

(1970) 10 GUJ CK 0005
In the Gujarat High Court

Vrajlal Makandas Valiya

APPELLANT

Vs

L.D. Joshi, Collector

RESPONDENT

Date of Decision : 05-10-1970

Acts Referred:

Bombay Stamp Act, 1958 — Article 25(b), 47(b), 5, 54(1A), 54(1A)
Income Tax Act, 1922 — Section 10(2)(vii)
Partnership Act, 1932 — Section 46

Citation : (1971) 12 GLR 586

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

Bench : Full Bench

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 certain 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 Also Vad Amas, Samvat Year 2021, ten persons carried on business in partnership in the firm name of Messrs. Velo Industries. Three of (hem retired from the firm with effect from Also 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 or set out some of its material provisions in extension. 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 lease hold rights, quotas, permits, licenses 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 (he 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 upto 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 salestax will also have to be discharged by you.

5. We retiring partners have no right, title or interest in any registration, license, permits, quotas etc. which belong to the firm or which might hereafter to 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, licenses, permits and quotas.

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 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 Maganlal Makandas Valiya, 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"/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).

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.

2. 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 clauses since the common requirement in both clauses is that the instrument must be 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 Venkatachalapaihi v. State AIR 1966 Mys323. 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 moneys 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 in his proportion of the partnership assets after 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 representative, or to a legatee of his share; and which on his bankruptcy passes to his trustee.

The Supreme Court had also occasion to consider this question in *Addanki Narayanappa and Another Vs. Bhaskara Krishtappa and Others*, 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 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.

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 upon among the partners and after the dissolution of the partnership 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.

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 remained 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 deducting liabilities and prior charges is determined on taking accounts on the footing of a notional 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 the 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 here clearly and indisputably no sale of interest in the partnership assets by the retiring partners to the continuing partners.

3. 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* (supra), we might profitably refer to the decision of the Supreme Court in *Commissioner of Income Tax, Madhya Pradesh Vs. 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 books of the 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 account 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 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. It prescribes the sequence in which the various outgoings are to be applied and the residue remaining is to be divided 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 theatre 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 theatres were not in law sold by the partnership to the individual partners in consideration of their respective shares in the residue. The expression "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.

(underlining is ours).

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 right between the retiring partner and the continuing partners in the assets of the partnership : the share of the retiring partner in the partnership is made over to him.

4. It is true that the Mysore High Court has taken a different view in Venkatachalapathi v. State (supra) 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 special parties of the dissolved firm and corresponding augmentation of the rights and interest of the second party, in consideration 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 relay 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 (supra), it must be regarded as devoid of authority.

5. 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 that it was chargeable to stamp duty under Article 5.

5.1 We answer the questions referred to us in the following manner: Question

No. 1: In the negative; Question No. 2: also in the negative. The instrument being an agreement or at any rate a memorandum of an 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.