
(1974) 02 KL CK 0013
In the High Court Of Kerala
Case No : Income Tax R. No. 15 of 1973

V.O. Markose

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 07-02-1974

Acts Referred:

Citation : (1975) 98 ITR 504

Hon'ble Judges : P. Govindan Nair, C.J;V. Balakrishna Eradi, J

Bench : Division Bench

Advocate : M. Pathrose Mathai, Joy Joseph and Joseph Vellappally, for the Appellant; P.A. Francis and P.K.R. Menon, for the Respondent

Judgement

Govindan Nair, C.J.—Two questions have been referred to us by the Income Tax Appellate Tribunal, Cochin Bench, which read as follows:

"(i) Whether, on the facts and circumstances of the case, the Tribunal was correct in law in holding that the admission of a new partner in the firm of M/s. Joseph & Markose with a 25% share along with the reduction of the share of the assessee in the said firm by 25% involved a gift by the assessee ?

(ii) If the answer to the first question is in the affirmative, whether the Tribunal is justified in rejecting the assessee's claim for exemption of the said gift u/s 5(1) (xiv) of the Gift-tax Act, 1958 ?"

2. For the assessment year 1968-69, Sri V. O. Markose, partner, M/s. V.J. Joseph & Markose, Lawyers, Kottayam, claimed that 50% of his share in the assets of the said firm was transferred to one Sri V. O. Abraham who was admitted to the partnership with effect from August 17, 1966, and that such transfer did not constitute a gift. He further contended that, even if it amounted to a gift, that gift was exempted by virtue of Section 5(1)(xiv) of the Gift-tax Act, 1958. Both these contentions were negated by the Income Tax Officer, in appeal by the Appellate Assistant Commissioner, and in further appeal by the assessee, by the Tribunal.

3. Sri V. O. Markose was one of the two partners of the firm of M/s. Joseph and Markose for a fairly long period and V. O. Markose was entitled to a half share in the profits of the firm. The partners of the firm were members of the legal profession practising law. At the time of the transfer, Sri V. O. Markose was 75 years old and his partner, Sri Thomas Vellapally, has had a serious heart attack and was not in full vigour or health. Sri V. O. Markose wrote two letters explaining the circumstances under which and the reasons that prompted the induction of the new partner. The new partner was a man with varied experience and quite elderly. He has been assisting the firm by doing part of the work of the firm for four years and he was being given remuneration by the firm for such work before he was taken as a partner in the firm. During the last two of those four years he had been paid substantial remuneration for the work that he did for the firm amounting to Rs. 18,000 for each of those years. It is thus clear that the person taken in was one competent to discharge the functions of a partner and was a person associated with the particular type of work that the firm has been doing, and a person who has had experience in handling the type of cases the firm had to deal with. There were only two partners in the firm as we indicated already and both were not in good physical condition which would permit them to undertake arduous tasks which an advocate or counsel is often called upon to discharge, and at, times for continuous periods without any respite. A need for assistance has, therefore, been clearly made out and the partners of the firm decided to take one who was associated with the firm and who had apparently proved to be useful to the firm.

4. In the above circumstances the senior partner decided to transfer one-half of his interest in the assets of the firm to the person newly admitted without any consideration. This transfer certainly amounted to a gift and it was not seriously contended before us that the transfer did not amount to a gift. Section 5(1)(xiv) is in these terms :

"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."

5. The gift must be "in the course of carrying on a business" and further "it must be bona fide for the purpose of the business", A number of decisions had been cited before us by counsel for the assessee and by counsel for the department. But we do not think we should in the light of the two categorical pronouncements of the Supreme Court refer to all these decisions. We shall, however, refer to one case on which much reliance had been placed by counsel for the department merely for the purpose of saying that it will have no application to the question before us. The decision is in *AK. Venkiteswaran v. Commissioner of Income Tax*. The section that was construed by a Division Bench of this court in that case is

Section 16(v) of the Income Tax Act, 1961, for short " the Act", That section is in these terms :

"16. The income chargeable under the head "Salaries" shall be computed after making the following deductions, namely :--.....

(v) any amount actually expended by the assessee, not being as amount expended on the purchase of books or other publications, or on entertainment or on the maintenance of a conveyance, which, by the conditions of his service, he is required to spend out of his remuneration wholly, necessarily and exclusively in the performance of his duties."

6. The assessee in that case, an Income Tax Officer, claimed that the rent he paid for a building that he took on hire in Ernakulam to which place the officer was transferred was a payment made by him which satisfied the requirements of the section and so claimed the rent as an allowable deduction from his salary in computing his total income for the purpose of assessment under the Income Tax Act, 1961. This court ruled that the payment of rent may perhaps be for the performance of his duties but was not wholly, necessarily and exclusively required to be spent in the performance of the duties. The claim of the assessee was, therefore, negatived. We do not think that the principle of this decision has any application.

7. In the decision of the Supreme Court in Commissioner of Gift-tax v. P. Gheevarghese, Travancore Timbers and Products there is an analysis of the critical words "in the course of" and "for the purpose of" occurring in the section. After referring to a very early, decision of the Supreme Court in State of Travancore-Cochin v. Shanmugha Vilas Cashewnut Factory, their Lordships observed :

"Thus, the expression "in the course of carrying on of business, etc., means that the gift should have some relationship with the carrying on of the business. If a donor makes a gift only while he is running the business that may not be sufficient to bring the gift within the first part of Clause (xiv) of Section 5(1) of the Act. It must further be established, to bring the gift within that provision, that there was some integral connection or relation between the making of the gift and the carrying on of the business."

8. These principles have not been doubted and no decision of the Supreme Court has been brought to our notice where a discordant note has been struck to the proposition enunciated. After having thus laid down the principles, the Supreme Court considered the facts of the case and stated as follows :

"We are satisfied that in the present case also it has not been established that the requirements of Section 5(1)(xiv) of the Act were satisfied. The assessee was certainly carrying on his business at the point of time when he admitted his two daughters into the firm. But from that fact alone it did not follow that the gift had been made in the course of the assessee's business nor could it be held that the

gift was made for the purpose of carrying on the assessee's business. The Tribunal came to the conclusion that the partnership did provide for the continuance of the partnership business in spite of the death of the partner and that the main intention of the assessee was to ensure the continuity of the business and to prevent its extinction on his death. A true and correct reading of the deed of partnership indicates that the partners could go out from the partnership in terms of Clause 2 of the schedule in the deed of partnership. Moreover, the partnership was expressly stated to be at will. The real intention of the assessee apparently was to take his daughters into the firm with the object of conferring benefit on them for the natural reason that the father wanted to look to the advancement of his daughters. It was further provided in the deed that even the minor children would, in due course, be admitted to partnership. Clause 18 of the schedule already referred to laid down that the assessee could nominate either one or all of his minor children to be partner or partners on their attaining majority and such nomination or appointment could be made even by a will or codicil. The assessee retained complete control over the running of the partnership business and it can hardly be said that he needed any help from his daughters particularly when there is no evidence that he was in a weak state of health, his age being below 50 years. Moreover, there is nothing to show that the daughters had any specialised knowledge or business experience so as to be able to assist in the development or management of the business. We are wholly unable in these circumstances to accept that the present case is different from Dr. George Kuruvilla's case. In our judgment there was no cogent material to come to the conclusion that the gift of Rs. 25,000 to each of the daughters by the assessee was "in the course of carrying on the business" of the assessee and was "for the purpose of the business".

9. In Commissioner of Gift-tax v. Dr. George Kuruvilla the Supreme Court was unable to find on the facts that the gift was in the course of business and for the purpose of the business. The relevant part of the judgment in the case has been extracted by the Tribunal in its order. We do not think that we should go in greater detail into that decision, for the ambit of the words "in the course of" and "for the purpose of" has been fully dealt with in P. Gheevarghese's case, to which we have already referred to.

10. Turning now to the facts of the case it is not as though there was no material, though the Tribunal has repeatedly said that there was no material and that there was no evidence. Apparently the Tribunal was looking for material and evidence which we are inclined to think was unnecessary for the purpose of establishing the claim of exemption under the section. The material the Tribunal was searching for is clear from what the Tribunal has said in its order. In paragraph 10 of its order, having said earlier that there was no material, there is the following sentence :

"It was not shown, for instance, that but for the admission of the new partner, the work of the firm would have been stopped or even seriously curtailed."

11. Again at the end of the paragraph, after having observed that there was no evidence, the Tribunal proceeded to state :

"It is not shown, for example, that the management of the assessee-firm came to be left wholly to the new partner and that before his induction, the two old partners were not in a position to manage the affairs of the firm and that there was a grave danger of the firm coming to a close."

12. It is unnecessary that the work of the firm would have come to a stop or would have been even seriously curtailed but for the taking of the partner for the section to apply. Nor is it necessary that the affairs of the firm should be left wholly to the new partner. The Tribunal has applied wrong principles of law in determining the ambit of Section 5(1)(xiv). The question whether the requirements of the section have been satisfied or not cannot certainly be a pure question of fact. It must of course depend upon in the first instance certainly on what may be termed to be evidentiary facts. The conclusion to be reached from such evidentiary facts must depend upon the correct legal principles that should be applied and upon the proper legal approach. The second question referred to us in this case can be compared with the question which had of ten arisen whether a particular transaction was an adventure in the nature of trade. Dealing with such a question the Supreme Court elaborately dealt with this aspect whether the conclusion reached by the Tribunal that in a particular case there was an adventure in the nature of trade was a conclusion on a pure question of fact unassailable before the High Court on a reference except when the conclusion on the question of fact itself had been referred to the High Court. In paragraph 11 of the judgment in *G. Venkataswami Naidu & Co. v. Commissioner of Income Tax* this aspect has been fully dealt with, It is not only useful but necessary to extract the passage in view of the contentious that have been referred to by counsel for the department that the conclusion reached by the Tribunal is a conclusion on a pure question of fact which we should accept in trying to answer the question before us :

"What then is the nature of the question raised before us in the present appeal ? The Tribunal and the High Court have found that the transaction in question is an adventure in the nature of trade; and it is the correctness of this view that is challenged in the present appeal. The expression "adventure in the nature of trade" is used by the Act in Section 2, Sub-section (4), which defines business as including any trade, commerce or manufacture, or any adventure or concern in the nature of trade, commerce or manufacture. u/s 10 tax shall be payable by an assessee under the head "profits and gains of business, profession or vocation" in respect of the profits or gains of any business, profession or vocation carried on by him. Thus, the appellant would be liable to pay the tax on the relevant amount if it is held that the transaction which brought him this amount was business within the meaning of Section 2, Sub-section (4), and it can be said to be business of the appellant if it is held that it is an adventure in the nature of trade. In other words, in reaching the conclusion that the transaction is an

adventure in the nature of trade, the Tribunal has to find primary evidentiary facts and then apply the legal principles involved in the expression "adventure in the nature of trade" used by Section 2, Sub-section (4). It is patent that the clause "in the nature of trade" postulates the existence of certain elements in the adventure which in law would invest it with the character of a trade or business; and that would make the question and its decision one of mixed law and fact. This view has been incidentally expressed by this court in the case of Sree Meenakshi Mills in repelling the appellant's argument based on the decision of the House of Lords in *Edwards v. Bairstow and Harrison*. For the respondent, the learned Attorney-General has, however, relied on the fact that the relevant observations in the case of Sree Meenakshi Mills are obiter and he has invited our attention to the decision in the case of *Edwards* in support of his contention that the judgment of the House of Lords would show that the question about the character of the transaction was ultimately treated as a question of fact. Before we refer to the said decision it may be relevant to observe that there are two ways in which the question may be approached. Even if the conclusion of the Tribunal about the character of the transaction is treated as a conclusion on a question of fact, it cannot be ignored that, in arriving at its final conclusion on facts proved, the Tribunal has undoubtedly to address itself to the legal requirements associated with the concept of trade or business. Without taking into account such relevant legal principles it would not be possible to decide whether the transaction in question is or is not in the nature of trade. If that be so, the final conclusion of the Tribunal can be challenged on the ground that the relevant legal principles have been misapplied by the Tribunal in reaching its decision on the point; and such a challenge would be open u/s 66(1) because it is a challenge on a ground of law. The same result is achieved from another point of view and that is to treat the final conclusion as one on a mixed question of law and fact. On this view the conclusion is not treated as one on a pure question of fact, and its validity is allowed to be impeached on the ground that it has been based on a misapplication of the true legal principles. It would thus be seen that whether we call the conclusion in question as one of fact or as one on a question of mixed law and fact, the application of legal principles which is an essential part in the process of reaching the said conclusion is undoubtedly a matter of law and if there has been an error in the application of the said principles it can be challenged as an error of law. The difference then is merely one of form and not substance; and on the whole it is more convenient to describe the question involved as a mixed question of law and fact. That is the view expressed by this court in the case of Sree Meenakshi Mills and, in our opinion, it avoids any confusion of thought and simplifies the position by treating such questions as analogous to those falling under the category of questions of law."

13. We cannot, therefore, accept the contention advanced by Sri P.A. Francis on behalf of the revenue that the matter is concluded against the assessee by the findings entered by the Tribunal. The approach made is clearly erroneous. We are constrained to say that the ambit of the decision of the Supreme Court in P.

Gheevarghese's case and the principles laid down therein have not been properly appreciated or understood by the Tribunal.

14. The gift was not merely during the carrying on of the business. It was in the course of the business, for we see a direct link between the gift and the carrying on of the business satisfying the first requirement of the section and the purpose, design, the plan, and what is sought to be achieved was certainly a continuance of the business and the proper management of the business. In all the circumstances, the gift and the taking of the partner were bona fide acts done for the purpose of the business. The section must inevitably apply and the exemption should have been granted. In the light of the above, we answer the first question referred to us in the affirmative, that is, against the assessee and in favour of the department and the second question in the negative, that is, in favour of the assessee and against the department. We direct the parties to bear their respective costs.

15. A copy of this judgment under the seal of the High Court and the signature of the Registrar will be sent to the Appellate Tribunal as required by Sub-section (1) of Section 260 of the Income Tax Act, 1961.