MISCELLANEOUS CIVIL.

Before Sir Shah Muhammad Sulaiman, Chief Justice, and Mr. Justice Mukerji.

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April, 22.

IN THE MATTER OF JAI DAYAL MADAN GOPAL.*

Partnership—Firm—Whether a firm can be a partner in another firm—Contract Act (IX of 1872), section 239—"Person"—General Clauses Act (X of 1897), section 3(39)—Income-tax Act (XI of 1922), sections 2(2), and 66.

A firm cannot legally be a partner in another firm. The word "person" in section 239 of the Contract Act should not be interpreted so as to include a firm.

[*Per* SULAIMAN, C.J.—The question is not free from difficulty; if the definition of "person" as given in the General Clauses Act were to be applied to section 239 of the Contract Act, a firm would come within the term "person"; and there was nothing repugnant in section 239 itself to the applicability of that definition. Also, according to section 2(2) of the Income-tax Act a firm which is assessed to income-tax and is the assessee is, by the definition of assessee, a "person".]

[*Per* SULAIMAN, C. J.—The Income-tax Act recognizes a firm, which has got itself registered under section 26A of the Act, as a distinct legal entity separate from the individuals who are its partners or proprietors. If a part of the funds of the firm are invested in some other firm, under a mistaken view of the law that the firm can be a partner in the other firm, and some profits are earned on such funds and received by the firm as its own income, the money is income of the firm for the purposes of income-tax.]

[*Per* MUKERJI, J.—If the partners who constituted the registered firm did invest, in ignorance of the law that the firm could not be a partner of another firm, money in the firm's account with the other firm, that fact by itself could not make the income, the source of which was known, the property of the firm and not that of the partners individually.]

In a reference to the High Court under section 66(2) of the Income-tax Act it is open to the High Court to find out for itself what are the questions of law that do arise between the parties and call for determination by the Court, and to re-frame the questions accordingly and decide them.

*Miscellaneous Civil No. 653 of 1931.

Dr. *K. N. Katju* and Mr. *Harnandan Prasad*, for the applicant.

Mr. *U. S. Bajpai* (Government Advocate) for the Crown.

SULAIMAN, C. J. :—The question referred to the High Court by the Commissioner is in the following words :—

"Whether, having regard to the deed of partnership dated the 16th of April, 1928, and to other relevant evidence on the record, the finding that the registered firm Jai Dayal Madan Gopal of Benares is in its corporate capacity a partner in nine other firms bearing the same name was a legal and proper finding."

It is obvious that the Commissioner has assumed that a registered firm can under the law be a partner in another firm in its corporate capacity, and he has asked us to answer the question whether, having regard to the deed of the partnership and to other relevant evidence on the record, the firm Jai Dayal Madan Gopal of Benares is a partner in the other firms.

Strictly speaking, the question of law that one firm cannot legally be a partner in another firm in its corporate capacity has not been referred to us. This would be clear if we see the grounds in the petition of the assessee for reference to the Hgh Court. * * * * The question of the impossibility of one firm being a partner in another firm was not asked to be referred to.

It is, however, clear from the way in which the question has been put by the Commissioner, challenging as it does the legality and propriety of the finding of the Income-tax officer, that it may well be said to include the question of law as stated above. We have power to re-frame the question so as to answer it correctly. But when re-framing it we must take care that we do not answer the new question in a way which would lead the Income-tax department to imply an answer to another question not directly included. The real matter

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with which the department is concerned is whether the income received by the Benares firm from the various partnership concerns in other places is a part of the taxable income of the Benares firm or not. It is in a proceeding relating to the assessment of tax on the income of the Benares firm that the question whether the Benares firm can legally be a partner in the other firms arises.

* * * * *

If an answer were sought as to whether the Benares firm is a partner in the other firms on the basis of the deed of the partnership and other relevant evidence on the record, I would decline to answer the question because that is not a question of law at all but one of fact. Where the evidence is both oral and documentary in addition to the deed of partnership, I would not say that the matter is merely one of a legal inference from found facts, but I would say that it is a question of fact itself.

But if a question were asked whether one firm can legally be a partner in another firm, then I would unhesitatingly proceed to answer it.

There is authority for the view that one firm cannot legally be a partner in another firm. Section 239 of the Contract Act defines a partnership as the relation which subsists between persons who have agreed to combine their property, labour or skill in some business, and to share the profits thereof between them. The view has been expressed that the word "person" in this section does not include a firm. I may refer to the case of *Seodoyal Khemka* v. *Joharmull Manmull* (1), where PAGE, J., remarked that a firm is not a person, it is not an entity but is merely a collective name for the individuals who are members of the partnership. This case was followed by a Division Bench of the Calcutta High Court in *Brojo Lal Saha* v. *Budh Nath Pyarilal* (2), where it was held that a partnership entered into

(1) (1923) I.L.R., 50 Cal., 549(558) (2) (1927) I.L.R., 55 Cal., 551.

by two persons is not a legal person and that a firm is not a person within the meaning of section 239 of the Contract Act. A Bench of our own High Court, in *Basanti Bibi* v. *Babu Lal Poddar* (1), expressed a similar view that the owning of a five annas share in the factory could not be regarded as forming a separate partnership, but that there was only one partnership owning the whole factory. The facts of the last mentioned case were, however, peculiar.

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But it may be pointed out that the definition of the word "person" as given in the General Clauses Act of 1868 which was in force when the Contract Act was passed, and which definition has been reproduced in the Act of 1897, was not expressly considered in the above cases. According to that definition a person includes any company or association or body of individuals, whether incorporated or not: See section II (3) of the Act of 1868 and section 3(39) of the Act of 1897.

In *Kader Bux Omer Hyat* v. *Bukt Behari* (2) another learned Judge of the Calcutta High Court, when considering the argument that a partnership which purports to exist between a firm and an individual is unlawful according to Indian law, pointed out the fallacy in that argument as follows:—"Conceding that a firm is not a legal person, a person within the meaning of section 239 may yet be a combination of persons. 'Person' is not defined in the Contract Act, and the definition of person in the General Clauses Act permits of this being the case. The terms of the section do not render unlawful or impossible a partnership between an association of persons, although unregistered, and an individual". But the learned Judge went on to say "that a firm is nothing but an association of individuals, and that when such an association under a firm name enters into a partnership with another individual or another association of individuals, it is not the ag-

(1) [1930] A.L.J., 1517(1519). (2) (1932) 36 C.W.N., 489(490).

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gregate that combines with the individual but the individuals composing that aggregate."

If the definition of "person" as given in the General Clauses Act were to be applied to the word "person" in section 239, there would be absolutely no reason to exclude a firm from the scope of that word. No doubt the definitions in the General Clauses Act apply only when there is nothing repugnant in the subject or context. But it would be difficult to say that there is something repugnant in section 239 itself to the applicability of that definition of person. No doubt there are other sections in chapter XI of the Contract Act dealing particularly with the death or disability of partners which would not be applicable to a firm.

There is nothing absolutely incongruous in holding that a firm is a legal person. Indeed such a conception exists in some systems of law. The English Partnership Act of 1890 (53 and 54 Vict. Cap. 39), section 4, subsection (2) lays down that in Scotland a firm is a legal person distinct from the partners of whom it is composed.

The question is not free from difficulty, but having regard to the previous authorities, particularly of this Court, I am not prepared to dissent from the view that the word "person" in section 239 of the Contract Act should not be interpreted so as to include a firm. Such an interpretation avoids complications in dissolution of partnerships and may well be accepted.

But the question whether a firm cannot be legally a partner in another firm, so as to be able to enforce all the rights of a partner and be burdened with all the liabilities of a partner, is entirely different from the question whether the income received by a firm which was wrongly admitted as a partner and paid over to that firm is not legally money belonging to that firm.

The question before us arises under the Indian Income-tax Act. The firm Jai Dayal Madan Gopal

of Benares is the assessee in this case. According to section 2(2) of that Act an assessee means a *person* by whom income-tax is payable. The present reference under section 66 arises in the course of an assessment and has been made at the request of the assessee. We must for the purposes of the Income-tax Act regard the assessee, namely the Benares firm, as a "person", otherwise the department cannot tax the assessee at all. Under section 239 of the Indian Contract Act the firm of Benares is a partnership firm. It can own property and have its own income. It can have a manager authorised to act on its behalf and to dispose of its funds. The Income-tax Act recognizes a firm which has got itself registered under section 26A of the Income-tax Act. It, therefore, seems to me that the firm of Benares is a distinct legal entity recognized by law, separate from the two individuals who are its partners or proprietors. If the Benares firm had some funds of its own, and a part of its funds was invested in some other firm under a mistaken view of the law that the firm can be a partner in the other firm, and some profit was earned on such funds and has been paid over to the Benares firm and received by it as its own income, the money belongs to the Benares firm and it is income received by that firm for purposes of the income-tax. It is immaterial whether in the eye of the law the status of the Benares firm was that of a partner in the other firm or not, and quite immaterial whether the Benares firm could have in a court of law enforced its rights as a partner in the other firm or that other firm could have enforced the liability of the Benares firm as a partner. Money that has already been paid over to the Benares firm without protest as profits on that firm's own funds has become a part of the income of the Benares firm. If once it is conceded that the Benares firm exists as an entity, separate from the two individuals who own it, it cannot be said that a part of its funds ceases to

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be the property of the firm as soon as it is invested in another firm. Surely, even if the relationship of a partner does not legally come into existence, the money so invested continues to be the property of the Benares firm, and its return can be claimed. If profit earned on it has been paid to the Benares firm, the profit must be the property of that firm. In my opinion the question whether such income belongs to the firm or to the partners in their individual capacities is entirely one of fact. If money had been taken by the partners out of the Benares firm and re-invested by them in the other firms, then it is their money and the profits earned on it belonged to them in their individual capacities. If, on the other hand, the money belonged to the Benares firm and was invested by the Benares firm as such and profits on the amount had been received back by the Benares firm, the capital continues to belong to the Benares firm and the income earned thereon is the property of the Benares firm, although the Benares firm cannot in the eye of the law have the status of a partner in the other firms.

Subject to the limitation that it does not necessarily follow that the income received by the Benares firm is no part of its own income, I would answer the question referred by saying that even though the finding may be justified on the evidence, the Benares firm cannot legally be a partner in the nine other firms.

MUKERJI, J. :—This is a reference under section 66, sub-section (2), of the Income-tax Act by the Commissioner of Income-tax, United Provinces.

There is a firm in Benares known as Jai Dayal Madan Gopal. It consists of two partners with equal shares, one being Lala Jai Dayal and the other Rai Sahib Ram Ratan Das.

The firm has an extensive business. Besides owning this firm the two partners have an interest in numerous firms bearing the same name and carrying on business at different parts of the country. In the year, of which

the income for the purpose of assessment was under investigation, it was found that the firm made no profits. It was, however, calculated that the other firms in which the two partners at Benares were interested made considerable profits, which after a slight correction was declared to be Rs.1,81,338. On this amount the tax and super-tax leviable has already been realised in the hands of the different firms. It appears that under the proviso to section 55 of the Income-tax Act, where profits of an unregistered firm have been assessed to super-tax, no further super-tax can be levied on that sum in the hands of an individual partner of the firm. If the two gentlemen, Mr. Jai Dayal and Rai Sahib Ram Ratan Das, be treated as partners of the numerous firms which have yielded the income described above, they would not be any longer liable to pay super-tax on their individual share in the profits. The firm Jai Dayal Madan Gopal has been registered within the meaning of section 2, clause (14), of the Income-tax Act. The view taken by the Income-tax department is that the registered firm Jai Dayal Madan Gopal is a corporate body and as a corporate body is a partner in the nine unregistered firms the profits of which have come to Rs.1,81,338. If this view be correct, the exemption from super-tax contained in the proviso to section 55 of the Income-tax Act will no longer be applicable to the shares of the two individuals, Lala Jai Dayal and Rai Sahib Ram Ratan Das. The contention of these gentlemen is that, as a matter of law, the firm Jai Dayal Madan Gopal is not a corporate body, and could not be, having regard to the provisions of section 239 of the Indian Contract Act, a partner of any other firm. They further contend that as a matter of law they, namely Lala Jai Dayal and Rai Sahib Ram Ratan Das, are partners in the nine firms mentioned, in their individual capacity and are, therefore, not liable to be taxed with super-tax on one-half of the amount Rs.1,81,338.

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A preliminary objection was taken by the learned Government Advocate that the reference itself was incompetent because the controversy arises not because any tax is sought to be levied on the firm Jai Dayal Madan Gopal but because of a controversy that arises out of assessment on the individuals Lala Jai Dayal and Rai Sahib Ram Ratan Das. This contention, however, is not sound because the question has arisen "in the course of the assessment" on the firm Jai Dayal Madan Gopal. The reference is correct and competent.

The question that has been referred to us by the learned Commissioner of Income-tax runs as follows: "Whether, having regard to the deed of partnership dated 16th April, 1928, and other relevant evidence on the record, the finding that the registered firm Jai Dayal Madan Gopal of Benares is in its corporate capacity a partner in nine other firms bearing the same name was a legal and proper finding."

In framing this question for determination by the High Court the learned Commissioner has taken it for granted that the firm Jai Dayal Madan Gopal is a corporate body and it was possible, under the law as contained in the Indian Contract Act, for a firm like this to be a partner of another firm. The assessee firm has always contended that the income of Rs.1,81,338 and odd is their individual income and not the income of the firm Jai Dayal Madan Gopal. The question was very prominently and very clearly put before the Commissioner of Income-tax in paragraphs 4 and 5 at page 25 of the printed reference. The same questions were raised before the Assistant Commissioner of Income-tax in their appeal by the assessee firm.

It has been held in this Court that when a Commissioner of Income-tax states a case, it is open to this Court to find out for itself what are the question or questions of law that do arise between the parties, namely

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the assessee and the Income-tax department, for determination by the High Court and to decide those questions: See *Shiva Prasad Gupta* v. *Commissioner of Income-tax* (1); *In the matter of Kajori Mal Kalyan Mal* (2). This view has been followed in Bombay in the case of *Commissioner of Income-tax* v. *National Mutual Life Association* (3).

In this view of the law this Court has to determine first what was the real point of controversy between the parties and then to pronounce an opinion on it. The real controversy between the parties is whether the partners of the nine unregistered firms which yielded profits are Lala Jai Dayal and Rai Sahib Lala Ram Ratan Das individually or whether it is the firm Jai Dayal Madan Gopal, i.e. the partnership. This is also clear from paragraph 3 of the statement of the case.

There can be no doubt that under section 239 of the Indian Contract Act a firm cannot be a partner of an other firm. According to the Income-tax Act the words "firm", "partner" and "partnership" have the same meaning respectively as in the Indian Contract Act, 1872: Vide section 2, sub-section (6A). A partner ship as defined in section 239 of the Indian Contract Act is the relation which subsists between persons who are agreed to combine their property, labour or skill in some business and to share the profits thereof between them. Persons who have entered into a partnership with one another are called collectively a firm.

It is true that under the definition of the word "person" contained in the General Clauses Act of 1868 a person includes a number of individuals associated for a purpose, although they may not be a corporate body. But this definition would apply only if any other meaning is not indicated by the context of the law to be interpreted. Now by the second paragraph of the definition of "partnership" persons who have entered into a partnership with one another are called collectively a

(1) A.I.R., 1929 All., 819. (2) [1930] A.L.J., 78.
(3) (1931) I.L.R., 55 Bom., 637.

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firm. Then if a firm can be a partner, we have this position that in defining a "partnership" the law uses the word "firm", which is hardly to be expected. For the definition of "partnership" would then run something like this: Partnership is the relation which subsists between individual persons or a firm and another firm or a firm and individual persons who have agreed, etc. This way of defining a term of law is hardly satisfactory. Then if we look to the other sections of the Act, we shall find that chapter XI of the Indian Contract Act never contemplated that an incorporated body like a firm could be a partner. Take for example section 254 which runs as follows: "At the suit of a partner the court may dissolve the partnership in the following cases: (1) When a partner becomes of unsound mind." Now can a firm become of unsound mind? Then again let us consider section 253. Almost each of the rules regulating the relations of persons *inter se* presuppose that the partners are individuals and not an incorporate body like a firm. My own opinion, therefore, is that a firm cannot be a partner in another firm. This opinion of mine was expressed by my brother BENNET, J., sitting with me, in *Basanti Bibi* v. *Babu Lal Poddar* (1). This view has also been taken in Calcutta; See *Seodoyal Khemka* v. *Joharmull Manmull* (2), which was approved in *Brojo Lal Saha* v. *Budh Nath Pyarilal* (3). The latest Calcutta case, *Kader Bux Omer Hyat* v. *Bukt Behari* (4), does not take a contrary view, as was urged by the learned Government Advocate.

It being then the settled law that a firm cannot be a partner in another firm, the Income-tax officer was undoubtedly in the wrong when he held that the firm Jai Dayal Madan Gopal was a partner in the nine firms carrying on business at different places under the style Jai Dayal Madan Gopal.

(1) [1930] A.L.J., 1517.
(2) (1923) I.L.R., 50 Cal., 549.
(3) (1927) I.L.R., 55 Cal., 551.
(4) (1932) 36 C.W.N., 489.