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P. N. KRISHNA IYER

v.

COMMISSIONER OF INCOME-TAX, KERALA

September 3, 1968

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[J. C. SHAH, V. RAMASWAMI AND A. N. GROVER, JJ.]

Indian Income-tax Act, 1922, s. 3 and s. 33B—Hindu undivided family business taken over by company—Karta appointed Governing Director—Salary, Commissioner 'sitting fee' of Governing Director whether assessable in hands of Hindu undivided family—Principles for deciding—Commissioner's powers under s. 33B—Scope of.

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The appellant, on partition of joint family property between himself and his brothers, got as his share the family's motor transport business which had been established by his efforts, along with 'the workshop, stores, agency, cinema companies etc.' The Hindu undivided family consisting of the appellant and his sons transferred the motor transport business to a private limited company; the company credited the account of the family in its books with the value of the assets of the business taken over by it. With family money the appellant purchased 100 shares of the company and was appointed—according to the terms of the Articles of Association—as its Governing Director for life, at a salary of Rs. 3,000 per month with 15% commission on net profits. He was also in lieu of his experience and his services to the business, allotted 4,880 fully paid up shares of the company; the dividend from these, when declared, was credited to the account of the Hindu undivided family. In proceedings for assessment the Income-tax Officer brought to tax in the assessment year 1954-55 the remuneration received by the appellant from the company together with the commission, sitting fee, and income from property business and other sources as the separate income of the appellant. The Appellate Assistant Commissioner modified the order and in carrying out his directions the Income-tax Officer included the income from property business and other sources in the income of the Hindu undivided family and made corresponding modifications in the assessment of the appellant as an individual. But the Commissioner of Income-tax being of the opinion that the order of the Income-tax Officer was prejudicial to the revenue revised the said order under s. 33B of the Income-tax Act, 1922 and included the appellant's income from salary, commission and 'sitting fee' in the total income of the Hindu undivided family. The Tribunal reversed the order of the Commissioner. In reference the High Court upheld the order of the Commissioner. The appellant in his capacity as karta of the family appealed to the Supreme Court and contended:

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(i) that the Commissioner had no power under s. 33B to revise the order of the Income-tax Officer after it had been carried in appeal to the Appellate Assistant Commissioner, nor could he revise an order made by the Income-tax Officer in pursuance of the direction by the Appellate Assistant Commissioner; (ii) that the salary, commission and 'sitting fee' were his individual income and not that of the Hindu Undivided Family.

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HELD: (i) There was no ground for holding that the Commissioner had attempted to revise the order of the Appellate Assistant Commissioner. In computing the income of the appellant as an individual the Appellate Assistant Commissioner had directed certain modifications to be made, and pursuant thereto the assessments of the appellant and of the Hindu undivided family of which the appellant was the karta were rectified.

The order of assessment of the Hindu undivided family was never challenged in appeal. The Commissioner had power to revise the order of the Income-tax Officer which had not been appealed from. [1947 D-F]

Modification in the order of the Income-tax Officer in so far as it related to the assessment of the appellant as an individual was a consequential order made in order to avoid double assessment of the same income. Therefore, the fact that the assessment of the appellant as an individual had become final before the order of the Commissioner did not bar the exercise of the Commissioner's power under s. 33B. [1947 F-G]

(ii) Income received by a member of a Hindu undivided family from a firm or a company in which the funds of the Hindu undivided family are invested, even though the income may be partially traceable to personal exertion of the member, is taxable as the income of the Hindu undivided family, if it is earned by detriment to the family funds or with the aid or assistance of those funds; otherwise it is taxable as the member's separate income. [1949 G]

Case law referred to.

V. D. Dhanwatey v. Commissioner of Income-tax, 68 I.T.R. 365, *M. D. Dhanwatey v. Commissioner of Income-tax*, 68 I.T.R. 285 and *S. RM. C.T. PL. Palainappa Chettiar v. Commissioner of Income-tax*, 68 I.T.R. 221, applied.

In the present case the shares which qualified the appellant to become a member of the company were purchased with the aid of joint family funds. The shares which were allotted to the appellant in lieu of his services were also treated as shares belonging to the joint family. The entire capital assets of the company originally belonged to the joint family and were made available to the company in consideration of a mere promise to pay the amount for which the assets were valued. The income was primarily earned by utilising the joint family assets or funds and the mere fact that in the process of gaining the advantage an element of personal service or skill or labour was involved the character of the income was on that account not altered. In cases of this class the character of the receipt must be determined by reference to its source, its relation to the assets of the family of which the recipient was the member and the primary object with which the benefit received was disbursed. The conclusion of the High Court that the income from salary, commission and 'sitting fee' were the individual income of the appellant was not vitiated by any error. [1950 D-F]

(iii) The question whether the income was the income of the Hindu undivided family or the individual income of the appellant was a finding on a mixed question of law and fact and the final conclusion drawn from the primary evidentiary facts was open to challenge before the High Court on the plea that the relevant principle had been misapplied by the Tribunal. [1950 C]

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 1997 of 1966.

Appeal by special leave from the judgment and order dated June 16, 1965 of the Kerala High Court in Income-tax Referred Case No. 9 of 1964.

S. T. Desai and *R. Thiagarajan*, for the appellant.

- A *D. Narsaraju, T. A. Ramachandran, R. N. Sachthey and B. D. Sharma*, for the respondent.

The Judgment of the Court was delivered by

- B **Shah, J.** P. N. Krishna Iyer—hereinafter called the assessee set up in 1923 a motor transport business in the former State of Travancore. In 1945 there arose disputes between the assessee and his brothers about the division of the estate of the joint family of which they were members. The disputes were settled by mutual agreement dated October 23, 1951 and the motor transport business together with the “workshop, stores, agency, cinema companies etc.” were treated as the business of the joint family, and on partition were allotted to the assessee. An application filed by the assessee before the 1st Additional Income-tax Officer, Trichur, for recording the partition was accepted.

- D In the meantime on July 3, 1952, a private limited company P. S. N. Motors (Private) Ltd. was floated with the object of taking over the motor transport business carried on by the assessee. By the Articles of Association, the assessee was to be the Governing Director of the Company for life and to draw such remuneration and exercise such powers detailed in the agreement to be entered into between him and the company in that behalf, and so long as he held the office of Governing Director, the general management of the company’s business was to remain in his hands. The assessee purchased 100 shares of the Company of the face value of Rs. 100 each. On August 18, 1952, the assessee was appointed by the Company Governing Director with an office allowance of Rs. 3,000 per mensem and a commission of 15 per cent. on the net profit. On the same day the Directors approved the purchase from the Hindu undivided family of the assessee of assets (but not the liabilities) of the transport business valued at Rs. 8,01,074/1/4. In the books of the Company credit entries were posted in the name of the Hindu undivided family. On August 18, 1952, the Directors passed certain resolutions relating to the repayment of the amount due to the Hindu undivided family. On September 28, 1952, the Company passed a special resolution that in consideration of the “valuable services” rendered by the assessee in the promotion of the Company and of the “large sacrifices” made by him in agreeing to place his services at the disposal of the company and the benefit that the company received on account of his “long experience, goodwill and reputation in this line of business,” the assessee be allotted 4880 fully paid up shares of the Company.

- H The Income-tax Officer brought to tax in the assessment year 1954-55 the remuneration received by the assessee from the Company together with the commission, “sitting fee” and income

from property, business and other sources as the separate income of the assessee. The Appellate Assistant Commissioner modified that order, and directed that income other than the income from salary, commission and "sitting fee" received from the Company be included in the assessment of the Hindu undivided family. The Income-tax Officer then carried out the direction and included the income from property, business and other sources in the total income of the Hindu undivided family and made corresponding modifications in the assessment of the assessee as an individual. A B

But the Commissioner of Income-tax being of the opinion that the order passed by the Income-tax Officer was wrong and prejudicial to the interests of revenue revised the order of the Income-tax Officer exercising power under s. 33B of the Income-tax Act, 1922, and included the income from salary, commission and "sitting fee" aggregating to Rs. 43,240 in the total income of the Hindu undivided family. In appeal against the order, the Tribunal reversed the order of the Commissioner and ordered that the three items be excluded from the assessment of the Hindu undivided family. C

At the instance of the Commissioner of Income-tax, the following question was referred by the Tribunal to the High Court of Kerala : D

Whether on the facts and in the circumstances of the case, the Tribunal was justified in holding that the income from salary, commission and sitting fees obtained by Sri P. N. Krishna Iyer from M/s P.S.N. Motors (Private) Ltd., Trichur, represented his individual income and not the income of the Hindu undivided family of which he is the *karta* ?" E

At the instance of the assessee the following question also was referred by the Tribunal : F

"Whether the Commissioner has jurisdiction to revise the order of the Income-tax Officer in view of the decision of the Appellate Assistant Commissioner in appeals for the assessment years 1954-55 to 1957-58 in the assessment of Sri P. N. Krishna Iyer in the status of an individual ?" G

The High Court answered the question referred at the instance of the Commissioner in the negative and the question referred at the instance of the assessee in the affirmative. The assessee has appealed to this Court with special leave granted by this Court.

The question relating to jurisdiction of the Commissioner to revise the order of the Income-tax Officer presents little difficulty. Sub-section (1) of s. 33B of the Income-tax Act, 1922, provides : H

A "The Commissioner may call for and examine the record of any proceeding under this Act and if he considers that any order passed therein by the Income-tax Officer is erroneous in so far as it is prejudicial to the interests of the revenue, he may
B pass such order thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment, or cancelling the assessment and directing a fresh assessment."

C Counsel for the assessee urged that the Commissioner has no power under s. 33B to revise an order of the Income-tax Officer after it had been carried in appeal to the Appellate Assistant Commissioner, and also urged that an order passed by an Income-tax Officer in pursuance of a direction by the Appellate Assistant Commissioner could not be revised by the Commissioner in exercise of the power under s. 33B. But in our judgment there is no ground for holding that the Commissioner has attempted to revise the order of the Appellate Assistant Commissioner. In
D computing the income of the assessee as an individual, the Appellate Assistant Commissioner had directed certain modifications to be made, and pursuant thereto the assessments of the assessee and of the Hindu Undivided family of which the assessee was the *karta* were rectified. The order of assessment of the Hindu Undivided family was never challenged in appeal to the Appellate Assistant Commissioner. The Commissioner revised
E the order passed by the Income-tax Officer insofar as it related to the Hindu Undivided family. It is true that in consequence of the order of the Commissioner, the salary, commission and the "sitting fee" received by the assessee had to be excluded from the total income of the assessee. But the Commissioner had power to revise the order passed by the Income-tax Officer which had
F not been appealed from. Modification in the order of the Income-tax Officer insofar as it related to the assessment of the assessee was consequential upon that order : it was made to prevent double taxation of the same income. It is true that the assessment of the assessee as an individual had become final before the order of the Commissioner, but that did not bar the exercise of jurisdiction by the Commissioner under s. 33B (1). The question referred at the instance of the assessee was, therefore, rightly
G answered by the High Court.

H Turning to the other question, the relevant facts which are undisputed may be recapitulated. Rs. 10,000 paid by the assessee for purchasing 100 shares of the Company belonged to the undivided family and were not from the personal fund of the assessee. The Company took over the assets belonging to the family and merely credited the family with rupees eight lakhs odd. The Company valued the services rendered by the assessee

in "the promotion of the Company and the very large sacrifices he had made in agreeing to place his services at the disposal of the Company and the immense benefit that the Company received on account of his long experience, goodwill and reputation in this line of business", at rupees five lakhs and allotted to the assessee 4,880 fully paid up shares of the Company of the face value of Rs. 100 each. Dividends from the shares standing in the name of the assessee were credited not the personal account of the assessee but to the account of the Hindu Undivided family.

In the view of the Tribunal the income from salary, commission and "sitting fee" earned by the assessee was his separate income, because the transport business was "built up with the sole effort of the assessee". The High Court held that the business was at the partition of 1951 treated as the business of the joint family of the assessee and his brothers and was allotted to the assessee as an item of the family property; that the assets of the business were on that account the assets of the Hindu Undivided family of the assessee and his sons, that those assets were made available to the Company without receiving any cash consideration, that the shares initially purchased by the assessee were purchased with the aid of the family funds, and that the shares allotted to the assessee were also treated as belonging to the family and to the assessee.

Whether remuneration earned by a member of a Hindu Undivided family as an officer of a company or a firm, in which the assets of the Hindu undivided family have either been invested or the office has been acquired with the aid of the funds of the family is the income of the family or the individual income of the member has arisen in several cases before this Court : *Commissioner of Income-tax v. Kalu Babu Lal Chand*⁽¹⁾; *Piyare Lal Adishwar Lal v. Commissioner of Income-tax*⁽²⁾; *Mathura Prasad v. Commissioner of Income-tax*⁽³⁾; *S. RM. CT. PL. Palaniappa Chettiar v. Commissioner of Income-tax*⁽⁴⁾; *V. D. Dhanwatey v. Commissioner of Income-tax*⁽⁵⁾; and *M. D. Dhanwatey v. Commissioner of Income-tax*⁽⁶⁾; No useful purpose will be served by making an analysis of the earlier cases, because in our view three recent judgments of this Court lay down the principles which govern this class of cases. In *V. D. Dhanwatey's case*⁽⁵⁾ V the Karta of a Hindu undivided family contributed to the capital of a firm out of the funds of the family. Under the agreement of partnership the general management and supervision of the partnership business was to be in the hands of V, and he was to be paid a monthly remuneration out of the gross earnings of the partnership business. V joined the partnership

(1) 37 U.T.R. 123.

(3) 60 I.T.R. 428.

(5) 68 I.T.R. 365.

(2) 40 I.T.R. 17.

(4) 68 I.T.R. 221.

(6) 68 I.T.R. 285.

A as representing the family and he became a partner on account of the investments of the joint family assets in the capital of the partnership and that the remuneration received by V was only an increased share of the profits paid to him as representing the family. This Court (Hegde, J. dissenting) held that the remuneration paid to V was directly related to the investments from the assets of the family in the partnership business and "there was real and sufficient connection between the investment from the joint family funds and the remuneration paid to V". The salary paid to V was therefore assessable as the income of the Hindu Undivided family.

C In *M. D. Dhanwatey's case*⁽¹⁾ the facts were parallel to the facts in *V. D. Dhanwatey's case*⁽²⁾ and salary received by the *karta* of the Hindu Undivided family was treated as income of the family.

D In *S. RM. CT. PL. Palaniappa Chattiar's case*⁽³⁾ the *karta* of a Hindu Undivided family acquired 90 out of 300 shares in a transport company with the funds of the family. In course of time he became the managing director of the Company. As managing director the *karta* was entitled to salary and commission on the net profits of the company, and was entrusted with control over the financial and administrative affairs of the company. The only qualification under the articles of association for the office of a director was the holding of not less than 25 shares in his own right. It was held that the shares were acquired by the family not with the object that the *karta* should become the managing director, but in the ordinary course of investment, and there was no real connection between the investment of joint family funds in the purchase of the shares and the appointment of the *karta* as managing director of the company. The remuneration of the managing director, it was held, was not earned on account of any detriment to the joint family assets, and the amounts received by the *karta* as managing director's remuneration, commission and "sitting fee" were not assessable as the income of the Hindu Undivided family.

G Income received by a member of a Hindu Undivided family from a firm or a company in which the funds of the Hindu undivided family are invested, even though the income may be partially traceable to personal exertion of the member, is taxable as the income of the Hindu Undivided family, if it is earned by detriment to the family funds or with the aid or assistance of those funds; otherwise it is taxable as the member's separate income.

H Counsel for the assessee contended that the Tribunal had found that the business of M/s P.S.N. Motors was built up "by

(1) 68 I.T.R. 285.

(2) 68 I.T.R. 365.

(3) 68 I.T.R. 221.

the sole exertions" of the assessee and when the business was converted into a private limited company the shares therein were allotted to the assessee in view of "the valuable services rendered" by him in the promotion of the company and the "large sacrifices" he had made in agreeing to place his services at the disposal of the Company and "the immense benefit" that the Company received "on account of his long experience, goodwill and reputation in the line of business", and, therefore, the salary, commission and "sitting fee" were in consideration of the services which the assessee rendered and were not attributable to the fact that the family had contributed to the main capital of the Company. Counsel said that this was a finding of fact which was binding upon the High Court. But this Court in *V. D. Dhanwatey's* case⁽¹⁾ has held that the question whether the income was the income of the Hindu undivided family or the individual income was a finding on a mixed question of law and fact, and the final conclusion drawn from the primary evidentiary facts was open to challenge on the plea that the relevant principle had been misapplied by the Tribunal.

The shares which qualified the assessee to become a member of the Company were purchased with the aid of joint family funds. The shares which were allotted to the assessee in lieu of his services were also treated as shares belonging to the joint family. The entire capital assets of the Company originally belonged to the joint family and were made available to the Company in consideration of a mere promise to pay the amount for which the assets were valued. The income was primarily earned by utilising the joint family assets or funds and the mere fact that in the process of gaining the advantage an element of personal service or skill or labour was involved did not alter the character of the income. In cases of this class the character of the receipt must be determined by reference to its source, its relation to the assets of the family of which the recipient was the member, and the primary object with which the benefit received was disbursed. The conclusion of the High Court cannot be said to be vitiated by any error.

The appeal fails and is dismissed with costs.

G.C.

Appeal dismissed.

(1) 68 I.T.R. 365.