
(1998) 04 MAD CK 0045
In the Madras High Court
Case No : T.C. No. 1900 of 1984

Commissioner of Income Tax

APPELLANT

Vs

S. Natarajan

RESPONDENT

Date of Decision : 28-04-1998

Acts Referred:

Income Tax Act, 1961 — Section 41(2), 45

Citation : (1999) 236 ITR 472

Hon'ble Judges : R. Jayasimha Babu, J;N.V. Balasubramanian, J

Bench : Division Bench

Advocate : C.V. Rajan, for the Appellant; None, for the Respondent

Judgement

N.V. Balasubramanian, J.—At the instance of the Revenue, the following question of law has been referred under the Income Tax Act,

1961 :

Whether, on the facts and in the circumstances of the case and having regard to the provisions of Section 2(47) of the Income Tax Act, 1961, the

Appellate Tribunal was right in holding that the assessee was not liable to capital gains tax u/s 45 when the business of the assessee which runs in

the name and style of V.R. Sambasiva Iyer and Sons was transferred by him to Mir Mohammed Ali ?

2. The assessee is an individual. He sold his proprietorship business styled as V.R. Sambasiva Aiyar and Company as a going concern to one Shri

Mir Mohammed Ali for a consideration of Rs. 36,000. The Tribunal referred to the retirement of the assessee from the two partnerships viz.,

Kamakshi Industries and Southern Engineering Company, due to dispute which arose among the partners. The assessee had received a sum of Rs.

10,000 for taking over his share in Shree Kamakshi Industries and Rs. 8,000 for taking over 5 per cent. of the share which the assessee held in the firm of Southern Engineering Company when both the firms were reconstituted on January 1, 1973. The assessee filed a return of income for the assessment year 1974-75 claiming a loss of Rs. 47,267. The assessee claimed that he was entitled to carry forward certain business losses. The Income Tax Officer, inter alia, determined the business income as against the loss returned at Rs. 1,43,219 by adjusting the loss claimed against a deemed profit u/s 41(2) of Rs. 2,08,595 on the ground that it had arisen by reason of sale of the business of V.R. Sambasiva Aiyar and Co., as a going concern. We are not concerned with the other items found in the order of assessment. The Income Tax Officer also declined to carry forward the depreciation business loss as the business was relinquished in the year of accounting. On appeal, the Appellate Assistant Commissioner confirmed the assessment. The assessee carried the matter in appeal to the Appellate Tribunal and raised several contentions regarding the assessment of profit u/s 41(2) of the Act. The Tribunal raised the following points for consideration :

1. Whether the assessee is liable to Section 41(2) profits to the extent of Rs. 2,08,959 ?
2. Whether the assessee is liable to long-term capital gains of Rs. 1,58,800 as arising from the transfer of the assessee's proprietary interest in the concern of V.R. Sambasiva Aiyar and Company ?
3. Whether the assessee is liable for short-term capital gains of Rs. 2,05,213 as regards Kamakshi Industries ?
4. Whether the assessee is liable for capital gains of Rs. 1,38,637 in the case of Southern Engineering Company ?

The Tribunal noticed that under the agreement dated August 16, 1973, wherein the business was sold as a going concern, the assessee transferred his rights in the industrial unit, viz., K. R. Sundaram Industrial Estate (P.) Ltd., and the rights under the hire purchase agreement with National Small Scale Industries in favour of the buyer. The Tribunal noticed how the Income Tax Officer arrived at the amounts of profits u/s 41(2) and the capital gains. The Income Tax Officer had noticed the value of the assets as per the balance sheet was Rs. 1,11,746 and he granted deduction of the

same from the total value of the liability amounting to Rs. 4,34,505 and determined the difference at Rs. 3,31,759. The sum of Rs. 36,000 was

added to the said amount of Rs. 3,31,759 and the total consideration under the agreement was thus determined and on the total sum, the Income

Tax Officer determined the profits chargeable u/s 41(2) of the Act and the amounts chargeable under capital gains. The contention of the assessee

before the Tribunal was that the sale consideration was only Rs. 36,000 and the profit could not be Rs. 2,08,959. The Tribunal came to the

conclusion that when the business was transferred as a whole, there was no question of the assessee being liable to profits u/s 41(2) of the Act. As

regards the long-term capital gains arising on the transfer of the assessee's proprietorship business in V. R. Sambasiva Aiyar and Company, the

Tribunal relied upon the decision of the Supreme Court in the case of Commissioner of Income Tax (Central), Calcutta Vs. Mugneeram Bangur

and Co. (Land Department), and held that when the sale was of the whole concern, no part of the price can be attributed to the cost of the land,

and no part of the same is taxable. The Tribunal referred to the cases arising from the retirement of partnership and held that there was no transfer

of capital in the transfer in favour of the partnerships and came to the conclusion that the assessee was not liable to capital gains. In that view of the

matter, it held that it was not necessary to consider the question relating to carry forward of the losses.

3. We have gone through the order of the Appellate Tribunal. The Tribunal was of the view that the decision of the Supreme Court in

Commissioner of Income Tax (Central), Calcutta Vs. Mugneeram Bangur and Co. (Land Department), , was applicable to the facts of the case.

The Tribunal, in the view it had taken should have examined the question further whether any part of the consideration was attributable to the

assets sold by the assessee. The Tribunal unfortunately has not determined that question at all. Secondly, the Income Tax Officer found that even

though under the agreement, it is stated that a sum of Rs. 36,000 was the consideration, the buyer took over the liability amounting to Rs.

3,31,759, as a part of consideration. The Tribunal did not give due attention to the fact that it was the figure arrived at by the parties and when the

buyer took over the liability amounting to Rs. 3,31,759, the assessee to that extent was relieved of the liabilities and it formed part of the

transaction. The amount of liability agreed to be taken over was an agreed sum and the figure of Rs. 3,31,759 cannot be regarded as an ad hoc

figure. The Supreme Court in Commissioner of Income Tax (Central), Calcutta Vs. Mugneeram Bangur and Co. (Land Department), , held that a

sum of rupees one lakh and odd shown as liabilities did not relate to any particular asset and there was no liability u/s 41(2) of the Act. On the

other hand, it is seen that when the parties arrived at a figure for transfer of a business as a whole, and when the buyer took over the business

including the assessee's liabilities and where the liabilities taken over exceeded the value of the assets, the value of the liabilities arrived at by the

parties would be a part of the consideration of the transfer. When considering the question whether the consideration for the transfer can be

attributed to a particular asset transferred to the buyer, it has to be determined whether a portion of the consideration can be attributed to a

particular asset. When the entire business is sold as a going concern, it is impermissible to ignore the liability taken over by the buyer and disregard

the same as not forming a part of the consideration. The Tribunal also did not attach much importance to the fact that even if the assessee succeeds

in its claim that the amount cannot be taxed u/s 41(2) of the Act, the profit or gain arising on the transfer of the assets would be assessable under

capital gains. The Tribunal, therefore, in our opinion, erred in applying the principles laid down in Commissioner of Income Tax (Central), Calcutta

Vs. Mugneeram Bangur and Co. (Land Department), , which was a case where the Supreme Court was dealing with the determination of profit

arising under capital gains when the entire proprietary concern of the assessee was transferred.

4. The Supreme Court subsequently in Commissioner of Income Tax, Gujarat Vs. M/s. Artex Manufacturing Co., explained the decision in

Commissioner of Income Tax (Central), Calcutta Vs. Mugneeram Bangur and Co. (Land Department), , and held that even in the case of a

realisation sale, the excess amount realised over the written down value on the sale of the asset, would be liable to tax, where it is possible to

attribute the sale price to the assets sold and when the value of the plant and machinery was evaluated and transferred. Therefore, in each case, it

has to be seen whether under the agreement, the value of the machinery was evaluated before it was sold. In this case, the Tribunal has not

examined this aspect at all. Further, this court in Additional Commissioner of Income Tax Vs. Govindoss Purushothamdoss, held that where the

parties showed a particular value for the assets in the books, the value arrived at by the parties cannot be taken as a notional figure but a real one.

As we have already pointed out, the Tribunal has not undertaken any such exercise to find out whether the parties have evaluated the value of the

plant and machinery or stock or the liability taken over by the buyer and on what basis the sum of Rs. 56,000 was ultimately agreed to be paid by

the buyer in favour of the assessee.

5. That apart, we are of the view, the case arises on the question regarding the assessability of profits u/s 41(2) of the Act as well as the capital

gains u/s 45 of the Act. We have already indicated that if the case of the assessee succeeds u/s 41(2) of the Act, it has to necessarily fail u/s 45 of

the Act. Admittedly, there was a transfer of business and the business was taken over by the purchaser.

6. In our opinion, the Tribunal should determine the question once again and find out what is the amount of sale consideration for the transfer and

whether it is possible to attribute the sale consideration to any of the assets transferred attracting the provisions of Section 41(2) of the Act and if

Section 41(2) is not attracted, whether there is any liability arising under capital gains. Since the Tribunal has not applied the proper tests in

cancelling the assessment, we direct the Appellate Tribunal to consider the question de novo in the light of the observations made by us.

7. Accordingly, we answer the question of law referred to us in the affirmative, in favour of the Department and against the assessee, subject to the

direction that the Tribunal should go into the question once again and determine the liability to tax. As there was no representation on behalf of the

assessee, there will be no order as to costs.