
(1983) 03 MAD CK 0018
In the Madras High Court
Case No : Tax Case No. 1519 of 1977

M.K. Kuppuraj

APPELLANT

Vs

Commissioner of Gift-tax

RESPONDENT

Date of Decision : 01-03-1983

Acts Referred:

Gift Tax Act, 1958 — Section 2

Citation : (1984) 38 CTR 314 : (1985) 153 ITR 481

Hon'ble Judges : P. Shanmugam, J;G. Ramanujam, J

Bench : Division Bench

Advocate : T.V. Balakrishnan, for the Appellant; J. Jayaraman and Nalini Chidambaram, for the Respondent

Judgement

Ramanujam, J.—The assessee in this case is an individual and he was originally assessed to gift-tax on June 22, 1971. Later, while

completing the assessment in the case of one M/s. M. K. Krishna Chetty for the assessment year 1971-72, it was noticed that the assessee had

relinquished his right over future profits by 8% by reducing his share of profit from 50% to 42% and conferring a benefit in favour of four minors,

who were admitted to the benefits of the partnership. The GTO held that by relinquishing his right to the extent of 8%, he should be taken to have

gifted that right to future profits, in favour of the four minors, who were admitted to the benefits of the partnership. He thereafter valued the gift

taking five years' profit of the firm from 1966-67 to 1970-71 as the basis and arrived at an average profit of Rs. 6,46,000. After deducting a sum

of Rs. 1,08,000 representing management remuneration and another sum of Rs. 12,000 being interest on capital employed, he arrived at a net

figure of Rs. 5,26,000. He then ascertained 8% thereon and determined the two

years" purchase at Rs. 84,160. Thus the value of relinquishment of the right by the assessee was deemed to be a gift of the value of Rs. 84,160.

2. Aggrieved by the order of the GTO, the assessee appealed to the AAC. Before the AAC, the assessee contended that the admission of the

minors to the benefits of the partnership could not have constituted a gift or a deemed gift, since there was nothing in the partnership deed dated

April 14, 1970, which had the effect of conferring on the minors any interest in the assets of the firm; that all that the minors secured were the rights

to share the future profits; that the relinquishment of a portion of the assessee's right to future profits cannot be taken as a gift at all and that the

GTO has erred in holding that the gift was the transfer of the right to share future profits and as such the transaction will fall within the definition of

gift". The AAC, however, agree with the assessee's contention and held that the transfer of right to share future profits would not come within the

definition of "gift" as contemplated under the Act. In that view, he allowed the appeal of the assessee.

3. The Revenue took the matter before the Tribunal. The Tribunal, however, found that the assessee, who had a 50 % share in the partnership, on

reconstitution, got a reduced share of 42 % after relinquishing 8 % in favour of four minors, who had been admitted to the benefits of the

partnership and that the re-alignment of profit-sharing ratio consequent on the admission of four minors to the benefits of the partnership resulted in

a gift. In support of that conclusion, the Tribunal referred to the definition of "gift" in s. 2(xii) and the term "transfer of property" as defined in s.

2(xxiv). The Tribunal also referred to s. 30 of the Partnership Act and held that according to s. 30(2) of the Partnership Act, a minor, who had

been admitted to the benefits of a partnership, had a right to such share in the property and the profits of the firm as may be agreed upon. But the

deed in question only stipulated the share of profits. The Tribunal inferred from the terms of the partnership that since the partnership deed is silent,

it could be inferred that the minor partners were each entitled to a share of the firm's property. The Tribunal also referred to the decision of this

court in Commissioner of Gift-tax Vs. V.A.M. Ayya Nadar, , in support of its conclusion that the admission of the minors to the benefits of the

partnership with a right to share in the profits of a firm would amount to a gift.

4. Aggrieved by the decision of the Tribunal, the assessee had sought and obtained a reference to this court on the following question :

Whether, on the facts and in the circumstances of the case, the Appellate Tribunal was right in law in holding that the assessee was liable to gift-

tax ?

5. Before us the learned counsel for the assessee has raised the following three contentions. (1) On the facts of this case, it should be held that

there is no gift by the assessee and if at all there is any gift, it is a gift by the firm in favour of the minors, who had been admitted to the benefits of

the partnership. Even assuming that there is a gift by the assessee, the gift should be taken to be in favour of the partnership and not in favour of the

minors direct and, therefore, the assessee, who is an individual, cannot be subjected to gift-tax as he has not made a gift in favour of the minors. (2)

Even assuming that gift cannot be taken to have been made during the assessment year. (3) Even assuming that there is a gift by the assessee in

favour of the minors, it is a gift of the future profits of the business and, therefore, the estimated value of the gift as worked out by the GTO cannot

be taken to be correct.

6. We are, however, of the view that it is not open to the assessee to raise contention (2) and (3) set out above as the question referred to us is not

comprehensive enough to include them. The question referred only deals with the assessee's liability to gift tax, and the question is whether the

assessee was liable to any gift-tax at all having regard to the nature of the transaction. If the assessee is liable to pay gift-tax, whether the gift-tax is

payable in the assessment year or in any other assessment year is not comprehended by the question referred. Similarly, the quantum of the gift or

the extent of the assessee's gift-tax liability is not comprehended in the question referred to. We do not, therefore, feel compelled to express our

opinion in this case on those contentions advanced by the learned counsel for the assessee. Coming to the first contention which alone falls within

the ambit of the question referred to us, as already pointed out, the Tribunal, while disagreeing with the view taken by the AAC, held that on the

reconstitution of the partnership on April 14, 1970, the assessee had relinquished 8 % from and out of his profit-sharing ratio to the minors who

had been admitted to the benefits of the partnership and that that relinquishing

in favour of the minors will amount to a gift. The learned counsel for the assessee contends that since the minors got the benefits of the partnership as a result of the reconstitution of the partnership under the partnership deed dated April 4, 1970, the assessee should not be taken to be the donor. We have no hesitation in rejecting this contention for the reason that by agreeing to admit the minors to the benefits of the partnership, neither the partnership, nor the other partners, apart from the assessee, had suffered any detriment. Only if they had suffered some detriment and as a result of such detriment, if the minors had obtained a corresponding benefit, then one could say that there has been a transaction of a gift by the partnership or by to the partners to the minors, who have been admitted to the benefits of the partnership. It is true no doubt that it is only with the consent of the other partners the assessee can bring in the minors for getting the benefits of the partnership. But the consent of the other partners had been obtained by the assessee on his parting with 8 % of his profit-sharing ratio in favour of the minors, who have been admitted to the benefits to the partnership. Thus, the assessee alone suffered a detriment for the purpose of bringing in the minors into the partnership, though the consent of the partners only enabled the assessee to bring in the minors into the partnership. The consent given by the partners has no bearing on the question as to whether the transaction of the assessee was detriment to the firm or partners of the firm, because the assessee is admittedly the person who actually relinquished a portion of his interest and not the firm or the partners of the firm. Therefore, we are not able to see how the partners or the firm as such which had not suffered any detriment can be taken to be the donors as contended by the learned counsel for the assessee.

7. The learned counsel for the assessee then contends that the transfer of a right to future profits cannot be taken to be a gift at all because no property in praesenti is transferred and that it is not possible to estimate the future profits for the purpose of valuation of the gift, if any. The learned counsel refers to the decision of this court in Addl. Commissioner of Gift-tax Vs. P. Krishnamoorthy and Others, , in support of his submission that the right to a future profit cannot be a property at all which could be the subject-matter of a gift. The question that arose in the said case was

whether there is any relinquishment of a right to share in the profits of the partnership on a partner's retirement in favour of the continuing and newly admitted partners. The facts in that case were that some of the partners retired from the partnership after collecting from the firm whatever they were entitled to get and the firm continued with the remaining partners. Thereafter, the firm admitted new partners. The GTO took the view that since the retiring partner, even after retirement, had a share in the profits of the partnership, that right should be taken to have been relinquished in favour of the newly admitted partners and that would amount to a gift. When the matter went before the Tribunal, the Tribunal held that once the partners retired, their rights to share profits had ceased and, therefore, they cannot be taken to have relinquished any rights in favour of the newly added partners and, therefore, there is no gift element involved in the transaction. When the matter came before this court, this court took the view that the moment a partner retires from a firm, he will have no right to receive any future profits in the said firm and hence there is no question of his giving up any such right. The learned judges also pointed out in that case, that case, that unless there is an existing right, it cannot be taken to be property and there is no question of a retiring partner having a right to share the future profits and if so, such a non-existent right cannot be property"" as contemplated by the statute. We do not see how this decision will help the assessee in this case. There, it was actually found that the right to received any future profits did not exist and such a non-existent right cannot be taken to be the subject-matter of a gift. In that decision, the decision in Commissioner of Gift-tax Vs. V.A.M. Ayya Nadar, , has been referred to and distinguished by holding that the said decision does not apply to the facts of that case.

8. In the present case, it cannot be said that the right to share future profits does not exist. Admittedly, the assessee had 50% profit-sharing ratio before the admission of the minors to be benefits of the partnership. For the purpose of bringing in the minors to the benefits of the partnership, he has relinquished 8% out of his share of profits from and out of the said 50%. It is only because the assessee has agree to part with this 8% profit-sharing ratio, the other partners consented to the minors being admitted to the benefits of the partnership. This relinquishment of 8% profit-sharing

ratio is admittedly without consideration. Therefore, there is a relinquishment of a right by the assessee in favour of the minors who have been

admitted to the benefits of the partnership. The facts of this case squarely fall within the principle laid down by this court in Commissioner of Gift-

tax Vs. V.A.M. Ayya Nadar, . In that case, there was a reconstitution of the shares as and by way of mutual consent. A change was brought

about by the redistribution of shares by which the assessee, out of 3/9 the share, retained 1/9th share and the balance of 2/9ths share was taken by

the other two partners. This court held that the re-distribution by way of re-alignment of the share involves a transfer of property amounting to a gift

chargeable to gift-tax and that the right of a partner to share in the profits of a firm is as much property as a right of a partner to share in the assets

of the firm, and, therefore, a re-distribution of the share of the profits as between one partner and certain others involves a transfer of the right

which has the effect of diminishing a partner's interest and correspondingly increasing the value or quantum of the shares held by the other partners.

9. In this case, the minors had no interest in the partnership before the reconstitution of the firm on April 14, 1970. It is only by the new terms of

the partnership, the assessee relinquished a portion of the right to share his profits so that the minors can have the benefit of the share relinquished.

This will directly attract the principle laid down in the decision in Commissioner of Gift-tax Vs. V.A.M. Ayya Nadar, .

10. As already stated, the learned counsel for the assessee has contended that the right to receive future profits of the firm is not an existing right.

Similar contention was put forward before this court in the decision cited supra, based on the decision in Controller Commissioner of Gift-tax,

Madras Vs. N.S. Getti Chettiar, , and the Bench rejected the contention and held that the right to share the future profits is as much property as a

right of a partner to share in the assets of the firm.

11. The decision in Commissioner of Gift-tax Vs. V.A.M. Ayya Nadar, has been accepted and followed in Commissioner of Gift-tax Vs. A.M.

Abdul Rahman Rowther, and Commissioner of Gift-tax Vs. K.P.S.V. Duraiswamy Nadar (Decd.) (By Legal Representative), .

12. In Commissioner of Gift-tax Vs. A.M. Abdul Rahman Rowther, , the assessee, who was carrying on a business as sole proprietor, converted

his business into a partnership consisting of himself and his two daughters. While constituting that partnership, the assessee transferred Rs. 25,000

each to his daughter and son from his share capital account. The partnership deed provided that the gross assets and liabilities of the predecessor

firm shall form the assets and liabilities of the new firm and the capital of the firm shall belong equally to the five persons, namely, the assessee, his

three daughters and son, and the profits and losses of the firm shall be divided between and borne by the partners in equal proportions. The

transfer of share capital of Rs. 25,000 each to his daughter and son into the partnership, assigned them a portion of the share capital and realigned

the shares in the partnership and the profit-sharing ratio, which amounted to a gift chargeable to tax and that the redistribution of the profit-sharing

ratio on the admission of the two new partners amounted to a "gift" by the assessee of a portion of his share in the good-will of the firm.

13. In Commissioner of Gift-tax Vs. K.P.S.V. Duraiswamy Nadar (Decd.) (By Legal Representative), , this court has again reiterated its view that

redistribution of the shares in a partnership between partners resulting in diminution of a partner's interest and corresponding increase in the interest

of the other partners without any consideration, amounted to a "gift" chargeable to gift-tax. In that case, reference has been made to s. 29 of the

Partnership Act, which provides that a transferee of a partner's interest is entitled, during the continuance of the firm, to receive the share of profits

of the transferring partner and, on dissolution, to receive the share of the assets of the firm to which the transferring partner will be entitled.

14. Having regard to preponderance of judicial opinion, where a partner relinquishes a portion of his profit-sharing interest in the partnership in

favour of another, the transaction will amount to a "gift" falling within the definition of s. 2(xii) read with s. 2(xxiv) of the Act, we are in entire

agreement with the view taken by the Tribunal in this case. The question is, therefore, answered in the affirmative and against the assessee. The

assessee will pay the costs to the Revenue. Counsel's fee Rs. 500.