

to whether the power was properly exercised or not or whether its decision was correct and valid is a question that does not arise on this reference. The notice of motion is therefore dismissed with costs.

The assessee must pay the costs of the reference.

Attorneys for Applicants: *Daphtary Ferreira & Divan.*

Attorney for Respondent: *N. K. Petigara.*

Answer accordingly.

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INCOME-TAX REFERENCE

Before Mr. M. C. Chagla, Chief Justice and Mr. Justice Tendolkar.

BHOGILAL LAHERCHAND, APPLICANT *v.* THE COMMISSIONER OF INCOME-TAX, BOMBAY CITY-I, BOMBAY, RESPONDENT.*

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Indian Income-Tax Act (XI of 1922), s. 16 (3) (a) (ii)—Minor admitted to benefits of partnership between father and son—Accounts of such partnership made on Diwali every year—Minor attaining majority during middle of year and electing to continue as partner—Death of such minor thereafter—Whether Taxing Department entitled to include in father's income minor's share of profits as computed upto date of majority?

B. and his major son P. carried on business in partnership to the benefits of which B.'s minor sons A. and M. were admitted. The accounts of such partnership were made on the Diwali every year. A. attained majority on August 22, 1950 and on his electing to remain a partner of the firm a deed of partnership was executed between B. P. A. and M. on August 26, 1950. A died on August 31, 1950 in an Air-crash. The Income-Tax Department calculated the proportionate profits in the partnership coming to the share of A. as of August 22, 1950 at Rs. 2,49,459 and included such sum in the assessment of his father B. under s. 16 (3) of the Indian Income-Tax Act, 1922. The Income-Tax Appellate Tribunal confirmed the order passed by the Department. On the question whether the Department was entitled to include such sum in B.'s total income for the assessment year,

Held, that the profits or the losses of the partnership from the commercial point of view could only be ascertained when the accounts of the partnership are made up on the Diwali of each year and it would be impossible to predicate of this partnership that it had made any profit or any loss on any day prior to the Diwali of the particular year. Moreover, the only right which A. acquired on his election to continue as a partner was to receive his share of profits not as of date on which he attained majority but when the accounts were made up at Diwali or whenever partnership came to an end on dissolution or by operation of law, e. g. death.

Held, further, that before any income could be deemed to be the income of the father under s. 16 (3) of the Act, it must in the first place be the income of the minor.

Held, therefore, that the sum of Rs. 2,49,459 could not be included in the income of the father as A. himself had acquired no right to receive that amount on the date on which he attained majority.

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E. D. Sassoon Company Limited v. Commissioner of Income-Tax,⁽¹⁾ followed.

The following question was referred to the High Court at Bombay—

“Whether the sum of Rs. 2,49,459 could legally be included in the assessee’s total income of S. Y. 2006 liable to be assessed in the assessment year 1951-52?

N. A. Palkhivala, for the Applicant.

M. P. Amin, Advocate General with *G. N. Joshi*, for the Respondent.

Chagla C. J.—An interesting question arises on this reference as to the liability of the father to pay tax on the income of his minor son. The question might have presented some difficulty but for the fact that the recent decision of the Supreme Court really makes it almost impossible to come to any other conclusion than the one to which we have arrived.

The facts are that one Bhogilal had three sons—Pratap, Arvind and Mahesh. Bhogilal started a partnership with his three sons under a deed of partnership, dated April 14, 1943. At that date Pratap was a major and Arvind and Mahesh were minors and therefore Arvind and Mahesh were admitted to the benefits of the partnership. Arvind attained majority on August 22, 1950. He elected to continue to remain a partner of this firm and a fresh partnership deed was executed between Bhogilal the father and Pratap, Arvind and Mahesh on August 28, 1950. Arvind died on August 31, 1950. The year of account of Bhogilal who is the assessee as an individual before us is Samvat Year 2006 and the profits which were ascertained on August 31, 1950 as coming to the share of Arvind was Rs. 2,64,450 and the Income Tax Department calculated the proportionate profits coming to the share of Arvind on this basis as of the 22, August 1950 when he attained majority at Rs. 2,49,459, and the contention of the Department was that this sum of Rs. 2,49,459 constituted the income of Arvind as a minor and under s. 16(3) of the Income Tax Act this sum must be included in the assessment of Bhogilal the father and Bhogilal must pay tax on this amount. The Tribunal held in favour of the Department and Bhogilal has now come before us on this reference.

Under section 16(1)(c) certain income is deemed to be the income of an assessee. The income which the department is seeking to tax in the hands of Bhogilal is not his own income; it is the income of his minor son; but by reason of s. 16(3) that income in the eye of the law is looked upon as income of the father and the father is liable to pay the tax. But before the income can be looked upon as income of the father, it must be obviously in the first place the income of the minor. It is only if we are satisfied that the amount claimed by the

1. [1954] 26 I. T. R. 27 (S. C.).

Department was the income of Arvind in the year of account that the question would arise whether it is properly assessed to tax under s. 16(3). The relevant provisions of the section are that in computing the total income of any individual for the purpose of assessment, there shall be included so much of the income of a minor child of such individual as arises directly or indirectly from the admission of the minor to the benefits of partnership in a firm of which such individual is a partner. Therefore, the conditions which have got to be satisfied before this income is included in the total income of an assessee are that in the first place the assessee must be a partner in a firm and that his minor son must be admitted to the benefits of that partnership, and further the income which is sought to be included in the total income of the assessee must arise directly or indirectly from the fact of the minor being admitted to the benefits of the partnership.

The real question that has to be decided on this reference is, what is the proper meaning that should be given to the expression used in this sub-section, viz., as arises directly or indirectly. Two views are possible. It may be suggested that although the sum of Rs. 2,64,450 was computed as the share of Arvind on the dissolution of the partnership when he died on August 31, 1950, it is possible to apportion that income between the period when Arvind was a minor and the period after he ceased to be a minor. It may be said that this sum of Rs. 2,64,450 is a composite amount consisting of profits earned at different stages of the partnership. If this were the proper view, then the Department could conceivably urge that inasmuch as Rs. 2,49,459 was earned by Arvind upto August 22, 1950, that was the income of Arvind earned by him while he was a minor and therefore that income must be included in the total income of his father under s. 16(3). The other view, which as we shall presently point out is the correct view and which has now been pronounced to be the correct view by the Supreme Court, is that what we have to consider is whether in the year of account the minor had any right to receive any income from his being admitted to the benefits of the partnership. It is not enough that he should earn any income in rather a loose sense of that expression. He must have acquired a right to receive the particular income in the year of account which is being included in the total income of his father. Therefore, when the Department includes Rs. 2,49,459 in the total income of the assessee, the question that must be asked and answered is, did Arvind have the right to receive this amount from the partnership at any time in the year of account, and there can be no doubt that in law the minor never had the right to receive this amount from the partnership.

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Let us look at what the position in law is with regard to a minor who has been admitted to the benefits of a partnership and who attains majority. It is a common place that a minor can never become a partner but he can be admitted to the benefits of a partnership, and s. 30 of the Partnership Act regulates the rights of a minor who has been admitted to the benefits of a partnership, and broadly speaking the rights of a minor are, when he attains majority, that he has the option either to retire from the partnership or to continue in the partnership and a *locus poenitentiae* of six months is given to him to make up his mind. If he elects to continue as a partner then the partnership does not come to an end, the partnership continues, and sub-s. (7)(a) of s. 30 expressly provides that his rights and liabilities as a minor continue up to the date on which he becomes a partner but he also becomes personally liable to third parties for all acts of the firm done since he was admitted to the benefits of the partnership. On the other hand, if he elects not to become a partner, then he is entitled to claim whatever amount was due to him as computed at the date when he gives the public notice provided in sub-s. (5) of s. 30. Further, his share is not to be liable for any acts of the firm done after the date of the notice and he also becomes entitled to sue the partners for his share of the property and profits in accordance with sub-s. (4) which gives certain rights to the minor to sue the partners for an account of payment of the share of the minor when the minor serves his connection with the partnership. Therefore it is clear that if a minor on attaining majority elects to continue as a partner, the partnership does not come to an end, the partnership continues, and the minor having become a partner he is entitled to his profits as computed at the end of the year regulated by the partnership deed. On the other hand, if the minor elects not to be a partner, it is equally clear that he severs all his connection with the partnership and he becomes entitled to whatever amount is due to him at the date when he makes the election not to become a partner. Therefore, whereas in the first case there is no break in the continuity of the partnership and there is no need to make up any accounts otherwise than in the ordinary course, in the latter case there is a break in the partnership and accounts have to be made up as of a particular date because the minor who has become a major has the right to claim a specific amount as due to him on a particular date.

It is important to note that under both the partnership deeds, the partnership deed of April 14, 1943, and the partnership deed of August 28, 1950, it is specifically provided that on the Divali in the each year during the continuance of the partnership, accounts will be taken of all the assets and liabilities for the

time being of the partnership and a balance-sheet and profit and loss account is to be made up on a certain basis. Therefore the profits or the losses of this partnership from the commercial point of view can only be ascertained on the Divali of each year, and it would be impossible to predicate of this partnership that it had made any profit or any loss on any day preceding or prior to the Divali of a particular year. Of course, a partnership may come to an end by operation of law; a partner may die or a partner may retire, in which case the law provides that accounts would have to be made up on that particular day irrespective of the provision in the partnership deed for making up the accounts in the ordinary course. In the case of the minor also the law provides that by operation of law accounts would have to be made up on a particular day if the minor elects not to be a partner. But the law does not provide that there is any break in the partnership or there is a discontinuance of the partnership if the minor attaining the majority elects to continue as a partner.

The simple question, therefore, that we have to consider is whether in the circumstances of this case Arvind could ever have claimed from the partnership the sum of Rs. 2,49,459. As soon as the partnership deed of August 28, 1950, was executed and he elected to continue as a partner, the only right that Arvind had was to receive his share in the profits when the accounts were made up at Divali. He had no right to receive the profits that may have arisen when he attained majority on August 22, 1950. Let us look at this matter from a different point of view. In this case, as it so happens, Arvind unfortunately died, but assuming he had lived and the partnership had gone on working till the Divali of Samvat Year 2006 and assuming the partnership had made a loss, then Arvind's share of the loss would have been debited to him. The extraordinary claim of the Department is that although the partnership might result in a loss, although in fact Arvind as a partner may have debited to him his share of the loss, yet Arvind's father must pay tax on profits of the partnership which profits have been ascertained by computing them as of a particular date. As we said before, it is entirely fallacious to contend that it could ever be said of a partnership that there were profits in that partnership on any particular day. On the facts of this case the date August 22, 1950, has no particular charm or magic. Arvind may have attained majority on that date, but what we have to consider is what Arvind did after he attained majority and unless he exercised his option to get out of the partnership, it could not be said that on August 22, 1950, the partnership had either made profits or losses.

The Advocate General says that s. 16 is based on a fiction. It undoubtedly is, but the fiction is that the income of the

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minor becomes the income of his father. But the Advocate General wants to add a second fiction to the fiction already embodied in s. 16(3) and the second fiction is that although a certain amount is not the income of the minor still you must look upon it as his income and make the father pay tax on that income. We refuse to countenance the attempt on the part of the Department to add to a second fiction to the fiction contained in s. 16(3) which is sufficiently burdensome upon the assessee who happens to be the father.

Whatever view was possible to be taken with regard to the theory of apportionment between profits earned upto a particular date and profits earned subsequently, the decision of the Supreme Court in *E. D. Sassoon Company Ltd. v. Commissioner of Income-tax*,⁽²⁾ makes it impossible to take any other view of this case than the one we are suggesting to be the correct one. In that case we had held that when a managing agency is assigned by the managing agents, then the income earned by the assignor for the period during which they acted as managing agents should be apportioned with the income earned by the assignees during the period that the assignees acted as managing agents. In other words, we refused the attempt of the Department to tax the whole of the managing agents' income in the hands of the assignees because the income had accrued at the end of the relevant year at which date the managing agents happened to be the assignees and not the assignors. This decision of ours was found by the Supreme Court not to be a correct decision and the Supreme Court held that the managing agency commission could not be apportioned between the assignor and the assignee, that the commission had accrued to the assignee, and the assignee must pay tax on the whole of the commission. There are some very important passages in the judgment of Mr. Justice Bhagwati which have a direct bearing on the facts of this case. At page 51 the learned Judge says :

"It is clear therefore that income may accrue to an assessee without the actual receipt of the same. If the assessee acquires a right to receive the income, the income can be said to have accrued to him though it may be received later on its being ascertained. The basic conception is that he must have acquired a right to receive the income. There must be a debt owed to him by somebody. There must be as is otherwise expressed *debitum in praesenti, solvendum in futuro*. Unless and until there is created in favour of the assessee a debt due by somebody it cannot be said that he has acquired a right to receive the income or that income has accrued to him."

Applying this test, it is impossible to suggest that any debt, to use the language of Mr. Justice Bhagwati, was created in favour of Arvind at the time. Nor could it be said that the

sum of Rs. 2,49,459 was a debt due at any time by the partnership to Arvind. Again at p. 52 the learned Judge says :

"A debt must have come into existence and he must have acquired a right to receive the payment. Unless and until his contribution or parenthood is effective in bringing into existence a debt or a right to receive the payment or in other words a *debitum in praesenti, solvendum in futuro* it cannot be said that any income has accrued to him. The mere expression "earned" in the sense of rendering the service etc. by itself is of no avail."

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The only debt that came into existence and with regard to which Arvind or rather his estate acquired a right to receive the payment was a debt which could only be ascertained on making up the accounts of the partnership as of August 31, 1950. The position is made even clearer by the learned Judge at page 55 :

"What has however got to be determined is whether the income, profits or gains accrued to the assessee and in order that the same may accrue to him it is necessary that he must have acquired a right to receive the same or that a right to the income, profits or gains has become vested in him though its valuation may be postponed or though its materialisation may depend on the contingency that the making up of the accounts would show income, profits or gains."

Therefore, the Advocate General would be right that the mere fact that computation could not be made on August 22, 1950 and it could be made only later will not necessarily militate against the position that Arvind had acquired the right to receive the amount on August 22, 1950. But if he had no right to receive the amount at all, the mere computation will not create a right which did not exist.

Therefore, in our opinion, the Tribunal was in error when it took the view that the sum of Rs. 2,49,459 represented profits of the partnership to which Arvind as a minor was entitled. If the Tribunal was in error in taking that view, then clearly this amount could not be included in the assessee's total income of Samvat Year 2006.

We must therefore answer the question submitted to us in the negative. Commissioner to pay the costs.

Attorneys for Applicant : *Daphtary Ferreira & Diwan.*

Attorneys for Respondent : *N. K. Petigara.*

Answer accordingly.

P. M. P.