

JUGAL KISHORE BALDEO SAHAI

v.

COMMISSIONER OF INCOME-TAX, U.P., LUCKNOW

September 20, 1966

[J. C. SHAH AND V. BHARGAVA, JJ.]

Income tax Act (11 of 1922), s. 10(2)(xv)—Assessee, a Hindu joint family firm—Payment of remuneration to karta for managing business—If a deductible item of expenditure.

The assessee was a Hindu undivided family carrying on a joint family business and was also deriving some income from partnerships, in which its karta, representing the family, was a partner. The family consisted of two brothers and their minor sons. One of the brothers, who was the karta, asked the other for a salary of Rs. 1,000 per month, since he was managing the business. The other brother agreed to it, and the payments were made. The assessee claimed that the sum of Rs. 12,000 per year, paid as remuneration to the karta should be deducted as an item of expenditure under s. 10(2)(xv) of the Income-tax Act, 1922. The claim was rejected by the Department, the Tribunal and the High Court.

In appeal to this Court,

HELD : As the remuneration was paid under a valid agreement which was *bona fide* and in the interest of, and expedient for, the business of the family, and the payment was genuine and not excessive and was not a device to escape income-tax, the remuneration must be held to be an expenditure laid out wholly and exclusively for the purpose of the business of the family and must be allowed as an expenditure under the section. [421 B-C, D]

The karta of a family can be paid remuneration for carrying on family business, provided it is under some valid agreement. The test of the validity of such an agreement, when entered into on behalf of a minor, is that it should be for the benefit of the minor. The agreement in the instant case was entered into between the two adult members. Their minor sons were represented by them or by the karta and the agreement was not prejudicial to the minors' interests. In fact, it was acquiesced in by those minors who had later become majors. If the agreement was in the interests of the family it would not be invalid, when executed on behalf of the minors by the person authorised to act on their behalf, simply because the minors were represented by a person who received some benefit under the agreement. Further, the remuneration was not intended to cover any service rendered by the karta to the partnership firms, but was for looking after the interests of the family in those businesses and for managing the affairs of the family. [419 H; 420 B-C, D-H; 421 D-E, 422 E-F]

Jitmal Bhuramal v. Commissioner of Income-tax, Bihar and Orissa, (1962) 44 I.T.R. 887 (S.C.), explained and followed.

CIVIL APPELLATE JURISDICTION : Civil Appeal Nos. 594 to 600 of 1965.

Appeals by special leave from the judgment and order dated March 28, 1962 of the Allahabad High Court in I. T. Misc. Cas^e No. 424 of 1959.

A *A. K. Sen, T. A. Ramachandran, J. B. Dadachanji*, for the appellants (in all the appeals).

S. T. Desai, Gopal Singh and R. N. Sachthey, for the respondent (in all the appeals).

B The Judgment of the Court was delivered by

Bhargava, J. These appeals by special leave are directed against the judgment of the Allahabad High Court returning an answer to the following question referred to it by the Income-tax Appellate Tribunal:

C “Whether on the facts and circumstances of the case the salary paid or credited to a Karta of the family for looking after the family’s business was a permissible deduction under s. 10(2)(xv) in computing the income of the family business.”

D The assessee was a Hindu undivided family carrying on a joint family business of commission agency in cloth under the name of Jugal Kishore Baldeo Sahai and was, in addition, deriving income from some property and from some partnership business in which the karta Babu Ram was a partner representing the interest of the Hindu undivided family. The family consisted of Babu Ram, his brother Gobardhandas and their sons. In June, 1946, the karta Babu Ram wrote a letter to his brother Gobardhandas, who was the only other adult member of the family, stating that, since he was managing all the business, he ought to get a salary of Rs. 1,000 per month. Gobardhandas promptly agreed to this proposal and consequently in the account books of the family for the year in question a sum of Rs. 12,000 was debited in the expense account of the Hindu undivided family business, viz., of Jugal Kishore Baldeo Sahai and the same amount was credited in the name of Babu Ram as an individual. The first such credit was made in the account year relevant to the assessment year 1946-47 and similar credits continued to be made in subsequent accounting years upto the year relevant to the assessment year 1952-53. Thus, the debit against the Hindu family business at the rate of Rs. 12,000 per year and similar credit in the name of Babu Ram was made in the accounts for seven years. In each of these seven years the Hindu undivided family as the assessee claimed that this sum of Rs. 12,000 every year should be deducted as an expenditure under s. 10 (2) (xv) of the Income-tax Act. The Income-tax Officer rejected the claim and that order was upheld by the Appellate Assistant Commissioner as well as by the Tribunal. Thereupon, at the request of the assessee appellant, the question reproduced by us was referred by the Tribunal for the opinion of the High Court. The High Court answered the question against the

appellant and upheld the view of the Tribunal. Consequently, these appeals have been brought up before us. A

The High Court has taken the view that under the Hindu Law, a karta is bound by reason of his being the karta to manage all the business of the family without being entitled to any remuneration for the service of management. It went on to comment that indeed, when under the law a karta represents the family, it would be anomalous to think of a karta as being an employee of himself or being entitled to remuneration for acting as such and receiving payment from his ownself. This view was expressed by the High Court on the basis of its opinion about the rights and duties of a karta of a Hindu undivided family under the Hindu Law and to arrive at this view, the Court relied on a comment in Gopalchandra Sarkar Sastri's Hindu Law, 1940 Edn., N. E. Raghavachariar's Hindu Law, 4th Edn., and Mayne's Hindu Law, 11th Edn., and in addition, on a decision of the Madras High Court in *Krishnaswami Ayyangar v. Rajagopala Ayyangar*.⁽¹⁾ It was on the basis of these comments in the books of Hindu Law that the Allahabad High Court held the view that Babu Ram, being the karta of the family, was not entitled to draw any remuneration for carrying on the business of the Hindu undivided family. B

The decision of the Madras High Court and the views expressed by these commentators do not show that a Karta of a Hindu undivided family is not entitled to charge for services rendered to the family business under any circumstances at all. The right to receive remuneration is negated with some qualifications. Either it is stated that no remuneration is payable except under special arrangement, or a scope for payment is recognised by saying that the manager or karta is not "ordinarily" entitled to remuneration. The Madras High Court in the case of *Krishnaswami Ayyangar v. Rajagopala Ayyangar*⁽¹⁾ held that "the managing coparcener was not entitled to special remuneration in the absence of a valid special agreement". We are unable to understand the meaning of the expression "valid special agreement". It is, of course, necessary that before a karta receives remuneration, it should be under a valid agreement. In judging what is a valid or proper agreement which would justify the payment of remuneration paid to a karta of the Hindu undivided family for managing the business of the family to be deductible as an expenditure under s. 10 (2) (xv) of the Income-tax Act, the test, we think, which should be applied, is whether the agreement has been made by or on behalf of all the members of the Hindu undivided family and whether it was in the interest of the business of the family, so that it could be justified on grounds of commercial expediency. That is the test which has always to be applied when considering whether a particular C

(1) I.L.R. 18 Mad. 73 D

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A expenditure claimed as a deduction under s. 10 (2) (xv) of the Income-tax Act has been incurred wholly and exclusively for the purpose of the business.

B This Court in *Jitmal Bhuramal v. Commissioner of Income-Tax, Bihar and Orissa* (1) has already held that "a Hindu undivided family can be allowed to deduct salary paid to a member of the family, if the payment is made as a matter of commercial or business expediency". Mr. S. T. Desai, learned counsel appearing for the department tried to distinguish that case on the ground that in that case the salaries which were held to be deductible were paid to junior member of the family and not to the karta. The view expressed by this Court was in general terms and did not make any distinction between a junior member of the family or a karta. The principle was laid down by this Court without any such distinction even though the Court was then concerned with salaries which had been paid to junior members of the family.

D We do not consider that the decision given by this Court in that case needs to be given a narrow interpretation so as to confine the right of deducting the remuneration paid by a Hindu undivided family to junior members only. There seems to be no reason at all why if a karta is paid remuneration he should be in a position different from that of any junior member. It is true that a karta has a right to manage the property of the Hindu undivided family on behalf of all the coparceners but there is no obligation or duty on him to carry on a particular business of the family. It is well-established that any member of a Hindu undivided family including a karta can have a separate personal source of income if that income is earned independently of the Hindu undivided family assets or business. It is primarily on this basis that it has been held that salary or remuneration paid to the junior member of the family for services rendered to the family business becomes his separate income and consequently a deductible expenditure under s. 10(2) (xv) of the Act when computing the income of the family. In similar circumstances, if a karta offers his services to the family instead of choosing an independent career to earn his separate income and receives remuneration from the family, there is no reason why the remuneration so paid to him cannot be treated as an expenditure for carrying on the business of the family and consequently expended wholly and exclusively for the purpose of the business and deductible under s. 10 (2) (xv) of the Act.

H As we have already indicated above, the general view expressed by commentators on Hindu Law as well as in decided cases is that even the karta of a family can be paid remuneration for carrying on family business, provided it is under some agreement. There seems to be no reason why, if all persons competent in a Hindu

(1) 44 I.T.R. 887.

undivided family to enter into an agreement on its behalf consider it appropriate that the karta should be paid remuneration and enter into an agreement to pay remuneration to him, that remuneration should not be held to be an expenditure incurred in the interest of the family, and consequently an expenditure deductible under s. 10 (2) (xv) of the Act. In the present case, Babu Ram received remuneration when he and his brother Gobardhandas agreed that such remuneration should be payable. The other members of the Hindu undivided family were minor sons of Babu Ram himself or of Gobardhandas. Babu Ram and Gobardhandas, being the only two members of the family competent to act on behalf of the family including the minors, entered into this agreement, obviously because it was considered in the interest of the family that Babu Ram should receive this payment. We are not at all impressed by the argument urged on behalf of the department that, since some of the coparceners were minors, no valid agreement at all on their behalf could have been entered into by Babu Ram or Gobardhandas so as to allow payment of remuneration to the karta, Babu Ram. The minor sons of Babu Ram could certainly be represented by himself and the minor sons of Gobardhandas could either be represented by him, being his sons, or, in the alternative, Babu Ram could represent them in the agreement as the karta of the family to which they belonged. It is true that under the agreement, some payment was to be made out of the income of the family to Babu Ram so as to become his separate property. But that circumstance would not, in our opinion, invalidate the agreement merely because Babu Ram represented some of the minors on whose behalf the agreement was made. If the agreement is held to be in the interest of the family, the agreement would not be invalidated when executed on behalf of the minors by the person authorised to act on their behalf simply because the minors happened to be represented by a person who receives some benefit under the agreement. The test of the validity of an agreement on behalf of a minor is that it should be for the benefit of the minor, and in this case, there is no finding that the agreement entered into on behalf of the Hindu undivided family including the minors by Babu Ram and Gobardhandas was in any way prejudicial to the interests of the minor members. On the other hand, the facts found show that some of the minors subsequently attained majority and none of them challenged the validity of this agreement on the ground that it had been executed during their minority and that it was against their interest. In fact, it was found that subsequently, when there was a partition in which even the sons of Babu Ram separated from him, the amount to the credit of Babu Ram in the accounts was treated as his separate asset and was not included in the assets of the Hindu undivided family without any objection from any of the members of the family who were minors at the earlier stage when the agreement

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A was entered into. Consequently, we are unable to hold that the agreement, by which Babu Ram was allowed this remuneration of Rs. 1,000 p.m., was in any way vitiated, and, as we have already held above, it was an agreement executed in the interest of the family.

B In our view, if a remuneration is paid to the karta of the family under a valid agreement which is *bonafide* and in the interest of, and expedient for, the business of the family and the payment is genuine and not excessive, such remuneration must be held to be an expenditure laid out wholly and exclusively for the purpose of the business of the family and must be allowed as an expenditure under s. 10(2) (xv) of the Act.

C In this connection, we may take notice of a decision in the Patna case, *Commissioner of Income-tax, Bihar and Orissa v. Jainarain Jagannath*,⁽¹⁾ wherein also it was held that "a member of a joint Hindu family might conceivably do business in his individual capacity and in that capacity might render services to the joint family trading firm in consideration of which the firm might pay him such remuneration as it would pay to an outsider. If such remuneration is not excessive and is reasonable and is not a device to escape income-tax, then it will be a legitimate deduction in computing the profits of the business. If, on the other hand, the amount paid is unreasonably high and disproportionate to the services rendered by him, then it may be treated as part of the profits of the firm distributed in a particular manner. In the present case, there is no indication of any finding that the payment to Babu Ram was at all high, or was not commensurate with the services rendered by him.

F An alternative ground, on which Mr. Desai on behalf of the department challenged this deduction under s. 10(2) (xv), was that the remuneration was being paid to Babu Ram not only to manage the Hindu undivided family business carried on under the name of Jugal Kishore Baldeo Sahai, but also for other businesses, including those of the partnership firms in which Babu Ram was a partner in his own name, though representing the Hindu undivided family. In support of this proposition, learned counsel relied on the decision of the Calcutta High Court in *Jitmal Bhuramal v. Commissioner of Income-Tax, Bihar & Orissa*,⁽²⁾ which judgment was affirmed by this Court as reported in *Jitmal Bhuramal v. Commissioner of Income-tax, Bihar & Orissa*.⁽³⁾ In that case, there was a finding of fact that two junior members of the Hindu undivided family, Gulzarilal and Madanlal, were employed in the partnership business in which the Karta of the family was a partner and had rendered services to that business. This Court, while recognising the principle that

(1) 13 I.T.R. 410.

(2) 37 I.T.R. 528.

(3) 44 I.T.R. 887.

“a Hindu undivided family is allowed to deduct salaries paid to members of the family, if the payment is made as a matter of commercial or business expediency”, laid down the exception that the services rendered must be to the family. It was held that, since the services had been rendered not to the family, but to the partnership firm, the remuneration paid to those members was not a legitimate deduction under s. 10(2)(xv) from the income of the Hindu undivided family, and that it could be a valid deduction only when computing the income of the partnership business.

It is true that in the case before us the statement of the case mentions that the agreement for payment of remuneration to Babu Ram was to the effect that he was to get Rs. 1,000 p.m. for looking after the businesses of the Hindu undivided family. It is because of the use of the word “businesses” in the plural that learned counsel urged that the remuneration given to Babu Ram was not merely for looking after the Hindu undivided family business, but also for rendering services to the partnership firms in which Babu Ram was a partner. We do not consider that this interpretation of the agreement is correct. The agreement does not envisage any payment to Babu Ram for services rendered to the partnership firms. The language used was that Babu Ram should receive the remuneration for managing all the businesses of the Hindu undivided family, which can only mean that he was to manage the affairs of the Hindu undivided family firm and also to look after the interests of the Hindu undivided family in other businesses. Thus, the remuneration was not intended to cover any services rendered by him to the partnership firms apart from whatever he was required to do in the capacity of looking after and managing the affairs of the Hindu undivided family. The principle laid down in the case of *Jitmal Bhuramal v. Commissioner of Income-tax, Bihar and Orissa* (1) is, therefore, not applicable to the case before us.

The appeals are consequently allowed. The judgment of the High Court is set aside and the question referred by the Income-tax Appellate Tribunal is answered in the affirmative. The appellant will be entitled to its costs in this Court as well as in the High Court.

V.P.S.

Appeals allowed.