CASE ANALYSIS OF COMMISSIONER OF INCOME TAX V. PALANIAPPA

Written by ***Meher Tatineni***

2nd Year BBA LLB Student, School of Law Christ University, Bangalore, Karnataka

INTRODUCTION

The concept of Hindu law is deeply rooted in Hindu philosophy and Hindu religion. The ancient Hindu social structure and its continuance in modern times is to a great extent the outcome of Hindu philosophy and religion. One of the ancient Hindu concepts is that of Mitakshara joint family. It has been an unique feature of Hindu jurisprudence which has no match in any ancient or modern system of law. Joint and undivided family is the normal condition of a Hindu society. They are joint together not only in estate but also food and worship. Estate is most important as family can continue to be Joint Hindu Family even in absence of joint food and worship. A JHF consists of all persons lineally descended from a common male ancestor and includes their wives and unmarried daughters. The existence of joint estate/property is not an essential requisite to constitute joint family and family which does not own any property, may nevertheless be joint. The general principle is that a Hindu Family it presumed to be Joint unless the contrary is proved. The rights arise by birth and in case of death his claim ceases. The only benefit in this system is that of tax exemption.

Coparcenary is an unique feature of Joint Hindu Family. A coparcener is one who shares with others in inheritance in the estate of a common ancestor. A Hindu coparcenary is, however, a narrower body than the joint family, only males who acquire by birth an interest in the joint or coparcenary property can be members of the coparcenary or coparceners. No female could be a coparcener before 2005. Alienation of Coparcenary Property not possible because of community of Interest as each coparcener has a share in the property. Coparcenary is a creation of law, it cannot be created by act of parties. It varies according to various schools. But the 1956 act made it all into a single law by taking its roots from Mitakshara school. The Mitakshara classification of property into apratibandha daya or unobstructed heritage and

sapratibandha daya or obstructed heritage is jthe natural corollary to the twin concepts of son's birth-right and devolution of joint family property by survivorship

The whole Hindu law is very arbitrary about estate and inheritance and the concept of self acquired property. This vagueness paved way to an integrated act of 1956. Even though the act clarifies many concepts there are some which still need a detailed attention. One of the topics which tops that list of ambiguity is inheritance of self acquired property, and even before inheritance what can be classified as self acquired property. There are many judicial decisions which couldn't make this vagueness any better, they left this topic as muddled as it was. This was one of the earliest precedents regarding this matter which brought about a change in the trend and made an impact on future disputes. This particular case throws light on a very specific topic of salary and remuneration as self acquired property. How should it be treated and what are the various circumstances in which it cannot be treated as self acquired property. As it is evident, according to Hindu Law property can be divide into two kinds which are joint property and self acquired property. A member of the Hindu joint family can under the Hindu Law make separate acquisition of property. The concept of self acquired property was not accepted by the ancient law but slowly it evolved and Yajnavalkya was one of the first scholars to sum up the doctrine of self acquisition. The following was written by him:

"Whatever is acquired by the coparcener himself without detriment to the father's estate, as a present from a friend, or a gift at nuptials, does not appertain to the co-heirs."

The enactments of 1956 replaced a chapter of Hindu law. An altogether different image of Hindu law emerged after being moulded by the parliamentarians of independent India. These innovations have been penetrating the Hindu society, giving it fresh ideals and social perspectives. Conflicts entering the courtroom and the judicial pronouncements concerning them reveal the depth and extent of the change wrought. The law of partition and of coparcenary is a perplexing maze having at places some indicators put there by the decisions of the Privy Council and the Supreme Court.

FILAC ON CIT v. PALANIAPPA

Decided by a **FIVE JUDGE BENCH** consisting of K.N. Wanchoo, C.J., G.K. Mitter, K.S. Hegde, R.S. Bachawat and V. Ramaswami, JJ.

FACTS:

It was a case filed on appeal to the Supreme Court from the lower courts. The appellant is a Hindu Undivided Family consisting of the father and four major sons. The appellant became a shareholder in the Trichy-Sri Rangam Transport Company Ltd. in 1934 and owned 90 shares out of the 300 shares of the company. The shares were acquired with the funds of the Hindu Undivided family of the father and his four major sons. There were initially four shareholders including the appellant, two of whom were directors. On the death of one of the Directors, the appellant became a director in 1941 and on the death of another director who was managing the business the appellant became the Managing Director with effect from 1942. By a resolution dated April 16, 1944 the company granted him an honorarium of Rs. 3,000 for the year 1943-44 and subsequently raised it gradually till it became Rs. 1,000 per month with 12 1/2% commission on the net profits of the company. The Managing Director had control over the financial and administrative affairs of the company and the only qualification required was set out under Art. 19 of the Articles of Association of the company which was to the following effect:

"*The qualification of a Director including the first Director shall be the holding in his own right alone and not jointly with any other person of not less than 25 shares and the qualification shall be acquired within two months of appointment".*

From 1938-39 to 1959-60 the appellant had been submitting returns in the status of Hindu undivided family and upto 1949-50 the assessments were completed in that status. For the assessment years 1950-51 to 1955-56, the assessments were completed in the status of individual, though returns were submitted in the status of Hindu undivided family and the remuneration was included in those assessments. For the assessment year 1956-57, the appellant submitted the return in the status of Hindu undivided family but claimed for the first time that the remuneration and sitting fees from the company should be assessed separately in the Karta's hands. The claim was accepted and a separate assessment made on him as an individual in respect of the remuneration and commission received from the company. This continued till the assessment for the year 1958-59. For the year ended April 13, 1959 which was the previous year for the assessment year 1959-60, the appellant family returned an income of Rs. 26,780 which did not include the Salary, Commission and Sitting fees received by the Karta which amounted to Rs. 18,683. The Income-tax Officer added the remuneration of the

Karta for the assessment of the Hindu undivided family and on the basis of the decision of the Supreme Court.[i] The appellant appealed to the Appellate Assistant Commissioner but the appeal was dismissed. The appellant took the matter in further appeal to the Income-tax Appellate Tribunal, Madras Bench. The Tribunal held that the case was governed by the decision of the Madras High Court[ii] and that the remuneration of the Managing Director ought not to be treated as income of the family.

ISSUES:

Whether the sums of Rs. 9,000, Rs. 8,133 and Rs. 1,550 received by the appellant as Managing Director's remuneration, commission and sitting fees are assessable as the income of the Hindu undivided family of which Palaniappa Chettiar is the Karta or as a separate property of the Karta?

LAWS APPLIED:

INCOME TAX ACT, 1922:

In India, the system of direct taxation as it is known today has been in force in one form or another even from ancient times. It has been first introduced in the year 1860, and has been amended over in years like 1886, 1918 and 1922. The 1922 act was very important andgave, for the first time, a specific nomenclature to various Income-tax authorities. The Income Tax Act of 1922 remained in force until the year 1961. It had many complications so the government felt the need to amend it. At present, there are five heads of Income:

(1) Income from Salary;

(2) Income from House Property;

(3) Income from Profits and Gains of Business or Profession;

(4) Income from Capital Gains;

(5) Income from Other Sources.

In this particular case section 3 of the income tax act 1922 has been used which is “charge of income tax”

Where any Act of the Indian Legislature enacts that income- tax shall be charged for any year at any rate or rates applicable to the total income of an assessee, tax at that rate or those rates shall be charged for that year in accordance with, and subject to the provisions of, this Act in respect of all income, profits and gains of the previous year of every individual, company, firm and Hindu undivided family.

HINDU LAW:

It is a collection of legislatures which fall under the heads of Joint Family and Coparcenary ; Pious Obligation and Debts; Adoption; Marriage; Maintenance; Hindu Widows Right to Property Act, 1937; and Succession.

HINDU SUCCESSION ACT,1956:

There is no particular section talking about the classification of ancestral and self acquired property. Relevant sections can be section 8 which talks about devolution of property.

CASE LAWS REFERRED TO:

C.I.T. West Bengal v. Kalu Babu Lal Chand [iii].
C.I.T. Madras v. S.N.N. Sankaralinga Iyer[iv].
M/s. Piyare Lal Adishwar Lal v. The C.I.T. Delhi[v].

ARGUMENTS ADVANCED:

On behalf of the assessee Mr. Gopalakrishnan put forward the argument that the High Court was in error in holding that the present case was governed by the decision of this Court in The *C.I.T. West Bengal v. Kalu Babu Lal Chand*[vi], that the remuneration earned by the Managing Director was not earned as a result of the utilisation of the joint family funds in the business and there was no detriment to the joint family assets or the use of the joint family assets in the business. It was not therefore a right proposition to state that under the principle of Hindu Law the remuneration of the Managing Director in the present law was directly an accretion from the utilisation of the joint family funds and therefore constituted the income of the Hindu joint family. It was pointed out that in C.I.T., West Bengal v. Kalu Babu Lal Chand the income of the Managing Director arose directly from the use of joint family funds, but the material facts

in the present case are different. In our opinion, the argument of the appellant is well-founded and must be accepted as correct.

JUDGEMENT:

On the High Court giving the judgement against the assessee the case went on appeal by certificate to Supreme Court. The Apex Court observed joint family had control on 90 out of 300 shares which were purchased in ordinary course of business and not for purpose of qualification of 'karta' to become a director, therefore no real connection between investment and appointment of 'karta' as managing director. So, remuneration of managing director was not earned by any detriment to joint family assets, remuneration not to be treated as accretion to income of joint family held, remuneration, commission and sitting fees received by 'karta' are not assessable as income of Hindu Undivided Family.

ANALYSIS:

The above case had many repercussions but there are many cases before this which decided the characteristics of the self acquired property. The very first case is C.N . Arunachala Mudaliar v. C. A. Muruganatha Mudaliar[vii], this is a case which talks about the character of a self-acquired property given by the father by way of a gift to a son. In this case it was rightly pointed out that had the father's property devolved by succession on the son, son's son and son's son's son would have got a right by birth in it, and the property would have been coparcenary property. The question, therefore, is, can the father, by changing the mode of devolution, change the character of the property? The property being father's separate property, he certainly had the right to give it away in gift or alienate it in any other manner. Had he gifted it to a third person, the question would not have arisen, as the third person would have taken it as separate property. The question arose because the donee was a son. The Supreme Court held that the character of the property in the hands of the donee-son would depend upon the intention of the donor-father. If he gave it as a separate property, it would be a separate property, and if he gave it as joint family property, it would have that character. Referring to the character of the separate property on its passing by succession to the son, Mukherjea J. made the following observations:

It is obvious, however, that the son can assert this equal right with the father only when the grandfather's property has devolved upon his father and has become ancestral property in his

hands. The property of the grandfather can normally vest in the father as ancestral property if and when the father inherits such property on the death of the grandfather or receives it by partition, made by the grand father himself during his life-time. On both these occasions, the grandfather's property comes to the father by virtue of the latter's legal right as a son or descendent of the former and consequently it becomes ancestral property in his hands J

The learned judge stated the obvious. The separate property of a Hindu becomes ancestral property in the hands of his son so as to give him in it a coparcenary interest only when: (i) it devolves on him by succession, or (ii) the father, during his lifetime, divides it among his sons. The simple proposition of Hindu law that when a Hindu gets his father's separate property by inheritance, he holds it as a coparcenary property with his son or sons if he has any at that time, and if he has none, then the moment he gets one. In the interlude, i.e., between the period from the death of his father when he inherits the property and a son is born to him, he can treat the property as his separate property and may alienate it, and if, by the time he gets a son, no property is left, the son will obviously get no interest. But if he does not alienate and the inherited property is still with him, the moment a son is born to him, the son becomes a coparcener with him. There is nothing in the Act which expressly or by necessary implication lays down that the old Hindu law relating to the character of inherited or ancestral property has been changed. Nowhere it is laid down that a Mitakshara Hindu male succeeding to his father's separate property will take it as his separate property and his son will have no interest in it by birth.

Way before the above case there was a case regarding salary and remuneration as self acquired property which is *Murugappa v. The Commissioner of Income Tax*[viii], in this case it was held that commission earned by a managing agent is his individual property, unless it is shown that the right was obtained utilising joint family property to its detriment. In another case of *Kalu Babu* as already discussed above the Supreme Court overruled the lower court's decision stating that if the salary or commission is the indirect result of joint family property it cannot be treated as individual property.

The present case emphasised more on what property can be treated as detriment to the joint property and created trend in further judicial decisions. But still there are existed some ambiguities and various situations arose to decide what can be a separate property. In *Piyare Lal v. Income Tax Commissioner*[ix] the court held that the earnings of Karta as a manager are

not the result of the family investment but were his personal skill and outcome so it should be treated as a separate property. On the other hand in *Dhanwantry v. Commissioner of Income Tax*[x] it was held that the salaries earned by coparceners constituted joint family property.

CONCLUSION

There are a lot simulations throughout the judicial history pertaining to this specific matter but the above stated case laws are the important one for important situations that might arise in future. On the basis of above judgements there are some rules which can be established although there are still some unanswered questions and lack of consistency in the decisions. The position can be summed up as follows: if acquisitions are made by a coparcener or by a karta by use of family funds (direct or indirect) they constitute joint family property. The factor of personal skill is not considered in such situation whereas if they are made without any detriment to joint family funds it is separate or self acquired property.

REFERENCES

[i] *C.I.T. West Bengal v. Kalu Babu Lal Chand* ,MANU/SC/0102/1959.
[ii] *C.I.T. Madras v. S.N.N. Sankaralinga Iyer*, MANU/TN/0257/1950.
[iii] MANU/SC/0102/1959
[iv] MANU/TN/0257/1950
[v] MANU/SC/0184/1960
[vi] *Supra note 3.*
[vii] AIR 1953 SC 495.
[viii] 1952 Mad. 828.
[ix] 1960 SC 997.
[x] 1968 SC 683.