

**COMMISSIONER OF INCOME-TAX, BANGALORE**

v.

**SHRI D. C. SHAH**

February 6, 1969

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

*Income-tax—Hindu undivided family invested funds in firm—Remuneration earned by member as officer of the firm—Whether income of family or individual member.*

The assessee—a Hindu undivided family—through its karta was a partner in two firms. The Karta had rich experience in the line of business carried on by the firms. In one of the firms, the Karta was appointed as its Managing Partner and paid a remuneration as Managing Partner in addition to the benefits enjoyed as a partner. In the other firm, another partner was appointed as the Managing Partner, and it was provided that on his retirement, the Karta was to be appointed as the Managing Partner and entitled to the remunerations. The Karta was appointed the Managing Partner of the second firm also on the retirement of its earlier Managing Partner. The assessee-family claimed that the remunerations received by the Karta as Managing Partner should be deleted from the assessment of the assessee, and they were the personal income of the Karta.

**HELD :** The remuneration of the Karta was not earned on account of any detriment to the joint family assets and the accounts received by the Karta as the Managing Partner of the two partnerships were not assessable as the income of the Hindu undivided family. [591 F]

Upon the facts of the case, there was no real or sufficient connection between the investment of the joint family funds and the remuneration paid by the partners to the Karta. The remuneration was paid not because of the family funds invested in the partnership, but for the personal qualifications of the Karta. [591 D—F]

*S. R. M.C.T. PL. Palaniappa Chettiar v. Commissioner of Income-tax*, 68 I.T.R. 221, followed.

*Gurunath V. Dhakappa v. Commissioner of Income-tax, Mysore*, 53 I.T.R. 575; *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; *P. N. Krishna Iyer v. Commissioner of Income-tax Kerala*, [1969] 1 S.C.R. 943 and *Commissioner of Income-tax, Mysore v. G V. Dhakappa*, Civil Appeal No. 713 of 1965 decided on 23-7-1968, referred to.

**CIVIL APPELLATE JURISDICTION :** Civil Appeals Nos. 817 and 818 of 1966.

Appeals by special leave from the judgment and order dated January 19, 1965 of the Mysore High Court in I.T.R.C. No. 1 of 1964.

*Niren De, Attorney-General, S. C. Manchanda and R. N. Sachthy*, for the appellant.

- A *M. C. Chagla, Sharad J. Mhaispurkar, O. P. Malhotra and O. C. Mathur*, for the respondent.

The Judgment of the Court was delivered by

- B **Ramaswami, J.** The respondent is a Hindu Undivided Family (hereinafter called the assessee) of which Shri D. C. Shah is the karta. The assessment years are 1959-60 and 1960-61 and the relevant accounting periods are Samvat years 2014 and 2015. The assessee through its karta Shri D. C. Shah was a partner in the firms of (1) M/s C. U. Shah and Co. and (2) M/s Oriental Can Manufacturing Co. as per terms and conditions set out in the Instruments of Partnership dated 5-6-1961 and 11-9-1957. Shri D. C. Shah was paid a remuneration of Rs. 12,000/- per year for both the assessment years by M/s C. U. Shah and Company. He was paid Rs. 10,000/- for the assessment year 1959-60 by the Oriental Can Manufacturing Company. The amounts received by Shri D. C. Shah were shown by the assessee in its returns of income along with balance of the share income from the aforesaid firms. The Income Tax Officer in assessing the Hindu Undivided Family included the remuneration received by Shri D. C. Shah as a part of the share income from the respective firms. Before the Appellate Assistant Commissioner the assessee contended that the remuneration received by Shri D. C. Shah was his personal income and the amounts were wrongly shown in the returns of the Hindu Undivided Family as its income and should not have been included in the assessment. In so contending the assessee relied on clauses 8, 9 and 10 of the Instrument of Partnership dated 5-6-1961 by which the firm of M/s C. U. Shah and Company was constituted. The assessee also relied on clauses 14, 15 and 16 of the Instrument of Partnership dated 11-9-1957 by which the firm of M/s Oriental Can Manufacturing Company was constituted. Clauses 8, 9 and 10 of the Instrument of Partnership dated 5-6-1961 are to the following effect :

- G "8. The partner No. 1 Shri D. C. Shah who has been managing the business of this firm shall hereinafter also continue to act as Managing partner for conducting the said business free from any interference of other partners, of whatsoever nature. The said Managing partner shall manage, direct, appoint and/or remove any one of the employees, and/or do all other things, which include right to draw cheques, to make, deliver and accept documents either legal or commercial in respect of the partnership business as may be deemed necessary for effectively carrying on the partnership business. The said Managing partner shall be paid Rs. 1,000/- (Rupees one thousand only) per month in addition to all other benefits that he is entitled to enjoy as a partner of the firm.

9. The said Managing partner shall continue to be the Managing Partner for his life time or his retirement whichever is earlier.

10. All other partners shall devote as much time to the furtherance of the partnership business as they think proper, necessary and advisable".

Clauses 14, 15 and 16 of the Instrument of Partnership dated 11-9-1957 are to the following effect :

"14. The partner No. 2 shall be the Managing Partner for conducting the said business free from any interference of whatsoever nature by others. The said Managing Partner shall manage, carry, direct, appoint and/or remove any of the employees and/or Agent and do all other things, as may be deemed necessary, for effectively carrying on the Partnership business. The said Managing Partner shall be entitled, in addition to all other benefits, to a monthly remuneration of Rs. 2,000/- (Rupees two thousand only).

15. The Partner No. 2 shall continue to be the Managing Partner for his lifetime or retirement. In the event of Partner No. 2's demise or retirement, whichever is earlier, the Partner No. 1 shall then act and perform duties and functions of Managing Partner. In the event of the demise or retirement of Partner No. 1, the Managing Partner shall be appointed by the remaining partners or their legal representatives, as the case may be.

16. Partner No. 3 shall be responsible for the duties and functions to be performed under the direction of No. 2, the Managing Partner. In the event of failure on the part of No. 3 to perform duties and functions or otherwise entrusted by No. 2, the Managing Partner, the matter shall be referred to No. 2 and his decision shall be binding on No. 3".

The Appellate Assistant Commissioner accepted the contention of the assessee and held that the remuneration paid and received by Shri D. C Shah should be deleted from the assessment of the assessee. The Income Tax Officer thereafter preferred appeals to the Income Tax Tribunal which set aside the order of the Appellate Assistant Commissioner and held that the remuneration paid should be included in the total income of the assessee. At the instance of the assessee, the Income Tax Appellate Tribunal stated a case to the High Court on the following question of law :—

"Whether on the facts and in the circumstances of the case, was the salary received by D. C. Shah from the

- A** two firms of M/s C. U. Shah & Co. and M/s Oriental Can Manufacturing Co., includible in the assessment of the H.U.F. of which Shri D. C. Shah was the Karta?"

**B** The High Court relying upon its earlier decision in *Gurunath V. Dhakappa v. Commissioner of Income-tax, Mysore*<sup>(1)</sup> held that the salary received by Shri D. C. Shah from the aforesaid firms cannot be included in the assessment of the Hindu Undivided Family of which he was the karta. These appeals are brought by special leave on behalf of the Commissioner of Income Tax, Bangalore from the judgment of the Mysore High Court, dated 19th January, 1965 in Income Tax Reference No. 1 of 1964.

**C** The question whether the 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 been the subject matter of consideration in several cases before this Court. In *V. D. Dhanwatey v. Commissioner of Income-tax*<sup>(2)</sup>, 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 the 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.

**D** It was found that V joined the partnership as representing the family and 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. In this state of facts it was held by this Court that the remuneration paid to V was directly related to the investments of the assets of the family in the partnership business and "there was a real and sufficient connection between the investment from the joint family funds and the remuneration paid to V". It was therefore held by this Court that the salary paid to V was, rightly assessed as the income of the Hindu Undivided Family. In *M. D. Dhanwatey v. Commissioner of Income Tax*<sup>(3)</sup> the facts were parallel to the facts in *V. D. Dhanwatey's case*<sup>(2)</sup> and the salary received by the karta of the Hindu Undivided Family was treated as the income of the family.

**E** In *S. R. M. CT. PL. Palaniappa Chettiar v. Commissioner of Income Tax*<sup>(4)</sup>, the material facts were different. 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

(1) 53 I.T.R. 575.

(3) 68 I.T.R. 285.

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

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

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 found 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 the joint family funds in the purchase of the shares and the appointment of the karta as Managing Director of the company. It was held therefore that the remuneration of the Managing Director 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.

In *P. N. Krishna Iyer v. Commissioner of Income Tax Kerala*<sup>(1)</sup>, the principle laid down in *V. D. Dhanwatey's case*<sup>(2)</sup> was applied. It was held that the remuneration received by the assessee from the company of which he was the Managing Director together with commission and 'sitting fee', should be included in the assessment of the Hindu Undivided Family. It was pointed out that the shares which qualified the assessee to become a member of the company were purchased with the aid of the 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 and the proximity of the connection between the investment from the joint family funds and the remuneration paid. Applying the principle laid down in *V. D. Dhanwatey's case*<sup>(3)</sup>, it was held that the tribunal was justified in holding that the income from the salary, commission or 'sitting fee' obtained by the assessee did not represent his individual income but was the income of the Hindu Undivided Family of which he was the karta.

(1) [1969] 1 S.C.R. 943.

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

**A** In *Commissioner of Income Tax, Mysore v. G. V. Dhakappa*<sup>(1)</sup>, the principle laid down in *V. D. Dhanwatey's*<sup>(2)</sup> case was applied again. It was held that there was no finding that the income which was received by G. V. Dhakappa was directly related to any assets of the family utilised in the partnership, and, therefore, the income of G. V. Dhakappa cannot be treated as the income of the Hindu Undivided Family.

**B** In our opinion, the present case falls within the principle laid down by this Court in *S.R.M. CT. PL. Palaniappa Chettiar's* case<sup>(3)</sup>. It has been found that Shri D. C. Shah was a man of rich experience in the line of business which these two firms were carrying on. Clauses 9 and 10 of the Partnership deed dated 5-6-1961 indicate that the remuneration was paid not because of the family funds invested in the partnership but for the personal qualification of Shri D. C. Shah. In the case of Oriental Can Manufacturing Company clause 14 provided for Shri K. K. Dhote being appointed as the Managing partner. After the said Shri Dhote retired Shri D. C. Shah was appointed as the Managing partner during the assessment year 1959-60. Clause 15 of the partnership deed provided for such an appointment. A reading of clauses 14, 15 and 16 of the Partnership Deed indicates that the remuneration was paid for the specific acts of management done by Shri D. C. Shah resting on his personal qualification and not because he represented the firm. It should also be noticed that no other partner was paid any salary. Upon the particular facts of this case, it is manifest that there was no real or sufficient connection between the investment of the joint family funds and the remuneration paid by the partnership to Shri D. C. Shah. It follows that the remuneration of Shri D. C. Shah was not earned on account of any detriment to the joint family assets and the amounts of remuneration received by Shri D. C. Shah as the Managing partner of the two partnerships were not assessable as income of the Hindu Undivided Family.

For these reasons we hold that there is no merit in these appeals which are accordingly dismissed with costs. There will be one hearing fee.

Y.P.

*Appeals dismissed.*

(1) Civil Appeal No. 713 of 1965 decided on 23-7 1968.

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

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