

Narayanan and Co. and anr. Vs. Commissioner Income Tax. (Also K. S. Ramakrishnan, P. K. Narayanan and Co. V. Cit (it Ref. Nos. 62 to 64 of 1991)).

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Court : Kerala

Decided On : Mar-14-1996

Reported in : (1996)134CTR(Ker)105

Appeal No. : IT Ref. No. 61 of 1991, 14th March, 1996

Appellant : Narayanan and Co. and anr.

Respondent : Commissioner Income Tax. (Also K. S. Ramakrishnan, P. K. Narayanan and Co. V. Cit (it Ref. Nos. 62

Judgement :

K. SREEDHARAN, J. :

These references have come before us pursuant to an order of reference dt. 30th Sept., 1993 passed by a Division Bench. The Bench doubted the correctness of an earlier Bench decision of this Court in CIT vs . Union Tobacco Co. : [1961]41ITR115(Ker) . According to the Bench, in view of the later pronouncement of the Supreme Court, viz., Jer & Co. vs . CIT : [1971]79ITR546(SC) , the decision of this Court in : [1961]41ITR115(Ker) requires a second look as to whether it laid down good law.

2. IT Ref. No. 61 is a reference made by the Tribunal, Cochin Bench, at the instance of M/s Narayanan & Co., an assessee under the IT Act, in relation to the

asst. yr. 1981-82. IT Ref. Nos. 62 to 64 of 1991 are references made by the Tribunal at the instance of M/s K. S. Ramakrishnan, P. K. Narayanan & Co. The assessment years concerned in these IT References are 1980-81 to 1982-83. Common questions of law arise for consideration in these references. The questions referred are :

1. 'Whether, on the facts and in the circumstances of the case, the firm was entitled to registration under s. 185(1)(a) of the IT Act, 1961, for the asst. yr. 1981-82 ?

2. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that forming a partnership by an Abkari licensee and exploiting the licence amounts to transfer of licence making the business of the firm illegal ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in holding that forming a partnership by an abkari licensee and exploiting the licence making the business of the firm illegal ?

4. Whether, on the facts and in the circumstances of the case, the firm was entitled to registration under s. 185(1)(a) of the IT Act, 1961, for the asst. yrs. 1980-81, 1981-82 and 1982-83 ?'

3. The two assessees are two different firms. During the accounting period relevant to the asst. yr. 1981-82, the firm M/s Narayanan & Co., Edappally and during the accounting periods relevant to asst. yrs. 1980-81, 1981-82 and 1982-83, the firm M/s K. S. Ramakrishnan, P. K. Narayanan & Co., Ernakulam, carried on abkari business exploiting the licences granted in the name of one of the partners of the firm. The firm applied for registration under s. 184 of the IT Act, 1961. The ITO found that there was transfer of licence obtained in the name of one of the partners when the firm was allowed to exploit the licence. The said action on the part of the firm was a violation of the provision contained in s. 15 of the Abkari Act. Consequently, the ITO refused to register the partnership under the IT Act. On appeal, CIT(A) took the view that there was absolutely no prohibition against carrying on of a business in liquor by more than one person forming

themselves into a partnership, since the prohibition under the Act was in respect of the transfer of the licence and not against the exploitation of the licence in partnership with another. CIT, in support of this view, relied on the decision of the Supreme Court in *Jer & Co. vs. CIT* (supra). The AAC consequently held that there was no violation of the Abkari Act or any other provisions of law in constituting a partnership for conducting business as per the licence obtained in the name of one of the partners. Thus, he cancelled the order passed by the ITO refusing registration to the firm. Revenue filed appeal to the Tribunal questioning the decision of the first appellate authority. The Tribunal went into the question as to whether entering into a partnership by a licensee will amount to sale or otherwise transfer of the licence. It took the view that the prohibition in the Abkari Act against the 'sale or otherwise transfer' of the licence was an embargo, which was of a very wider amplitude and would embrace within itself any kind of transaction which had the effect of passing out a substantial interest by the licence holder. In this view of the matter, the Tribunal quashed the order of CIT(A) and restored the orders passed by the ITO. Hence, these references.

4. It is the admitted case of parties that one of the partners alone was the licensee to conduct sale of arrack covered by the licence. After obtaining the licence in his individual name, he entered into partnership with others and thereby constituted M/s Narayanan & Co. in relation to the asst. yr. 1981-82 and M/s K. S. Ramakrishnan, P. K. Narayanan & Co. for the asst. yrs. 1980-81 to 1982-83. The question is whether the licensee was justified in constituting the above partnership firms for carrying on the business of liquor as per the licence granted to one of the partners.

5. Sec. 15 of the Abkari Act prohibits sale of liquor or intoxicating drugs without licence granted by the Commissioner. It states that no liquor or intoxicating drug shall be sold without a licence from the Commissioner. The provisos to that section are not of any relevance as far as the facts on hand are concerned. Sec. 24 of the Act, inter alia, provides that every licence or permit granted under the Act shall be subject to such restrictions and on such conditions as the Government may direct either generally or in any particular instance in that behalf. 'Such conditions and such restrictions' means, the conditions imposed as per the Rules

framed under the Act. Kerala Abkari Shops (Disposal in Auction) Rules, 1974, hereinafter referred to as 'the Rules', among other Rules, lay down general conditions applicable to the licensees who were granted permission to vend liquor. Rule 6(22) of the rules provides :

'The licensee shall not sell or otherwise transfer his contract or licence without the written consent of the Asstt. Excise Commissioner concerned. No licensee shall lease out or sub-rent the whole or any portion of the privilege granted to him under the licence.'

A perusal of the other provisions of the said Rules lead to the conclusion that the State was giving the privilege to vend liquor to the licensee and the licensee only. In other words, the privilege to vend liquor is a personal privilege given to the licensee. The question that is to be tackled in this case is whether the personal privilege that has been granted to the licensee to vend liquor within the State can be shared by him with others on the ground that the others are partners in exploiting the licence granted to the individual and that there is no transfer of the licence. The Supreme Court in *Biharilal Jaiswal vs . CIT* : [1996]217ITR746(SC) , went into the question as to whether a partnership entered into for conducting business in liquor under a licence granted to an individual can be registered under the IT Act, 1961. After an exhaustive survey of the entire decisions on the point, their Lordships came to the conclusion that where the statutory provisions or the conditions of licence do not prohibit the formation of a partnership for exploiting the licence to deal in liquor, such a partnership cannot be held to be illegal; but where there is a specific prohibition, any partnership entered into in contravention of those provisions would be unlawful and void. Such an agreement cannot be recognised by the IT Act as a genuine partnership. Consequently, the only question to be dealt with in the cases on hand, according to us, is whether the provisions of the Abkari Act, the Rules framed thereunder and the conditions of the licence contain any specific prohibition in entering into a partnership for the conduct of the business in liquor covered by a licence granted to an individual partner.

6. The prohibition under the Rules, which is quoted above, is that the licensee shall not sell or otherwise transfer his contract or licence without the written consent of the Asstt. Excise Commissioner. If this prohibition takes within it an embargo on the licensee on entering into a partnership, then the partnership if entered into for exploiting the licence, will be a void one under the Abkari Act and the Rules. Such an agreement, which is contrary to the statutory provision, is void under s. 23 of the Contract Act. Such a partnership, which is void as being prohibited by law, cannot be a genuine partnership entitled to get registration under the IT Act, 1961. So, we have to examine the true scope and effect of r. 6(22) of the Rules.

7. Before examining the above aspect, we have to take note of the public policy behind the grant of licence granted by the State for the production, manufacture, possession, transport, purchase and sale of intoxicating liquors. It has been consistently held by Courts in this country that no person has a fundamental right to deal or trade in intoxicating liquors and the State is entitled to prohibit or regulate their production, manufacture, possession, transport, purchase and sale. This position has been put beyond any doubt whatsoever by the Constitution Bench of the Supreme Court in the decision *Khoday Distilleries Ltd. vs . State of Karnataka* : (1995)1SCC574 . Thus, the right of a citizen to deal in intoxicating liquors is only to the extent it is provided for and permitted by the Act and the Rules made thereunder. As far as the State of Kerala is concerned, the licensee should not 'sell or otherwise transfer' his licence without the written consent of the Asstt. Excise Commissioner. This prohibition imposed on the licensee is one imposed on public policy. The State grants a privilege to the licensee to deal in liquor. The licensee is the only person who is given that privilege and he alone is looked upon by the Government to see whether the said privilege is properly put to use. If the contract entered into between the licensee and the Government is varied in any manner whatsoever, that will tend to injure the public interest. A personal privilege that is obtained by the licensee should be exercised by him and him alone. If he shares that privilege with others, the said action of the licensee will certainly have the tendency to go against the public policy behind the grant of the privilege. Government in its wisdom enacted the Abkari Act and the Rules thereunder taking note of the public good in restricting the privilege to deal in liquor

to the licensee only. That privilege should not be allowed to be shared by the licensee with others. If the licensee is allowed to share the privilege obtained by him under the licence with others, that will certainly go against the public interest and would be injurious and harmful to the public good.

8. Rule 6(22) of the Rules, as noted earlier, prevents sale or otherwise transfer. The word 'otherwise transfer' should be given the widest possible meaning. When the rule making authority use the words 'or otherwise transfer', it apparently intended to cover other cases which may not come within the strict meaning of the word 'sell'. If the rule making authority intended to cover all possible cases of transfer, Courts must give full import to that intention. According to the assessee, r. 6(22) in the latter half deals with lease or sub-rent. So, it is contended that the word 'otherwise transfer' must be read ejusdem generis with the words 'sell', 'lease' or 'sub-rent'. If it is so done, the words 'or otherwise' should take in only those categories which belong to the same genus as 'sale', 'lease' or 'sub-rent'. It cannot be given any wider ambit. Such an interpretation if resorted to, will certainly go to defeat the intention of the rule making authority not to allow the licensee to share his privilege with others. A Constitution Bench of the Supreme Court in *Lila Vati Bai vs . Bombay State* : [1957]1SCR721 , took the view that the words 'or otherwise' should be given the widest possible meaning if so required to give effect to the intention of the legislature. Their Lordships observed :

'The rule of ejusdem generis is intended to be applied where general words have been used following particular and specific words of the same nature on the established rule of construction that the legislature presumed to use the general words in a restricted sense, that is to say, as belonging to the same genus as the particular and specific words. Such a restricted meaning has to be given to words of general import only where the context of the whole scheme of legislation requires it. But where the context and the object and mischief of the enactment do not require such restricted meaning to be attached to words of general import, it becomes the duty of the Courts to give those words their plain and ordinary meaning.'

Under the Abkari Act and the Rules framed thereunder, Government wanted to restrict the rights of individuals in dealing in liquor to the licensees and licensees only. When the licensee is granted such a personal privilege, he cannot be allowed to share that privilege with others. Any interpretation which will enable the licensee to exploit the licence along with others, that interpretation will certainly go to defeat the mischief which is sought to be prevented by the legislature. According to us, the words 'or otherwise' should be given the widest possible meaning and import.

9. Their Lordships of the Supreme Court in *Union of India vs . Om Prakash* : [1976]3SCR998 , while dealing with cl. (c) of s. 30 of the Arbitration Act, 1940, which stated that an award shall not be set aside except on one or more of the following grounds, namely (c) that an award has been improperly procured or is otherwise invalid, observed :

'The words 'or is otherwise invalid' in cl. (c) of s. 30 are wide enough to cover all forms of invalidity including invalidity of the reference. We do not find any reason why the general and unqualified language of cl. (c) should not include an award on an invalid reference which is a nullity.'

This observation also makes it clear that words 'or otherwise' should be wide enough to take in all types of transactions wherein the rights of the original owner is shared by him with others.

10. Now we have to examine what can be the import of the word 'or otherwise transfer'. In its general sense, the expression 'transfer of property' connotes the passing of rights in the property from one person to another. In the case of sale, the entire bundle of rights of the transferor passes on to the transferee. If the transaction does not amount to the passing of the entire rights of the transferor to the transferee can it be described as a transfer of some other kind There are transactions wherein there may be a reduction of the exclusive interest in the totality of rights of the original owner in favour of others. There, the original owner may be sharing his interest with others. The exclusive interest in the property, which is a large interest, if shared by one with another, the exclusive interest of the transferor is reduced to the extent to which he shares the interest with others. The

original owner may not be losing his rights altogether. But, what he enjoys after the transfer is an abridged right which is lesser than the full right which he had. When the licensee enters into a partnership with others, even if there is no sale of his rights to the partners, during the subsistence of the partnership the licensee will not be in a position to deal with the licence as his own. His right becomes restricted to the share of profits which may fall to his share from time to time. In *Addanki Narayanappa vs . Bhaskara Krishnappa* : [1966]3SCR400 , their Lordships observed :

'The whole concept of partnership is to embark upon a joint venture and for that purpose to bring in as capital money or even property including immovable property. Once that is done whatever is brought in would cease to be the exclusive property of the person who brought it in. It would be the trading asset of the partnership in which all the partners would have interest in proportion to their share in the joint venture of the business of partnership. The person who brought it in would, therefore, not be able to claim or exercise any exclusive right over any property which he has brought in, much less over any other partnership property. He would not be able to exercise his right even to the extent of his share in the business of the partnership. As already stated, his right during the subsistence of the partnership is to get his share of profits from time to time as may be agreed upon among the partners and after the dissolution of the partnership or with his retirement from partnership of the value of his share in the net partnership assets as on the date of dissolution or retirement after a deduction of liabilities and prior charges.'

The law stated by their Lordships makes it clear that the licensee when enters into a partnership for exploiting the licence will be parting with his exclusive right under the licence in favour of the other partners. In other words, he transfers a portion of his exclusive privilege to deal in liquor covered by the licence in favour of his partners. Such a transfer is hit by the provision in r. 6(22) of the Rules. Consequently, the partnership is against the Abkari Act and the Rules, because the licence which originally belonged solely to the licensee now becomes subject to the rights of other partners to the partnership. Thus, the licensee by entering into a partnership transfers a portion of his privilege under the licence in favour of

other partners. So, the partnership that has been entered into for sharing the privilege in dealing in liquor with other partners is a prohibited one. Such a contract of partnership is void under s. 23 of the Contract Act. Such a void contract of partnership cannot be recognised as a genuine partnership under the IT Act, 1961.

11. According to the assessee, the Supreme Court in *Jer & Co. vs. CIT* (supra) recognised transfer of the right covered by a licence to deal in liquor in favour of a partnership. So, that decision, it was argued, must govern the issue. This argument, we are afraid, cannot be accepted. In that case, their Lordships were concerned with the licence issued in FL-II, which did not prohibit the licensee from entering into partnership with respect to the business under the licence. The statutory provision dealt with therein only stated that the licensee shall not sub-rent or transfer the licence. In such a circumstance, since there was no prohibition against entry by the holder of the licence to a partnership, the question whether the partnership was illegal or not, according to their Lordships, did not arise. That decision has no application to the case on hand. The scope and ambit of r. 6(22) of the Kerala Rules being, as we stated earlier, the decision in *Jer & Co. vs. CIT* (supra) cannot be an authority for the proposition that a licensee can enter into a partnership for exploiting the licence.

12. In *CIT vs. Union Tobacco Co.* (supra), a Bench of this Court took the view that a licensee by entering into a partnership passes substantial interest in what he has in favour of another and thereby does what the rule seeks to forbid without permission. The statement of the law, according to us, is correct and we approve the same. The said view taken by the Division Bench is in tune with the decision of the Full Bench of this Court in *Appu Menon vs. Narayana Ayyar* 1961 KLT 620 (FB).

In view of what has been stated above, we answer all questions referred in the negative, i.e., against the assessee and in favour of the Revenue. As observed by their Lordships in : [1996]217ITR746(SC) , the partners are bound to be taxed either as an unregistered partnership firm or as an AOP.