables belonging to the business, but not in the factory buildings or the land on which these stood. It was emphasised that in the partnership agreement of 12th February, 1933, there is no mention of buildings—a contention which has been repeated before the Board. Their Lordships agree with the High Court in rejecting this construction of the agreement. It contains no reference to any stipulation for a tenancy of any kind or for leave and license on any terms. The land and buildings and the right to use them were essential constituents of the factory, and though the agreement does not purport to be itself the transfer of any property or interest from the father to the other members it does purport to express the terms on which the parties after such transfer had agreed to carry on business as a firm. Their Lordships think that it was an essential feature of the partnership agreement as expressed in the instrument of 12th February, 1933, that the wife and sons had a share in the immoveables.

On this view the High Court had no difficulty in agreeing with the conclusion arrived at by the Commissioner on the hypothesis that these immoveables were self-acquisitions of the father. On the hypothesis that they were joint family property, however, they were bound to disagree with his view that the alleged transaction could not be a partition because the shares were not in accordance with the parties' legal rights. Indeed this argument was not maintained before the High Court, but an argument based on section 25A of the Act was put forward instead on the Commissioner's behalf. The High Court accepted this new contention and was thus prepared to answer the question referred to in the negative on the hypothesis of joint family property as well as on that of self-acquisition by the father. The new contention has been maintained before their Lordships and must now be examined.

Subsections (1) and (2) of section 25A were introduced into the Act by Act III of 1928 and subsection (3) by Act XXII of 1930:

> 25A. (1) Where, at the time of making an assessment under Section 23 it is claimed by or on behalf of any member of a Hindu family hitherto assessed as undivided that a partition has taken place among the members of such family, the Income-tax Officer shall make such inquiry thereinto as he may think fit, and if he is satisfied that a separation of the members of the family has taken place and that the joint family property has been partitioned among the various members or groups of members in definite portions he shall record an order to that effect:
>
> Provided that no such order shall be recorded until notices of the inquiry have been served on all the members of the family.
>
> (2) Where such an order has been passed, the Income-tax Officer shall make an assessment of the total income received by or on behalf of the joint family as such, as if no separation or partition had taken place, and each member or group of members shall in addition to any income-tax for which he or it may be separately liable and notwithstanding anything contained in subsection (1) of section 14 be liable for a share of the tax on the income so assessed according to the portion of the joint family property allotted to him or it;
>
> And the Income-tax Officer shall make assessments accordingly on the various members and groups of members in accordance with the provisions of section 23:
>
> Provided that all the separated members and groups of members shall be liable jointly and severally for the tax assessed on the total income received by or on behalf of the joint family as such.
>
> (3) Where such an order has not been passed in respect of a Hindu family hitherto assessed as undivided, such family shall be deemed, for the purposes of this Act, to continue to be a Hindu undivided family.

On this section the contention of the Commissioner is that for the purposes of the Income-tax Act members of an undivided Hindu family cannot enter into a partnership in respect of a portion of the joint property which they have partitioned among themselves. But in their Lordships' view section 25A contains no warrant for any such prohibition. It has no reference at all to any case in which the Hindu undivided family remains in existence at the time of assessment. No difficulty whatever in the assessment of a Hindu undivided family is caused—or was ever thought to be caused—by the facts that in one year it has certain assets and certain income therefrom and that in the next year it is found to have parted with one asset and to be no longer in receipt of the same income. The same assessee has a different income in each year—that is all. It matters nothing whether the particular asset no longer possessed by the undivided family has become the separate property of a member or belongs to a stranger. Section 25A is directed to the difficulty which arose when an undivided family had received income in the year of account but was no longer in existence as such at the time of assessment. The difficulty was the more acute by reason of the provision—an important principle of the Act—contained in section 14 (1): "The tax shall not be payable by an assessee in respect of any sum which he receives as a member of a Hindu undivided family."

Section 25A deals with the difficulty in two ways, which are explained by the rule, applicable to families governed by the Mitakshara, that by a mere claim of partition a division of interest may be effected among coparceners so as to disrupt the family and put an end to all right of succession by survivorship. It is trite law that the filing of a suit for partition may have this effect though it may take years before the shares of the various parties are determined or partition made by metes and bounds.

Meanwhile the family property will belong to the members as it does in a Dayabhaga family—in effect as tenants in common. Section 25A provides that if it be found that the family property has been partitioned in definite portions, assessment may be made, notwithstanding section 14 (1), on each individual or group in respect of his or its share of the profits made by the undivided family, while holding all the members jointly and severally liable for the total tax. If, however, though the joint Hindu family has come to an end it be found that its property has not been partitioned in definite portions, then the family is to be deemed to continue—that is to be an existent Hindu family upon which assessment can be made on its gains of the previous year.

With all respect to the learned judges of the High Court they appear to have mistaken the effect of the previous decision of that Court with which they express agreement. *Biradhmal Lodha* v. *Commissioner of Income-tax* (1933) I.L.R. 56 All. 504. The section has nothing to say about any Hindu undivided family which continues in existence, never having been disrupted. Such a case is outside sub-section (3) because it is not within the section at all. No subsection is required to enable an undivided family which has never been broken up to be deemed to continue. But it need not have the same assets or the same income in each year and it can part with an item of its property to its individual members if it takes the proper steps.

The result is that the reasons given by the High Court do not justify a negative answer to the question referred. If the steps taken to vest in the wife and sons an interest in the immoveable assets of the business were not legally effective, e.g., for want of a registered instrument of transfer, the negative answer would in their Lordships' view be right, since the wife and sons could not compel the father to perfect a voluntary transfer. But on the assumption that the factory land and buildings were joint family property it has not been shown that a partition at the hands of the father could not be effected without a written instrument. To answer the question of law which has been propounded by the Commissioner it is necessary to descend from the realm of hypotheses to the region of fact. The Commissioner has taken pains to state some matters very fully, but he has not found the material facts as he should have done. It is necessary to know as regards (*a*) the business, machinery, plant and other moveables; (*b*) the factory buildings and land whether they were before 1931 the self-acquired property of the father or his ancestral property or joint family property or whether they fall into some other and what category according to the customary law. It is necessary that the customary law of the family should be found as a fact so as to show what right if any the father had to partition or transfer the moveable or immoveable property above-mentioned, to whatever category it may be found to belong in whole or in part. The *rivaj-i-am* is evidence of the custom but it is not conclusive and a finding as to custom is required. When the rights of the members of the family have been ascertained, it will be necessary to ascertain whether in fact the father did at any time purport to give shares or interests in any of the above-mentioned property to his wife and sons. If so at what time? What shares did he give? In what manner? In what property? Did he purport to be alienating his own property or effecting a partition of family property or how otherwise? Again, what agreement if any was made prior to the 12th February, 1933, and when as to a partnership being constituted to carry on the sugar factory and as to the assets which it was to have as a firm? None of these essential facts have been found and stated by the Commissioner, with the result that the question referred cannot be answered until the High Court has exercised its powers under subsection 4 of section 66 of the Act. Their Lordships leave it to the discretion of the High Court to specify the particular additions and alterations which the Commissioner should be directed to make.

They will humbly advise His Majesty that the judgment and decree of the High Court be discharged and the case remanded to the High Court for disposal after taking such action under subsection 4 of section 66 of the Indian Income-tax Act, 1922, as the High Court may think fit in the light of this judgment. The respondent will pay the appellants' costs of this appeal. The costs already incurred in the High Court will abide the order of the High Court at the final disposal of the reference.

(10376) Wt. 8026—151 170 6/42 D.L. G. 338

In The Privy Council

DR. SARDAR BAHADUR SIR SUNDER SINGH MAJITHIA (since deceased)

v.

THE COMMISSIONER OF INCOME-TAX, UNITED AND CENTRAL PROVINCES

DELIVERED BY SIR GEORGE RANKIN

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