

(1970) 10 GUJ CK 0006
In the Gujarat High Court
Case No : Stamp Reference No. 1 of 1968

Velo Industries

APPELLANT

Vs

Collector, Bhavnagar

RESPONDENT

Date of Decision : 05-10-1970

Acts Referred:

Bombay Stamp Act, 1958 — Article 25
Partnership Act, 1932 — Section 48

Citation : (1971) 80 ITR 291

Hon'ble Judges : P.N. Bhagwati, C.J;T.U. Mehta, J;B.J. Divan, J

Bench : Full Bench

Advocate : D.U. Shah, for the Appellant; J.R. Nanavati, Assistant Govt. Pleader, for the Respondent

Judgement

P.N. Bhagwati, C.J.—This is a reference made to us by the Chief Controlling Revenue Authority u/s 54(1A) of the Bombay Stamp Act,

1958. The question which arises for consideration on the reference is as to what is the proper article of the Act under which a creation instrument

executed between the partners of Messrs. Velo Industries is chargeable. To determine the question it is necessary to refer briefly to a few facts

giving rise to the reference. Prior to Aso Vad Amas Samvat year 2021, ten persons carried on business in partnership in the firm name of Messrs.

Velo Industries. Three of them retired from the firm with effect from Aso Vad Amas Samvat year 2021 leaving the other seven as continuing

partners of the firm. The terms and conditions of retirement were recorded in an instrument dated 24th October, 1963, executed by and between

the partners and, since the entire controversy between the parties has turned on the true interpretation of this instrument, it would be desirable to

set out some of its material provisions in extenso. They read, according to their English translation :

1. We have retired from the firm of Messrs. Velo Industries with effect from Aso Vad Amas Samvat year 2021 and you have taken over the

administration of the firm in its present condition together with all goods, debts, outstanding transactions, tenancy and leasehold rights, quotas,

permits, licences, etc., as also goods, properties, reserve funds, tools, equipment, etc., and all liabilities of the firm and you are entitled to carry on

the business in partnership between yourselves or by taking new partners. All rights and liabilities resulting from the administration of the business of

the firm hereafter will now devolve upon you and your new administration.

2. It is agreed between us that the accounts including determination of profit of the present administration up to Aso Vad Amas Samvat year 2021

are to be settled between us by mutual consent as soon as possible and whatever is the amount coming to the share of each of us is to be credited

in his respective account with the firm and no one is to be entitled to raise any objection to the same.

3. Now, we retiring partners and you continuing partners agree and acknowledge by mutual consent and also bind ourselves to that effect that the

accounts of the present administration for Samvat year 2021, or for any other previous year, are not to be reopened on any account and mutually

we abandon and give up our right to do so. Whatever is the amount by way of profit or otherwise credited or debited to our respective accounts

as a result of settlement of accounts already made is final and binding upon all of us.

4. The amounts which are lying credited to the respective accounts of each of the retiring partners shall be treated as a loan given to the firm by

each one of us and if any of us demands it at any time, it shall be returnable by the firm. The outstanding debts and liabilities of the present

administration are to be discharged by you the continuing partners and other partners whom you may admit in the firm. So also whatever are the

debts or outstanding they are to be taken by you..... The liability of the firm for sales tax will also have to be discharged by you.....

8. We retiring partners have no right, title or interest in any registration, licence, permits, quotas, etc., which belong to the firm or which might

hereafter be acquired by the firm on account of the present administration of the firm and you continuing partners or any other new firm which you

may constitute will be entitled to all such registration, licences, permits and quotas.

2. This instrument was submitted for registration at the office of the Sub-Registrar of Assurances on 15th November, 1965. The Sub-Registrar

registered the instrument but took the view that it was a conveyance on sale and, therefore, chargeable to stamp duty under article 25 of Schedule

I of the Act and, since the stamp of Rs. 30 which was fixed on the instrument was insufficient, he impounded the instrument u/s 33 and sent it to the

Collector u/s 37(2). The Collector acting u/s 39 felt a doubt as to the amount with which the instrument was chargeable and he, therefore,

submitted the case for the decision of the Chief Controlling Revenue Authority on 19th January, 1966, u/s 53(2). the Chief Controlling Revenue

Authority by a letter dated 4th October, 1967, intimated to the Collector his decision in the matter, namely, that the instrument was a conveyance

for the amount of Rs. 2,25,632.35 on which stamp of Rs. 12,430 would be required under article 25, clause (b), of the Schedule I to the Bombay

Stamp Act, 1958. Pursuant to the decision of the Chief Controlling Revenue Authority, the Collector passed an order dated 29th December,

1967, adjudicating that a sum of Rs. 12,430, should have been paid under article 25, clause (b) of Schedule I to the Act and, therefore, the

amount of deficit of stamp duty of Rs. 12,400, together with fine of Rs. 500 aggregating in all to Rs. 12,900 should be recovered from Madanlal

Makandas Valia, one of the continuing partners who had produced the instrument for registration. The firm was aggrieved by the decision of the

Chief Controlling Revenue Authority and, accordingly, an application dated 1st February, 1968, was made by the firm to the Chief Controlling

Revenue Authority, requiring him to draw up a statement of the case and refer it to the High Court and, on the application, the Chief Controlling

Revenue Authority made the present reference for obtaining the decision of this court on the following two questions :

(1) Whether the document be construed to be a deed of conveyance of Rs. 2,25,632.35 and requiring the duty of Rs. 12,430 at the rate of 5

1/2% (article 25(b) of Schedule I of the Bombay Stamp Act, 1958) ?

(2) Whether the document be treated as one of dissolution of partnership requiring the duty of Rs. 30 (article 47(b) of Schedule I of the Bombay

Stamp Act, 1958) ?

3. Though the questions referred to us present an alternative only between two articles, namely, 25(b) and 47(b), it would be necessary, in case it

is found that the present case does not fall within either of these two articles, to determine which is the proper article under which it is chargeable to

stamp duty.

4. The charging section in the Act is section 3 which provides, inter alia, that, subject to the provisions of the Act and the exemptions contained in

Schedule I, every instrument mentioned in that Schedule, which is executed in the State on or after the date of the commencement of the Act, shall

be chargeable with duty of the amount indicated in that Schedule as the proper duty for the instrument. Article 25 of Schedule I prescribes the

amount of duty for "conveyance". It consists of two clauses : (a) and (b). It is not material for our purpose to notice the difference between the two

classes since the common requirement in both clauses is that the instrument must be a conveyance and the only question before us is whether the

instrument in the present case could be said to be a conveyance. Now, conveyance is defined in section 2(g) to include a conveyance on sale and

every instrument by which property, whether movable or immovable, is transferred inter vivos and which is not otherwise specifically provided for

by Schedule I. The argument of the revenue was that the present instrument was a conveyance on sale since it transferred the interest of the retiring

partners in the partnership assets to the continuing partners for a sum of money and the transaction, therefore, satisfied the essential elements of a

sale. This argument was sought to be supported by reference to a recent Full Bench decision of the Mysore High Court in Venkatachalapathi v.

State. But we do not think the argument is well-founded. It ignores the true nature of the transaction embodied in the instrument. We have already

set out the relevant provisions of the instrument and it is clear from those provisions that the instrument is nothing but a simple deed of retirement

recording the terms and conditions on which three partners retired from the firm. On retirement, the three partners undoubtedly ceased to have

interest in the partnership assets and the partnership assets continued to belong

to the firm consisting of the continuing partners, but there was no transfer of interest from the retiring partners to the continuing partners in consideration of a sum of money. The retiring partners merely took money representing their respective shares in the partnership and went out of the firm. This position becomes very clear if we consider what is the true nature of the interest of a partner in a partnership and what happens when a partner retires from the firm. The following statement of the law is to be found in Lindley on Partnership, twelfth edition, at page 375, where the learned author describes the nature of the share of a partner in a partnership :

What is meant by the share of a partner is his proportion of the partnership assets they have been all realised and converted into money, and all the partnership debts and liabilities have been paid and discharged. This it is, and this only, which on the death of a partner passes to his representatives, or to a legatee of his share;..... and which on his bankruptcy passes to his trustee.

5. The Supreme Court had also occasion to consider this question in *Narayanappa v. Bhaskara Krishnappa*, and there, after referring to the relevant provisions of the Partnership Act, the Supreme Court proceeded to state the effect of these sections in the following words :

From a perusal of these provisions, it would be abundantly clear that whatever may be the character of the property which is brought in by the partners when the partnership is formed or which may be acquired in the course of the business of the partnership it becomes the property of the firm and what a partner is entitled to is his share of profits, if any, accruing to the partnership from the realisation of this property, and upon dissolution of the partnership from the realisation of this property, and upon dissolution of the partnership to a share in the money representing the value of the property. No doubt, since a firm has no legal existence, the partnership property will vest in all the partners and in that sense every partner has an interest in the property of the Partnership. During the subsistence of the partnership, however, no partner can deal with any portion of the property as his own. Nor can he assign his interest in a specific item of the partnership property to anyone. His right is to obtain such profits, if any, as fall to his share from time to time and upon the dissolution of the firm

to a share in the assets of the firm which remain after satisfying the liabilities set out in clause (a) and sub-clauses (i), (ii) and (iii) of clause (b) of section 48.

6. Then again, at another place in the same judgment, the Supreme Court reiterated this position by saying in clear and specific terms :

... his right during the subsistence of the partnership is to get his share of profits from time to time as may be agreed 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.

7. It is clear that the interest of a partner in the partnership is not an interest in a specific item of the partnership property, but, as pointed out by the

Supreme Court, it is a right to obtain his share of profits from time to time during the subsistence of the partnership and on dissolution of the

partnership or his retirement from the partnership, to get the value of his share in the net partnership assets which remain after satisfying the

liabilities set out in clause (a) and sub-clauses (i), (ii) and (iii) of clause (b) of section 48. When, therefore, a partner retires from the partnership

and the amount of his share in the net partnership assets after deduction of liabilities and prior charges is determined on taking accounts on the

footing of a national sale of the partnership assets and given to him, what he receives is his share in the partnership and not any price for sale of his

interest in the partnership. His share in the partnership is worked out by taking accounts in the manner prescribed by relevant provisions of the

partnership law and it is this and this only, namely, his share in the partnership which he receives in terms of money. There is in this transaction no

element of sale; the retiring partner does not sell his interest in the partnership to the continuing partners. He, on the contrary, carves out his interest

and takes it away by evaluating it. This is exactly what happened in the present case. The three partners retired from the firm and their respective

shares in the partnership at the date of retirement were ascertained on taking accounts and the amounts representing the shares were credited in

their respective accounts with the firm; the firm continued with the remaining partners and the partnership assets continued to belong to the firm

composed of the continuing partners. There was clearly and indisputably no sale

of interest in the partnership assets by the retiring partners to the continuing partners.

8. This conclusion would seem to be clear and inevitable on principle and there would appear to be no need of authority to support it but since the

Mysore High Court has taken a different view in Venkatachalapathi v. State, we might profitably refer to the decision of the Supreme Court in

Commissioner of Income Tax v. Dewas Cine Corporation, which completely supports the view we are taking. There, two partners, each owning a

cinema theatre, formed a partnership to carry on business in partnership as exhibitors of cinematograph films and they brought their respective

theatres into the books of partnership as its assets. The Income Tax Officer allowed depreciation aggregating to Rs. 44,380 in the assessments of

the partnership in respect of the two theatres for the assessment years 1950-51 to 1952-53. On the dissolution of the partnership on September

30, 1951, it was agreed that the theatres should be returned to their original owners and in the books of accounts of the partnership the assets

were shown as taken over at the original price less the depreciation allowed, the depreciation being equally divided between the two partners. The

question arose whether by restoring the theatres to the original owners, there was a transfer by the partnership and the entries adjusting the

depreciation and writing off of the assets at the original value amounted to total recoupment of the entire depreciation by the partnership and on

that account the second proviso to section 10 (2) (vii) of the Indian Income Tax Act, 1922, was attracted, the Supreme Court held that on the

dissolution of the partnership, each theatre had to be deemed to be returned to the original owner in satisfaction partially or wholly of his claim to a

share in the residue of the assets after discharging the debts and other obligations and there was accordingly no sale of the theatres by the

partnership to the individual partners in consideration of their respective shares in the residue, and, consequently, the amount of Rs. 44,380 could

not be included in the total income of the partnership under the second proviso to section 10(2)(vii). Shah J., speaking on behalf of the Supreme

Court, stated the law on the subject in these terms :

Under section 46 of the Partnership Act, 1932, on the dissolution of the firm every partner or his representative is entitled, as against all the other

partners or their representatives, to have the property of the firm applied in payment of the debts and liabilities of the firm, and to have the surplus

distributed among the partners or their representatives according to their rights. Section 48 of the Partnership Act provides for the mode of

settlement of accounts between the partners. The distribution of surplus is for the purpose of adjustment of the rights of the partners in the assets of the partnership; it does not amount to transfer of assets.

On dissolution of the partnership, each partner must be deemed to be returned to the original owner, in satisfaction partially or wholly of his claim

to a share in the residue of the assets after discharging the debts and other obligations. But thereby the partnership was not in law sold by the

partnership to the individual partners in consideration of their respective shares in the residue. The expressions "sale" and "sold" are not defined in

the Income Tax Act; those expressions are used in section 10(2)(vii) in their ordinary meaning.

"Sale", according to its ordinary meaning, is a transfer of property for a price, and adjustment of the rights of the partners in a dissolved firm is not

a transfer, nor is it for a price..... A partner may, it is true, in an action for dissolution, insist that the assets of the partnership be realised by sale of

its assets, but where in satisfaction of the claim of the partner to his share in the value of the residue determined on the footing of an actual or

notional sale property is allotted, the property so allotted to him cannot be deemed in law to be sold to him.

9. These observations, though made in the context of a dissolution of a partnership, are equally applicable where a partner retires from the

partnership. What is given to him by way of his share in the partnership, whether it be cash or some property of the partnership, is received by him

as his share in the net partnership assets, after deducting liabilities and prior charges on settlement of accounts and there is no transfer of any

interest in property from him to the continuing partners nor is it for a price. It is merely an adjustment of the rights between the retiring partners and

the continuing partners in the assets of the partnership; the share of the retiring partner in the partnership is made over to him.

10. It is true that the Mysore High Court has taken a different view in Venkatachalapathi v. State but, with the greatest respect to the learned

judges who decided that case, we find ourselves unable to accept that view. It appears from the judgment in that case that no argument was

advanced before the learned judges based on the distinctive character of the interest of a partner in a partnership. The interest of a partner in the

partnership assets was treated as if it were an interest of a co-owner in property. The learned judges held that, if the result intended to be achieved

by the execution of the instrument in question was extinguishment of the rights and interest of the first party in certain specified properties of the

dissolved firm and corresponding augmentation of the rights and interest of the second party, in consideration of a certain sum of money paid to the

first party, there was no reason why the transaction should not be regarded as a sale of the undivided interest of the first party to the second party.

This reasoning, with the greatest respect, overlooks the true nature of the interest of a partner in a partnership and fails to take into account what

really happens when a partner retires from a partnership and takes away, either in cash or in property, his share in the partnership. We cannot

accept this decision as laying down the correct law, and, in any event, in view of the decision of the Supreme Court in Commissioner of Income

Tax v. Dewas Cine Corporation, it must be regarded as devoid of authority. We must, therefore, reach the conclusion that the instrument in the

present case was not a conveyance on sale and, therefore, not a conveyance within the meaning of section 2(g) and hence it must be held to be not

chargeable under article 25 (b) of the First Schedule. The question then arises whether it was chargeable as a deed of dissolution under article 47

(b) of the First Schedule as contended on behalf of the continuing partners. Now, obviously, the instrument could not be said to be a deed of

dissolution since it did not bring about or record any dissolution of the firm. Three only of the partners retired from the firm while the firm continued

with the remaining partners. The instrument could not, therefore, be held to be chargeable under article 47 (b). But then which is the proper article

under which the instrument could be charged to stamp duty? The only article to which our attention was drawn and which appears to be applicable

in the present case is article 5 which provides for the rate of stamp duty on agreement or memorandum of agreement. The instrument before us is

clearly an agreement or, at any rate, a memorandum of agreement relating to retirement and it must, therefore, be held to be chargeable to stamp

duty under article 5.

11. We, therefore, answer the questions referred to us in the following manner :

Question No. 1 : - In the negative;

Question No. 2 : - Also in the negative.

12. The instrument being an agreement or, at any rate, a memorandum of agreement relating to retirement of three partners from the firm was

chargeable to stamp duty under article 5 of the First Schedule to the Act. The Chief Controlling Revenue Authority will pay the costs of the

reference to the applicant.