

(1978) 02 MAD CK 0036

In the Madras High Court

Case No : Tax Case No's. 3 of 1973 and 4 of 1975

Commissioner of Gift-tax

APPELLANT

Vs

G. Shanmugam and Another

RESPONDENT

Date of Decision : 04-02-1978

Acts Referred:

Gift Tax Act, 1958 — Section 5(1)

Citation : (1979) 118 ITR 890

Hon'ble Judges : P. Govindan Nair, C.J; S. Ratnavel Pandian, J

Bench : Division Bench

Advocate : Nalini Chidambaram, for the Appellant; S. Swaminathan and K. Ramagopal, for the Respondent

Judgement

Govindan Nair, C.J.—In relation to the assessment year 1965-66 the question has arisen whether a gift, said to arise from the transformation of an individual business to a partnership business, would be exempt from gift-tax u/s 5(1)(xiv) of the G.T. Act, 1958. At the instance of the revenue, the following question has been referred to this court and that question forms the subject matter of T.C. No. 3 of 1973 :

"Whether the Tribunal was justified in holding that the assessee was not liable to be assessed under the Gift-tax Act, 1958, in respect of the gift of goodwill consequent on the formation of a partnership under the deed executed on April 3, 1962, on the ground that the said gift was exempt u/s 5(1)(xiv) of the Act ?"

2. Not satisfied with the above reference, the revenue sought a more specific question being referred to this court in relation to the same assessment for the same year and that has resulted in T.C. No. 4 of 1975 with the following question :

"Whether there is material to support the finding of the Tribunal that the gift was made bona fide for the purpose of the donor's business and could also be held to be reasonable ?"

3. The admitted facts, on the basis of which these questions have to be answered, may now be referred to. One Alagiriswami Chetti was engaged in carrying on the business of transport by using carts. This was apparently a thriving business and this is evident from the assessment proceedings with which we are concerned, because the goodwill of the business had been determined at Rs. 1,60,990. By the end of the financial year ,1961-62, the said Alagiriswami Chetti had reached the ripe old age--it may not be imprudent to say that even now in India 70 is a ripe old age--of 70 years. At that time he decided to form a partnership with his two nephews, who were much younger to him. They were not only assisting him in the business but they were also employees of his, while he was carrying on the business. He took them on as partners and each of them was to get 25% of the profits. The partnership deed came into existence on April 1, 1962 The nephews paid nothing towards capital and they also paid nothing towards the goodwill of the firm. The relevant paragraphs of the partnership deed in the preamble are extracted at page 32 of the typed set of papers, which we may also incorporate in the judgment :

"Whereas the party of the first part has been conducting business in carting contracts with the help of trucks and bullocks since the past more than 30 years under the name and style as "V. Alagiriswamy Chetty" at No. 79, Suryanarayana Chetty Street, Royapuram, Madras-13, till 31st March, 1962.

AND WHEREAS the party of the first part is now unwell and is not able to attend to the business more efficiently as before due to his old age ;

AND WHEREAS the party of the first part has thought it would be convenient to have the business run on partnership basis ;

AND WHEREAS the parties of the second and third parts who were assistants and employees under the party of the first part till 31-3-1962."

4. The other relevant paragraphs in the deed are paras 5, 11 and 12, which were also noticed by the Tribunal and which can be seen at page 35 of the typed set of papers :

"5. The parties of the second and third parts shall be the working parties in the business and shall not be required to contribute any capital towards their shares.....

11. This partnership shall be at will and shall be terminable at any time by giving three calendar months" notice by any partner to the other partners ;

12. The party of the first part shall have the right to take over the business in case any partner retires by giving notice as stated in Clause 11 above."

5. The only other fact that we would like to mention is that within four years of the constitution of the partnership, Alagiriswami Chetti died. There was no appreciable difference in the income of the firm and that of Alagiriswami Chetti. The question is whether on these facts the requirements of Section 5(1)(xiv) of

the G.T. Act have been satisfied. Before dealing with this aspect, we would like to say that we are assuming for the purpose of this case without deciding that there was a gift of the goodwill arising from the constitution of the partnership.

6. We shall now extract Section 5(1)(xiv) of the Act :

"5. (1) Gift-tax shall not be charged under this Act in respect of gifts made by any person.....

(xiv) in the course of carrying on a business, profession or vocation, to the extent to which the gift is proved to the satisfaction of the Gift-tax Officer to have been made bona fide for the purpose of such business, profession or vocation."

7. Two elements are necessary to satisfy this section. The gift must be "in the course of carrying on a business" and the gift must be "for the purpose of the business". The matter has now been elaborately dealt with by the Supreme Court in the decision in Commissioner of Gift-Tax, Kerala Vs. P. Gheevarghese, Travancore Timbers and Products, and also in Commissioner of Gift Tax, Kerala Vs. George Kuruvilla, . It is, therefore, unnecessary and perhaps not permissible to deal with this aspect anew and afresh. The principles laid down by the Supreme Court are that it is not enough if the gift is made while running a business, but it must be established that it is in the course of business. To understand the meaning of the expression "in the course of a business" their Lordships referred to an early decision of the Supreme Court in State of Travancore-Cochin v. Shanmugha Vilas Cashewnut Factory [1953] 4 STC 205 and stated that there must be a link between the business and the gift in order that the gift can be said to be in the course of business. Apart from this connection or nexus between the business and the gift, it must also be established that there is a design, there is a purpose or plan in making the gift and that the gift is made for the purpose of the business. It is not enough if a gift is made in the course of business but it must also be established that the gift is for the purpose of the business. Such a purpose can be established when it is shown that the gift was made to protect the business, to ensure its continuity or to produce greater efficiency or to make it more profitable. It is not possible or even desirable that we should try to enumerate exhaustively the circumstances under which it can be said that the gift has been "for the purpose of the business". It can be for various reasons or purposes of the business and each case will have to be dealt with on the basis of the material and the evidence in that case.

8. Turning now to the gift before us specifically we find that Alagiriswami Chetti has been carrying on the business for some time and he was doing so with the assistance of two of his nephews, who were not only assisting him but were also employees in the business. It is reasonable, therefore, to presume that they gained experience and such skill as is necessary for the purpose of carrying on the business. The fact that they are related to the assessee will not detract from the position flowing from the connection with the business and the resulting

experience. Alagiriswami Chetti had become advanced in age. He did not live very much longer after the formation of the partnership. The Tribunal has found on the above facts that the gift was in the course of business and for the purpose of the business. This view is supported by the observations of the Supreme Court in the two decisions that we have already referred to and it is also supported by the decision of this court in Commissioner of Gift-tax Vs. T.S. Shanmugham, (by LR.), and by the decision of the Kerala High Court in V.O. Markose Vs. Commissioner of Income Tax, .

9. The question referred to us in T.C. No. 3 of 1973, though general, is sufficiently comprehensive to deal with the points of law arising from the order of the Tribunal. Whatever that be, we will deal with the question in T.C. No. 4 of 1975 as well. There was certainly material before the Tribunal and that material had been noticed by the Tribunal and relied on by the Tribunal. We have, therefore, to answer the question in T.C. No. 4 of 1975 in the affirmative, that is, in favour of the assessee and against the department and we do so.

10. Regarding the larger question, the only thing that can possibly be said in favour of the revenue results from the right given to the partners to leave the firm at will which is embodied in Clause 11 of the partnership deed. The Supreme Court in the decision Commissioner of Gift-Tax, Kerala Vs. P. Gheevarghese, Travancore Timbers and Products, noticed a similar provision in the partnership deed with which they were concerned and appear to have made a point that the right given to the partners to leave the firm was one of the factors among others which detracted from the gift involved being one for the purpose of the business. Such a provision by itself will not, however, be sufficient to say that the gift was not for the purpose of the business. What will happen when an assessee plans to carry on the business in a particular way and whether he will succeed or not is not very material for deciding what was the intention or the purpose with which the gift was made. If it ultimately turns out that the partners did not help in carrying on the business but left the firm, other arrangements will have to be made for carrying on the business. But it cannot be said merely from such a possibility of the partner leaving the firm that the constitution of the partnership was not made with the intention of carrying on the business or that the firm was not constituted for the purpose of the business. We do not think, therefore, that this provision that the partners can leave the firm at will is important by itself. This is particularly so in view of Clause 12 of the partnership deed which we have already noticed. It says that if any partner retires, the party of the first part, namely, the said Alagiriswami Chetti, will have the right to take over the business and run it. The continuity of the business is thus ensured and the purpose is clear that it must continue even if the newly taken partners choose to leave. Following the decision of this court in Commissioner of Gift-tax Vs. T.S. Shanmugham, (by LR.), and of the Kerala High Court in V.O. Markose Vs. Commissioner of Income Tax, , we answer the question in T.C. No. 3 of 1973 also in the affirmative, that is, in favour of the assessee and against the department. The department will pay the costs of the assessee including counsel's fee of Rs.

500 one set.