

(2000) 01 KL CK 0008

In the High Court Of Kerala

Case No : Income-tax Reference No. 64 of 1996

Commissioner of Gift-tax

APPELLANT

Vs

A.C. Raghava Menon

RESPONDENT

Date of Decision : 31-01-2000

Acts Referred:

Gift Tax Act, 1958 — Section 4(1)

Citation : (2000) 243 ITR 167

Hon'ble Judges : Arijit Pasayat, C.J.;K.S. Radhakrishnan, J

Bench : Division Bench

Advocate : P.K.R. Menon and N.R.K. Nair, for the Appellant; P. Balachandran, for the Respondent

Judgement

Arijit Pasayat, C.J.—Pursuant to the direction given by this court in O. P. No. 4880 of 1992, the following question has been referred to this court u/s 26(3) of the Gift-tax Act, 1958 (in short "the Act"), by the Income Tax Appellate Tribunal, Cochin Bench (in short "the Tribunal") :

"Whether, on the facts and in the circumstances of the case, the asses-see is liable to be taxed under the Gift-tax Act ?"

2. A factual position as indicated in the statement of case is as follows : The assessee was the sole proprietor of a business carried on in the name and style "Mercantile and Marine Services". On May 1, 1972, the said proprietorship business was converted into a partnership business by taking the assessee's major son, daughter and minor sons as partners. The Gift-tax Officer held that by converting the proprietary business into a partnership and allowing his children to share 80 per cent, of the profits of the business, the assessee had gifted 80 per cent, value of the goodwill in the firm and 80 per cent, value of the immovable assets as reduced by the credit given to him by way of capital. Accordingly, the value of the gift was computed and tax was levied. In appeal, the Commissioner of Gift-tax (Appeals), Ernakulam (in short "the CGT(A)"), held that there was no liability for the assessee to gift-tax. Reliance was placed on a

decision of the apex court in Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat, , for the conclusion. The Tribunal upheld the decision of the Commissioner of Gift-tax (Appeals).

3. According to the learned counsel for the Revenue, the decision in Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat, , was not applicable to the facts of the case. It is submitted that the said decision was rendered in a different context relating to capital gains and has no application to a proceeding under the Act. Learned counsel for the assessee, on the other hand, supported the order.

4. Since reliance is placed on a decision of the apex court in Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat, , it is necessary to extract a portion of the judgment (headnote) :

"Where a partner of a firm makes over capital assets which are held by him to a firm as his contribution towards capital, there is a transfer of a capital asset within the terms of Section 45 of the Income Tax Act, 1961, because an exclusive interest of the partner in personal assets is reduced, on their entry into the firm, into a shared interest . . .

The credit entry made in the partner's capital account in the books of the partnership firm does not represent the true value of the consideration. It is a notional value only, intended to be taken into account at the time of determining the value of the partner's share in the net partnership assets on the date of dissolution or on his retirement, a share which will depend upon deduction of the liabilities and prior charges existing on the date of dissolution or retirement. It is not possible to predicate beforehand what will be the position in terms of monetary value of a partner's share on that date. At the time when the partner transfers his personal asset to the partnership firm, there can be no reckoning of the liabilities and losses which the firm may suffer in the years to come. All that lies within the womb of the future. It is impossible to conceive of evaluating the consideration acquired by the partner when he brings his personal asset into the partnership firm when neither can the date of dissolution or retirement be envisaged nor can there be any ascertainment of liabilities and prior charges which may not have even arisen yet. Therefore, the consideration which a partner acquires on making over his personal asset to the firm as his contribution to its capital cannot fall within the terms of Section 48. And as that provision is fundamental to the computation machinery incorporated in the scheme relating to the determination of the charge provided in Section 45, such a case must be regarded as falling outside the scope of capital gains taxation altogether."

5. Section 3 of the Act provides that tax in respect of gift, if any, made by a person during the previous year at the rate specified in Schedule I has to be paid. The term "gift" has been defined to mean "transfer by one person to another of any existing movable or immovable property made voluntarily and without consideration in money or money's worth". It also includes transfer or

conversion of any property referred to in Section 4 which is deemed to be a gift under that section. Amongst others, a release, discharge or surrender, forfeiture or abandonment of any debt, contract or other actionable claim or of any interest on any property by any person, the value of the release, discharge, surrender, forfeiture or abandonment, to the extent to which it has not been found to the satisfaction of the Assessing Officer to have been bona fide, is deemed to be a gift made by the person responsible for the release, discharge, surrender, forfeiture or abandonment. Where a person absolutely entitled to a property causes or has caused the same to be vested in whatever manner in himself and any other person jointly without adequate consideration and such other person makes an appropriation from or out of such property, the amount of appropriation used for the benefit of the person making the appropriation or for the benefit of any other person is deemed to be a gift made in his favour by the person who causes or has caused the property to be so vested.

6. Strong reliance has been placed by learned counsel for the Revenue on a decision of the apex court in *Commissioner of Gift Tax, Gujarat Vs. Chhotalal Mohanlal*, , to contend that there was a deemed gift. On a close reading of the decision, it is clear that the said case related to minors who did not make any capital contribution to the partnership. The apex court observed that reconstitution of a firm admitting the minors to a firm of partnership would involve a gift under the Act. An identical case came up before a Full Bench of this court in *COMMISSIONER OF GIFT-TAX Vs. SMT. C. K. NIRMALA*, . It was held that no gift was involved. It was held that in view of the decisions of the apex court in *Khushal Khemgar Shah and Others Vs. Khorshed Banu Dadiba Boatwalla and Another*, and *Rustom Cavasjee Cooper Vs. Union of India (UOI)*, , goodwill is also an intangible asset. Section 14 of the Indian Partnership Act, 1932 (in short "the Partnership Act"), was also referred to to conclude that the property of the firm includes the goodwill of the business also. But the question as to what are the properties of the firm in a particular case has to be decided with reference to the terms of the contract between the parties. Therefore, the exigibility of gift-tax in a given case is largely dependent on the provisions of the terms of the partnership deed or the terms of the contract governing the transaction of the parties.

7. It has to be noted that in *Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat*, , the apex court has observed as follows (headnote) :

"The consideration for the transfer of the personal assets is the right which arises or accrues to the partner during the subsistence of the partnership to get his share of the profits from time to time and, after the dissolution of the partnership or with his retirement from the partnership, to get the value of his share in the net partnership assets as on the date of the dissolution or retirement after deduction of liabilities and prior charges. The credit entry made in the partner's capital account in the books of the partnership firm does not represent the true value of the consideration. It is a notional value only, intended to be taken into

account at the time of determining the value of the partner's share in the net partnership assets on the date of dissolution or on his retirement... It is impossible to conceive of evaluating the consideration acquired by the partner when he brings his personal asset into the partnership firm when neither can the date of dissolution or retirement be envisaged nor can there be any ascertainment of liabilities and prior charges which may not have even arisen yet. Therefore, the consideration which a partner acquires on making over his personal asset to the firm as his contribution to its capital cannot fall within the terms of Section 48. And as that provision is fundamental to the computation machinery incorporated in the scheme relating to the determination of the charge provided in Section 45, such a case must be regarded as falling outside the scope of capital gains taxation altogether."

8. As has been held in the aforesaid case, the credit entry in the capital account does not represent the true value of the consideration and that such entry simply represents the notional value of the asset. Inadequacy of consideration cannot be judged vis-a-vis a credit entry made in the capital account of the books of the firm. Except the credit entry made in the capital account, there is nothing else on record to conclude that the assessee had transferred the asset to the firm for inadequate consideration, in order to attract the provisions of Section 4(1)(a) of the Act, several conditions have to be fulfilled, i.e., (a) there must be a transfer of property ; (b) consideration for the transfer must be inadequate ; and (c) the market value of the property should be more than the consideration for which the transfer was effected. Only one factor seems to have been stressed upon by the Revenue, i.e., that there has been a transfer, but the remaining ingredients have not been established. That being the position, Section 4(1)(a) cannot be applied and no inference of deemed gift can be drawn. As has been observed in *Sunil Siddharthbhai Vs. Commissioner of Income Tax, Ahmedabad, Gujarat*, , consideration for a transfer is unascertainable until dissolution of the partnership. There is no factual finding with reference to the partnership deed or any other material that the amount recorded in the books of account of the firm was the value of the capital asset contributed by the partners of the firm and it has to be the consideration received or accrued as a result of transfer of the capital asset. The Tribunal has referred to clause 10 of the partnership deed to highlight that in the case of dissolution or retirement or cessation of a person as partner, goodwill remained exclusive property of the assessee. It is, therefore, impermissible to treat the amount credited in the capital account in the books of the firm as the consideration for transfer. The Tribunal was justified in holding that no gift was involved.

9. The answer to the question, therefore, is in the negative, in, favour of the assessee and against the Revenue.