

Gujarat High Court

Commissioner Of Income-Tax, ... vs Mohanbhai Pamabhai on 24 September, 1971

Author: Bhagwati

Bench: P Bhagwati, P Desai

JUDGMENT Bhagwati, C.J.

1. These references raise an interesting question of law relating to the scope of ambit of the charging provision in relation to capital gains tax. The question arises out of the assessments to income-tax made on the assessee for the assessment year 1963-64. Prior to 18th February, 1961, the assessee and seven other persons carried on business in partnership in the firm name of Prajapati Tiles Company. The business of the firm was the manufacture of Mangalore tiles and this business was being carried on by the firm ever since its inception on 13th January, 1953. There were disputes between the partners of the firm and as a result of these disputes, the assessee retired from the firm with effect from 18th February, 1962, leaving the other seven as continuing partners of the firm. The terms and conditions of retirement were recorded in document dated 18th February, 1962, executed by and between the partners. This document was in the form of minutes of the proceedings of the meeting held on 18th February, 1962, at which the decision was taken by the partners that the assessee should retire from the firm. Since one of the main controversies between the parties turns on the true interpretation of this document, it would be desirable to set out its material provisions in extenso. These provisions, according to their English translation, read :

" (1) Resolved that out of the partners of our firm, four partners, namely, (1) Shri Mohan Pamabhai, (2) Shri Chandubha Alubha Rana, (3) Shri Bhojubha Seshubha and (4) Shri Hansraj Notibhai are retiring from our partnership with effect from today, i.e., 18-2-1962, after taking their share in the partnership; and since then they are not partners in our firm.

(2) The seven partners, namely (1) Shri Mohan Rudabhai, (2) Shri Amarsi Motibhai, (3) Shri Virji Becharbhai, (4) Shri Parshottam Rudabhai (5) Shri Mohan Kalabhai (6) Shri Mohan Vanabhai and (7) Mrs. Sharda Chandulal Shah, have taken over the partnership business as a going concern together with all the assets, goodwill and other rights and claims and demands and liabilities of our firm and they have today taken over possession of the entire properties of the firm as a going concern; and the remaining four partners, (1) Shri Mohanbhai Pamabhai; (2) Shri Chandubha Alubha Rana; (3) Shri Bhojubha Seshubhai; and (4) Shri Hansraj Motibhai are retiring from the firm.

(3) The break-up value per share of the partnership assets is determined as follows. The assets and liabilities of the firm as of 18-2-62 are as follows :

Rs.

1,38,020.27	Structure.
32,561.36	Furnace.
58,949.78	Machinery.
17,217.06	Dead stock.
945.81	Cases (Pinjra).
21,252.00	Motor Trucks.
7,663.87	Stores.

8,003.17	Outstanding dues.
1,250.00	Investments.
2,481.43	Goods on hand (ready).
5,338.53	Goods (unready).
53,029.12	Balance.

3,46,712.40

Less :

7,595.25 Debts

3,39,117.16

The above is the value of seventeen shares and, therefore, the value of one share comes to Rs.

(4) The outgoing partners being entitled to get the amount of the goodwill in addition to the

(5) The amount mentioned in condition No. (4) above has been decided to be paid to the outgoing

2. On retirement, each assessee received a certain amount in respect of his share in the partnership as contemplated in clauses (3) and (4) and this amount was worked out by taking the proportionate value of his share in the net partnership assets after deduction of liabilities and prior charges. The amount received by each assessee included in its break-up an amount representing his proportionate share in the value of the goodwill, since goodwill constituted an asset of the partnership and it was liable to be taken into account in determining the share of each assessee in the partnership at the date of retirement. The Income-tax Officer assessing each of the assessees of the assessment year 1963-64, for which the relevant previous year was Samvat year 2016, took the view that the amount received by each assessee to the extent it included his proportionate share in the value of the goodwill represented capital gain chargeable to tax under section 45 of the Income-tax Act, 1961, and he accordingly brought it to tax in the assessment of each assessee. There is no dispute before us as to what was the amount representing the proportionate share of each assessee in the value of the goodwill which was included in the amount received by him on retirement and it is, therefore, not necessary to refer to the figures in the case of each assessee; it would be sufficient to state that in the case of the assessee in the first reference, namely, Income-tax Reference No. 22 of 1970, this amount was taken to be Rs. 28,598. Each of the assessees preferred an appeal to the Appellate Assistant Commissioner but the appeals were unsuccessful and the assessments were confirmed. This led to the filing of the further appeal to the Tribunal by each of the assessees. Two contentions in the main were advanced on behalf of the assessees in these appeals. The first contention was that the retirement of the assessee from the partnership amounted to dissolution of the firm within the meaning of section 47, clause (ii), and, therefore, no transfer of capital asset chargeable to tax under section 45 was involved in the process by which the goodwill of the firm was taken over by the remaining seven partners and the proportionate share in the value of the goodwill was paid to each of the assessees. This contention was negated by the Tribunal which took the view that the present

case was a case of retirement of four partners from the firm and not a case of dissolution which would attract the applicability of section 47, clause (ii). The second contention, however, found favour with the Tribunal and that contention was that goodwill was a self-created asset which has cost nothing to the firm and its partners in terms of money and a "transfer" of it was, therefore, not within the ambit of the charging provision contained in section 45 and the proportionate share in the value of the goodwill received by each assessee for transfer of his interest in the goodwill was not taxable as capital gains. The Tribunal in this view of the matter directed that in the case of each assessee, no amount received in respect of his proportionate share in the value of goodwill should be assessed to tax. The Commissioner was, obviously, dissatisfied with this decision of the Tribunal, in so far as it went against him and he, therefore, moved the Tribunal and, on his application, the following two questions of law were referred for the opinion of this court in the case of each assessee :

" (1) Whether the Tribunal was right in holding that the goodwill of the firm is a self-acquired asset of the firm ?

(2) Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that the amount received by the assessee by way of his share in the goodwill of the firm is not liable to be assessed to tax ?"

3. Each of the assessee submitted at the hearing of the reference application that in addition to the two question proposed by the Commissioner, a third question arising out of the order of the Tribunal, in so far as it decided the first contention against the assessee, should also be referred by the Tribunal. The Tribunal accordingly included the following third question in the reference made in the case of each assessee :

" (3) Whether, on the facts and in the circumstances of the case, the retirement of the assessee as partner from the firm amounted to dissolution of the firm, and, therefore, the capital gain, if any, is chargeable to tax in view of the provisions of section 47(iii) of the Act?"

4. We may point out straightaway that in the view we are taking as regardss questions Nos. (1) and (2), it is not necessary for us to consider the third question and we do not, therefore, propose to answer it.

5. So far as the second question is concerned, there were two contentions urged on behalf of the assessee in support of the decision of the Tribunal that the amount representing the proportionate share of each assessee in the value of the goodwill of the firm was not liable to be assessed to tax as capital gain. One contention was that the proportionate share in the value of the goodwill was received by each assessee as part of the amount representing his share in the net partnership assets after deduction of liabilities and prior charges and this last amount having been received by him in satisfaction of his share in the partnership and not by way of consideration for transfer of his interest in the goodwill or other assets of the firm, there was no transfer of capital asset which would attract liability to capital gains tax. This contention was at no time urged before the revenue authorities or even before the Tribunal and it was raised for the first time at the hearing

of the references before us, but since it does not involve a new question and represented merely a different aspect of the same question, we allowed the assessee to raise it and it must be said in fairness to the counsel for the revenue that the rightly did not contend that it should not be allowed to be raised. The other contention urged on behalf of the assesseees was that having regard to the scheme of the provisions relating to capital gains tax and particularly section 48, clause (ii), the capital asset contemplated by section 45 is a capital asset, acquisition of which has cost something to the assessee in terms of money, and since goodwill of the firm in the present case admittedly cost nothing to the firm and its partners in terms of money, transfer of his interest in the goodwill by each of the assesseees did not attract the charge of capital gains tax. Of these two contentions, the first is, in our opinion, well-founded while the second must be rejected. Our reasons for saying so are as follows :

Turning to the first contention, it is clear from the provisions of the document dated 18th February, 1962, that the assessee retired from the partnership and each of them received a certain amount representing his share in the net partnership assets after deducting debts and liabilities of the partnership. This amount was made up by adding two components : one component represented the proportionate share in the partnership assets other than goodwill after deducting debts and liabilities [vide clause (3)], and the other represented the proportionate share in the goodwill of the firm [vide clause (4)]. The argument of the revenue was that when the assesseees retired from the partnership, the interest of each of the assesseees in the partnership assets including the goodwill was extinguished and there was accordingly "transfer" of his interest in the goodwill by each of the assesseees within the meaning of section 2(47) and the amount representing the proportionate share in the value of the goodwill having been received by each assessee as consideration for transfer of his interest in the goodwill and there being no cost of acquisition of the goodwill to the firm and, consequently, to any partner the whole of such amount is liable to be taxed as capital gain in the hands of each assessee. This argument, plausible though it may seem, is fallacious in that it ignores the true nature of the interest of a partner in a partnership and the legal consequences which flow when a partner retires from the firm.

6. The most authoritative statement of the law on this subject, is to be found in the decision of the Supreme Court in *Narayanappa v. Bhaskara Krishnappa* (A. I. R. 1966 S. C. 1300, 1303, 1304). The facts of that case are rather important and we may briefly state them. The members of two joint Hindu families, which we may for the sake of convenience describe as "A" and "B", entered into a partnership for carrying on business of hulling rice, decorticating groundnuts, etc. The capital of the partnership consisted, inter alia, of some lands contributed by the two families and the course of business of the partnership also, some more lands were acquired by the partnership. The partnership was subsequently dissolved by mutual agreement between the partners and an unregistered document was executed recording the terms and conditions of dissolution which included, inter alia, a stipulation that "A" family had given up their share in the machines, etc., and in the business, and made over the same to the members of "B" family alone completely by way of adjustment. When members of "A" family sought to rely on this document in a subsequent suit for dissolution and accounts of the partnership, members of "B" family raised a contention that since the partnership assets included immovable properties and the document recorded relinquishment by members of "A" family of their interest in those assets, the document was compulsorily

registrable under section 17(1)(c) of the Registration Act and, as it was not registered, it was inadmissible in evidence. To determine the validity of this contention, the Supreme Court was called upon to consider what is the true nature of the interest of a partner in a partnership and what happens when the firm is dissolved or a partner retires from the firm. The Supreme Court analysed the relevant provisions of the Partnership Act and 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 property. No doubt, since in the money representing the value of the 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 on 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-clause (i), (ii), and (iii) of clause (b) of section 48."

7. The Supreme Court then quoted with approval the following statement of the law from Lindley on Partnership, 12th edition, at page 375 :

"What is meant by the share of a partner is 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 representatives, or to a legatee of his share.... and which on his bankruptcy passes to his trustee."

And, in a later portion of the judgment, summarized the position by stating 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."

8. The Supreme Court held that the partnership assets included immovable properties, the document did not operate as relinquishment of any interest in any of the immovable properties by members of "A" family, but it was merely by way of adjustment of the rights of the partners on dissolution by giving to each his share in the net partnership assets after deduction of liabilities and prior charges and it was, therefore, not compulsorily registrable under section 17(1)(c) of the Registration Act.

9. The same question again arose before the Supreme Court in a different context in Commissioner of Income-tax v. Dewas Cine Corporation ([1968] 68 I. T. R. 240, 243 [1968] 2 S. C. R. 173 (S. C.)). The 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 the partnership as its assets. The business was carried on for some time but, thereafter, the partnership was dissolved and, on dissolution, it was agreed that the theatres should be returned to their original owners and in the books of account of the partnership, the theatres were shown as taken over at the original price less the depreciation allowed during the subsistence of the partnership. The revenue contended on these facts that the assets must in law be deemed to be sold by the partnership to the individual partners in consideration of their respective shares and the difference between the price realised and the written down value should be included in the total income of the partnership under the second proviso to section 10(2)(vii). This contention was negated by the Supreme Court and Shah J., speaking on behalf of the Supreme Court, pointed out that on dissolution of a firm the only right of a partner is "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" and this 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." The learned judge proceeded to observe :

"..... adjudgment of the rights of the partners in a dissolved firm is not a transfer, nor it is 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."

10. The observations, though made in the context of a dissolution of partnership, are equally applicable where a partner retires from the partnership, the last passage quotes by us above from the decision of the Supreme Court in Narayanappa's case (A. I. R. 1966 S. C. 1300).

11. Both these decisions of the Supreme Court were followed by a Full Bench of this court in Velo Industries v. Collector, Bhavnagar ([1971] 80 I. T. R. 291, 297 (Guj) [F. B.]). That was a case under the Bombay Stamp Act, 1958, and the question was as to what is the nature of the transaction when 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 notional sale of the partnership assets and given to him : does it fall within the category of "conveyance on sale" so as to be liable to stamp duty under article 25, clause (b) of Schedule I of the Act ? The Full Bench held that such a transaction does not involve any element of sale of interest of a partner in the partnership assets. Speaking on behalf of the Full Bench, I pointed out, after referring to the decisions in Narayanappa's case (A. I. R. 1966 S. C. 1300) and Dewas Cine Corporation's Case ([1968] 68 I. T. R. 240; [1968] 2 S. C. R. 173 (S. C.)) that where a partner retires from a 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

inproperty 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."

12. These decisions clearly establish that the interest of a partner in the partnership is not interest in any specific item of the partnership property, but as pointed out by the Supreme Court and the Full Bench of this court, it is a right to obtain his share of profits from the time to time during the subsistence of the partnership, to get the value of his share in the net partnership assets which remain after satisfying the debts and liabilities of the partnership. When, therefore, a partner retires from a 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 final sale of the partnership assets and given to him, what he receives is his share in the partnership and not any consideration for transfer of his interest in the partnership to the continuing partners. His share in the partnership is worked out by taking accounts in the manner prescribed by the 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 transfer of interest in the partnership assets by the retiring partner to the continuing partners : vide also the recent decision of the Supreme Court in *Commissioner of Income-tax v. Bankey Lal Vaidya* ([1971] 79 I. T. R. 594; [1971] 3 S. C. R. 406 (S. C.)). It is true that section 2(47) defines "transfer" in relation to a capital asset and this definition given an artificially extended meaning to the term "transfer" by including within its scope and ambit two kinds of transactions which would not ordinarily constitute "transfer" in the accepted connotation of that word, namely, relinquishment of the capital asset and extinguishment of any rights in it. But, even in this artificially extended sense, there is no transfer of interest in the partnership assets involved when a partner retires from the partnership. If relinquishment or extinguishment of interest in partnership assets were involved in the retirement of a partner, the decision in *Narayanappa's case* (A. I. R. 1966 S. C. 1300) could not have been what it was. Section 17(1)(c) of the Registration Act requires compulsory registration of a document where it acknowledges receipt or payment of any consideration not only on account of creation, declaration, assignment or limitation but also on account of extinction of any right, title or interest in immovable property and the document in *Narayanappa's case* (A. I. R. 1966 S. C. 1300) could have, therefore, clearly and indubitably required compulsory registration, if there was any relinquishment or extinguishment of interest of members of "A" family in the immovable properties forming part of the partnership assets. But the Supreme Court held that the transaction merely represented adjustment of the rights of the partners on dissolution and did not involve relinquishment or extinguishment of the interest of member of "A" family in the partnership assets which included immovable properties and the document was, therefore, not compulsorily registrable. It is impossible to contend, in view of this decision of the Supreme Court, that when a partner retires from the partnership, there is relinquishment or extinguishment of his interest in the partnership assets. We must, therefore, hold it to be clear beyond doubt that, even if goodwill be assumed to be a capital asset within the charging provision enacted in section 45, there was, in the present case, transfer of interest of any assessee in the goodwill within the meaning of section 2(47) when the assessee retired from the firm. Each assessee, undoubtedly, received a certain amount on retirement, but this amount represented his share in the net partnership assets after deduction of liabilities and prior charges and it was received in satisfaction of his share in the partnership; each of them

realised his share in the partnership when the amount coming to his share was paid over to him. If there was no transfer of interest of any of the assessee in the goodwill within the meaning of section 2(47), the conclusion must inevitably follow that no part of the amount received by any assessee in respect of his share in the value of the goodwill could be regarded as capital gain chargeable to tax, for under the charging provision enacted in section 45, profit or gain is chargeable to tax as capital gains only if it is profit or gain arising from the "transfer" of a capital asset.

13. But, even if we are wrong in taking this view and the correct view is that when a partner retires from the partnership his interest in the partnership assets is extinguished and there was, therefore, in the present case, "transfer" of interest of each of the assessee in the goodwill when the assessee retired from the firm, the amount received by each assessee in respect of his share in the value of the goodwill must still be held to be outside the pale of chargeability to capital gains tax. It is not every transfer of a capital asset which attracts the charge of capital gains tax. Section 45 which is the charging section, undoubtedly, provides that any profits or gains arising from the transfer of a capital asset shall be chargeable to income-tax under the head "capital gains". But, section 48 shows that the transfer that is contemplated by section 45 is a transfer as a result of which consideration is received by the assessee or accrues to the assessee. Section 48 provides the mode of computation of capital gains by enacting that the income chargeable to tax as capital asset "the following amounts, namely : (i) expenditure incurred wholly and exclusively in connection with such transfer; and (ii) the cost of acquisition of the capital asset and the cost of any improvement thereto. The amounts specified in clauses (i) and (ii) are to be deducted from the "consideration received or accruing as a result of the transfer of the capital assets" for the purpose of determining the profits or gains chargeable to tax. It is, therefore, clear that the transfer of a capital asset, in order to attract the capital gains tax, must be a transfer as a result of which consideration is received by the assessee or accrues to the assessee. If there is no consideration received or accruing to the assessee as a result of the transfer, the machinery section enacted in section 48 would be wholly inapplicable and it would not be possible to compute profits or gains arising from the transfer of the capital asset. The transaction in order to attract the charge of tax as capital gains must, therefore, clearly be such that consideration is received by the assessee or accrues to the assessee as a result of the transfer of the capital asset. Where transfer consists in extinguishment of a right in the capital asset, there must be an element of consideration for such extinguishment, for then only it would be a transfer exigible to capital gains tax. This view is clearly supported by a recent decision given by a Division Bench of this court in *Commissioner of Income-tax v. R. M. Amin* ([1971] 82 I. T. R. 194 (Guj.)). Now, as we have already pointed out above, when a partner retires from a partnership and the amount of his share in the net partnership assets after deduction of liabilities and prior charges is paid to him, what he receives is his share in the partnership which is worked out and realised and it does not represent consideration received by him as a result of the extinguishment of his interest in the partnership assets. Moreover, it is not possible to say, in such a case, that any amount is received by the retiring partner as his share in any particular asset of the firm so that it may be said that a particular part of the amount was received as consideration for the extinguishment of the interest of the retiring partner. The amount he is entitled to get is not merely a share in the partnership assets; he has also to bear his share of the debts and liabilities and it is only his share in the net partnership assets; he has also to bear his share of the debts and liabilities and it is only his share in the net partnership assets after satisfying the debts and liabilities that he is entitled to get on retirement. The debts and liabilities have to be

deducted from the value of the partnership assets and it is only on the surplus that the retiring partner is entitled to claim a share. It is, therefore, not possible to predicate that a particular amount is received by the retiring partner in respect of his share in a particular partnership asset or that a particular amount represents consideration received by the retiring partner for extinguishment of his interest in a particular partnership asset. We are, therefore, of the view that when the assessee retired from the firm, there was no transfer of interest of any of the assessee in the goodwill of the firm and no part of the amount received by any of the assessee was assessable to capital gains tax under section 45.

14. This decision as regards the first contention renders it unnecessary for us to examine the validity of the second contention but since the second contention has been fully argued before us and it raises a question of some importance, we think it desirable to express our opinion upon it. The determination of this contention rests on the construction of a few relevant provisions of the Act. Section 45 which is the general charging section levies the charge of capital gains tax on "any profits or gains arising from the transfer of a capital asset". The expression "capital asset" occurring in this section is defined in section 2(14) to mean :

"2. In this Act, unless the context otherwise, requires, -...

(14)... property of any kind held by an assessee, whether or not connection with his business or profession, but does not include -

(i) any stock-in-trade, consumable stores or raw materials held for the purposes of his business or profession;

(ii) personal effects, that is to say, movable property (including wearing apparel, jewellery and furniture) held for personal use by the assessee or any member of his family dependent on him;

(iii) agricultural land in India;...."

15. The definition brings within the meaning of "capital asset" property of any kind held by an assessee, except that specifically excluded from the definition. The words "property of any kind" are words of widest amplitude; they exclude any limitation which may be sought to be introduced for the purpose of restricting the applicability of the definition. The adverbial clause "whether or not connected with his business or profession" also emphasizes the width and amplitude of the definition. Every kind of property held by an assessee, whatever be its nature or character, is within the connotation of the expression "capital asset" provided of course it does not fall within any of the excepted categories specified in clauses (i) to (iv). Now, it can hardly be disputed that goodwill of a business is "property" recognised by law.

16. The Supreme Court pointed out in *R. C. Cooper v. Union of India* ([1970] 40 Comp. Cas. 325; [1970] 3 S. C. R. 530; A. I. R. 1970 S. C. 564, 611), commonly known as the Bank Nationalisation case ([1970] 40 Comp. Cas. 325; [1970] 3 S. C. R. 530; A. I. R. 1970 S. C. 564, 611) :

"Goodwill of a business is an intangible asset : it is the whole advantage of the reputation and connection formed with the customers together with the circumstances making the connection durable. It is that component of the total value of the undertaking which is attributable to the ability of the concern to earn profits over a course of years or in excess of normal amounts because of its reputation, location and other features : *Trego v. Hunt* ([1896 A. C. 7 (H. L.)). Goodwill of an undertaking therefore is the value of the attraction to customers arising from the name, and reputation for skill, integrity, efficient business management, or efficient service."

17. The Supreme Court held that goodwill of a business is property and it cannot be acquired except on payment of compensation under article 31(2) of the Constitution. It is, therefore, clear that goodwill is a kind of property held by the owner of the business and it is a capital asset within the meaning of section 2(14).

18. It would, therefore, seem that if there is transfer of goodwill any profits or gains arise to the assessee from such transfer, they would be assessable to capital gains tax under section 45. But, what is the meaning of the word "transfer" ? The definition of "transfer" is to be found in section 2(47). We have already referred to that definition earlier and we need not, therefore, reproduce it here. It is sufficient to state that it is a definition which includes within its scope of ambit not only transactions which would constitute transfer according to the accepted connotation of that word, but also transactions which would not ordinarily be regarded as transfer according to its ordinary natural sense. The definition given an extended statutory meaning to the word "transfer" and includes within it relinquishment of a capital asset or the extinguishment of any rights therein. Now, if contrary to the view taken by us, it were held when the assessee retired from the firm, there was a transfer of interest of each of the assessee in the goodwill within the meaning of section 2(47) and the amount representing the value of the share of each assessee in the goodwill was paid to him in consideration of such transfer, the present case would clearly fall within the plain terms of section 45. The whole of the amount received by each assessee in respect of his share in the value of the goodwill would represent his profit or gain arising from the transfer of his interest in the goodwill, since admittedly it did not cost anything to the assessee in terms of money to acquire the goodwill. The question then is : Is there anything in the scheme of taxation relating to capital gains tax or in any other provision of the Act which takes such a transaction outside the scope of ambit of section 45 ?

19. The assessee relied strongly on section 48 in support of their contention that since goodwill did not cost anything to the assessee in terms of money, it was not a capital asset, transfer of which fell within the mischief of the charging provision enacted in section 45. The revenue urged that section 48 clearly postulates that there must be cost of acquisition of the capital asset and, therefore, if there is any capital asset which does not cost anything to the assessee in terms of money to acquire it, it would be outside the scheme of the taxing provisions. Now, we have already referred to section 48 and pointed out that it provides the mode of computation of capital gains. It seeks to arrive at the real profit earned by the assessee from the transfer of the capital asset. It takes the gross receipt of the assessee, namely, the full value of the consideration received or accruing as a result of the transfer of the capital asset, and provides for deduction of certain amounts out of it with a view to arriving at the real profit. One amount is the expenditure incurred wholly and exclusively in connection with the transfer of the capital asset : *vide* clause (i). There can be no doubt that if any

expenditure is incurred wholly and exclusively in connection with the transfer of the capital asset, it must be deducted from the gross receipt in order to ascertain the net profit of the assessee. Obviously, if no such expenditure is incurred, there can be no question of deducting it from the full value of the consideration. Another amount which is to be deducted from the full value of the consideration is "the cost of acquisition of the capital asset" : vide clause (ii). Where the capital asset has cost money to the assessee to acquire it, it must necessarily be deducted from the full value of the consideration in the order to ascertain the net profit earned by the assessee. The object of the charging provision is to tax "profits or gains" and this expression means real or net profits or gains and in order to arrive at real or net profits or gains, the cost which has been incurred by the assessee in acquiring the capital asset must be deducted from the full value of the consideration received by him. Now, one question may arise here for consideration : what is the meaning of the words "acquisition of the capital asset" in this context ? Do they mean only acquisition of the capital asset from a third party or do they also include capital asset created by the assessee ? These words seemed to suggest, according to the assessee, that the capital asset must exist as such at the date when it is acquired and that would be possible only when it is acquired from a third party. Where the capital asset is created by the assessee, as for example where a painting is produced by a painter or a statue chiselled by a sculptor or a building constructed by an owner, it would not be possible to say that the painting is acquired by the painter or the statue is acquired by the sculptor or the building is acquired by the owner. This argument, plausible though acquisition and creation. But, we do not think there is any such antithesis between these two concepts. The word "acquisition" is the noun from the verb "acquired" and the meaning of the word "acquisition". Black's Law Dictionary gives the following meaning of the word "acquire" : "To gain by any means, usually by one's own exertions; to get as one's own; to obtain by search, endeavour, practice, or purchase; receive or gain in whatever manner ; come to have." The word "acquire", accordingly to its plain natural meaning, is a word of very wide import. It is not confined to obtaining of a thing from the third party. When an assessee gains a thing by his own exertions or comes to own it or have it by any recognised mode which would doubtless include the mode of creation, he can be said to have acquired the thing. There are various modes of acquisition by which a thing may be acquired by an assessee and creation is one of them. When an assessee creates a painting, sculpture or a building, he gains it, he comes to have it or to own it. He acquires the painting sculpture or building by creating it. When a capital asset is created by an assessee, it becomes his property, he comes to own it and, therefore, he acquires it the moment it is created. Creation or production of a capital asset is not foreign to the concept of acquisition and even where a capital asset is a self-created asset of the assessee, it would be covered by clause (ii) of section 48 and if any cost has been incurred by the assessee in creating or producing it, it would represent the cost of acquisition of such capital asset and would be deductible from the value of the consideration received by the assessee as a result of transfer of such capital asset, for the purpose of computation of real profit assessable to capital gains tax.

20. But, what would be the position if no cost in terms of money has been incurred by the assessee in acquiring the capital asset, as in the present case, where admittedly creation of the goodwill did not cost anything to the firm and its partners in terms of money ? The argument of the assessee was that where the acquisition of the capital asset has cost nothing to the assessee in terms of money, the capital asset must be held to be outside the net of taxation cast by the taxing provision. Section 48, clause (ii), clearly shows, said the assessee, that the transfer of a capital asset would attract the

capital gains tax under section 45 only if the capital asset has actually cost of the assessee something in terms of money. If the capital asset did not cost anything to the assessee in terms of money in its acquisition, capital gain resulting from its transfer would not be exigible to tax. This contention was sought to be supported by reference to two decisions, one a decision of the Madras High Court in Commissioner of Income-tax v. K. Rathnam Nadar ([1969] 71 I. T. R. 433 (Mad.)), and the other, a decision of the Calcutta High Court in Commissioner of Income-tax v Chunilal Prabhudas and Co. ([1970] 76 I. T. R. 566 (Cal.)). We do not think this contention is well founded. It is based on a misapplication of the provision enacted in section 48, clause (ii). What is provided for in section 48, clause (ii), is deduction of the cost of acquisition of the capital asset and this deduction is for the purpose of arriving at the real profit of the assessee. If the capital asset has not cost anything to the assessee in terms of money and accordingly there was no cost of acquisition of the capital asset to the assessee, there would obviously be nothing to deduct under section 48, clause (ii), and the full value of the consideration received as a result of the transfer of the capital asset would be the real profit or gain of the assessee. It is difficult to see how a provision for deduction of the cost of acquisition of the capital asset can be construed to limit the scope or ambit of the charging provision enacted in section 45. If the provision for deduction applies in a given case, it must be given effect to, but if it does not apply, there would be nothing to deduct. It would indeed be strange logic to hold that the width and amplitude of the charging provision enacted in section 45 must be narrowed and restricted because there may be cases where the provision for deduction of the cost of acquisition of the capital asset is not applicable. The proper way of reading sections 45 and 48 would be that section 45 applies in case of every transfer of a capital asset where there is consideration received or accruing as a result of the transfer of the capital asset and so far as the computation of the real profit arising to the assessee from such transfer is concerned, it has to be made under section 48 by deducting from the full value of the consideration, inter alia, the cost of acquisition of the capital asset, where the capital asset has cost something to the assessee in terms of money. If the argument urged on behalf of the assessee in regard to the cost of acquisition of the capital asset were correct, it would also apply equally in regard to expenditure incurred wholly and exclusively in connection with the transfer and logically it should follow that where no expenditure is incurred wholly and exclusively in connection with the transfer, it would be held to be outside the scope and ambit of section 45. But such an argument would be manifestly unsustainable and if that be so, it must equally be unsustainable in regard to the cost of acquisition of the capital asset. The second part of clause (ii) of section 48 provides that the cost of any improvement of the capital asset should also be deducted from the full value of the consideration. That would also apply where any such cost is incurred by the assessee. If there is no such cost incurred by the assessee, there can be no question of deduction and the provision clearly cannot apply.

21. We cannot, therefore, assent to the argument of the assessee that the charging provision enacted in section 45 is confined only to those cases where the capital asset has cost something to the assessee in terms of money in acquiring it. Even a capital asset which has cost nothing to the assessee in acquiring it would be within the ambit and coverage of the charging provision, provided the conditions for the applicability of the charging provision are satisfied. We have been taken through the other sections of the Act relating to the capital gains tax but we do not find anything in those sections which compel us to give a narrow and constricted meaning to the charging provision enacted in section 45 by excluding self-created capital assets or capital assets which have

cost nothing to the assessee in terms of money in acquiring them. It is true that a different view has been taken by the Madras High Court in K. Rathnam Nadar's case ([1969] 71 I. T. R 433 (Mad.)) in regard to section 12B of the old Income-tax Act, 1922, corresponding to section 45 of the new Act and it has been held that section 12B of the old Act does not apply to transfer of capital assets which did not cost anything to the assessee in terms of money in their creation or acquisition, but with the respect to the learned judges who decided that use we find ourselves unable to accept the reasoning on which it proceeds. The reasoning is the same as that advanced before us with only this difference that whereas reliance is placed in the case before us on section 48, clause (ii), of the new Act, in the case before the Madras High Court reliance was placed on the corresponding provision in section 12B (2), clause (ii), of the old Act which was in almost identical terms. This reasoning is in our opinion defective and does not carry conviction. We have already stated our reasons for saying so.

22. The Calcutta High Court has also taken the view of Chunilal Prabhudas and Co.'s case ([1970] 76 I. T. R. 566, 574 (Cal.)) that profit or gain arising from transfer of goodwill of a business is not chargeable to tax under section 12B of the old Act, firstly, because the provisions of section 12B "do not make it clear..... expressly or by necessary implication that goodwill was at all a contemplated subject of taxable capital 12B does not levy the charge of capital gains tax on self-created assets like goodwill which cost nothing to the assessee in terms of money in their creation or acquisition. But, neither of these two arguments commends itself to us and we find ourselves unable to accept them. So far as the first argument is concerned, we do not find anything in any provision of the Act which militates against the taxability of profit or gain arising from the transfer of goodwill. The question is not whether there is anything in the provisions of the Act which expressly or by necessary implication shows that goodwill was contemplated to be a subject of taxable capital gain. That is, in our opinion, with the greatest respect to the Division Bench of the Calcutta High Court which decided Chunilal Prabhudas and Co.'s case ([1970] 76 I. T. R. 566, 574 (Cal.)), a wrong approach. Goodwill being property is capital asset and if it is transferred and there is in the result profit or gain, it would clearly be taxable under that section, unless we find anything in some other provision of the Act which expressly or by necessary implication shows that goodwill was not intended to be a subject of taxable capital gain. The inquiry must be not whether goodwill is intended to be a subject of taxable capital gain but whether it is intended to be excluded from the charge even though it falls within the plain terms of section 45. The second argument is the same which found favour with the Madras High Court and for reasons which we have already given, we are unable to accept it. The decision of the Calcutta High Court does not, therefore, appeal to us and we cannot accept it as laying down the correct law. We may also in passing refer to a recent decision of the Delhi High Court in Jagdev Singh Mumick v. Commissioner of Income-tax ([1971] 81 I. T. R. 500 (Delhi)) where the same view has been taken by the Delhi High Court in regard to taxability of profit or gain arising on transfer of goodwill of a business. But, this decision merely quotes the relevant passage from the judgment of the Madras High Court in K. Ramthnam Nadar's case ([1969] 71 I. T. R. 433 (Mad.)) and follows it without giving any independent reasoning of its own and it does not, therefore, carry the matter any further.

23. We are, therefore, of the view that though goodwill of a business is a capital asset and profit or gain arising from transfer of goodwill, where there is consideration received or accrued as a result of the transfer is chargeable to capital gains tax under section 45, there was in the present case no

transfer of interest of any of the assessee in the goodwill when the assessee retired from the firm and, in any event, even if there was transfer of such interest, there was no consideration received or accrued as a result of transfer of such interest and no part of the amount received by any of the assessee was, therefore, assessable to capital gains tax under section 45.

24. We, therefore, answer the questions referred to us in each of the four references as under :

Question No. (1) in the affirmative.

Question No. (2) in the affirmative.

Question No. (3) does not arise.

25. The Commissioner will pay the costs of each reference to the assessee.