(2015) 08 BOM CK 0301

Bombay High Court

Case No: Income Tax Appeal No. 40 of 2001

Manish R. Shah		APPELLANT
	Vs	
Income Tax Officer Ward-27(5)		RESPONDENT

Date of Decision: Aug. 6, 2015

Acts Referred:

- Income Tax Act, 1961 - Section 10, 10(3), 260-A, 45, 45(4)

Hon'ble Judges: M.S. Sanklecha and N.M. Jamdar, JJ.

Bench: Division Bench

Advocate: V.B. Joshi, for the Appellant; Suresh Kumar, for the Respondent

Judgement

1. This Appeal under Section 260-A of the Income Tax Act, 1961 (the Act), impeaches the order dated 31st July, 2000 passed by the Income Tax Appellate Tribunal (the Tribunal). The Assessment Year involved is 1992-93.

2. This Appeal was admitted on 1st April, 2004 on the following substantial question of law:--

"Whether on the facts and circumstances of the case and in law, the Tribunal erred in holding that the amount of Rs. 1,75,000/- received by the Appellant at the time of retirement on settlement of his account with the firm was taxable under Section 10(3) of the Act?"

3. The Appellant became a partner in M/s. Omega Research Laboratories (the Firm) w.e.f. 1st April, 1990. The firm was in business as manufacturer and dealers in petroleum and allied product since 1969. The Appellant did not bring in any capital into the firm and was inducted as a working partner, entitled to a share of 35% in the profit of the business.

4. In the year 1991, due to personal reasons, the Appellant had to shift base from Mumbai to Baroda, requiring him to retire from the said firm w.e.f. 1st April, 1991. At the time of retirement, it was mutually decided between the partners that besides

the credit standing to the capital account a further amount of Rs. 5 lakhs be distributed amongst the retiring partners in their profit sharing ratio. This was in the nature of goodwill as the firm has shown the above amount as asset of goodwill in its Balance Sheet as on 31st March, 1992. Consequently, in terms of Deed of Partnership-cum-Retirement Deed dated 3rd April, 1991, the Appellant received the amount standing to its credit in the capital account as well as the sum of Rs. 1,75,000/- being the amount contributed to the goodwill of the firm by him, payable out of Rs. 5 lakhs being distributed amongst the retiring partners in the profit sharing ratio. In its return of income for the relevant Assessment Year 1992-93, the Appellant had appended a note that a sum of Rs. 1,75,000/- received from the said firm on full and final settlement of his account and the same has been deposited in IDBI Capital Bonds.

5. The Assessing Officer by his order dated 27th December, 1994 did not accept the Appellant''s contention that the above amount of Rs. 1,75,000/- is not taxable as it was a capital receipt. It taxed an amount of Rs. 1,70,000/- out of Rs. 1,75,000/- as casual and non-recurring receipt under Section 10(3) of the Act by relying upon the decision of the Allahabad High Court in Gulabchand v. CIT 192 ITR 549.

6. Being aggrieved by the order of the Assessing Officer dated 27th December, 1994, the Appellant preferred an appeal to the Commissioner of Income Tax (Appeal) [CIT(A)]. On consideration of the facts involved by an order dated 1st September, 1995, the Appeal of the Appellant was allowed, inter alia holding that the amount of Rs. 1,75,000/- received by the Appellant cannot be subjected to tax under Section 10(3) of the Act. This inter alia, on the ground that the amount received by the Appellant as retiring partner, was goodwill attributable to Appellant i.e. the income earning capacity of the firm. Consequently, holding that Section 10(3) of the Act would not no application as it is not casual and non-recurring receipt. Further, in the alternative, it was held that the issue stands concluded by the decision of the Supreme Court in Additional CIT, Gujarat v. Mohanbhai Pamabhai 165 ITR 166 to hold that what has been received on retirement by the Appellant cannot be subjected to tax as what is received by the partner is his share in partnership firm and there is no income.

7. Being aggrieved, the Revenue carried the issue in appeal to the Tribunal. By the impugned order dated 31st July, 2000, the Appeal was allowed by holding that the Appellant had been partner of the firm only for a period of one year and goodwill is built generally over a period of time. Thus, the amount received of Rs. 1,75,000/- was on capital account. Further, reliance was placed upon clauses of the agreement dated 3rd April, 1991 titled as Deed of Partnership-cum-Retirement which does not provide for payment of goodwill. Consequently, the impugned order held that the amount received to be casual and non-recurring receipt hit by Section 10(3) of the Act.

8. For proper adjudication of the dispute before dealing with the submission made on behalf of the parties, it would be useful to reproduce Section 10(3) of the Act as in force in the subject Assessment Year;-

"Section 10 :-- In computing the total income of the previous year of any person, any income following within any of the following clauses shall not be included:--

(3)(1)&(2) any receipts which are of a causal and nonrecurring nature to the extent such receipts do not exceed five thousand rupees in the aggregate:

Provided that where such receipts relate to winnings from races, the provisions of this clause shall have effect as if for the words "five thousand rupees" the words "two thousand five hundred rupees" had been substituted: Provided further that this clause shall not apply to-

(i) capital gains chargeable under the provisions of section 45 ; or

(ii) receipts arising from business or the exercise of a profession or occupation; or

(iii) receipts by way of addition to the remuneration of an employee."

9. Mr. Joshi, learned Counsel appearing for the Appellant made following submissions:--

"(a) The impugned order of the Tribunal setting aside the order of the CIT(A) to hold that the amount of Rs. 1.75 lakhs paid to the Appellant cannot be attributed to the goodwill belonging to the Appellant in the firm is without any evidence. It proceeds merely on the basis of assumption and presumptions;

(b) Section 10(3) of the Act would have no application when the amount received are chargeable to tax under the head ''Capital gains'' as provided under Section 45 of the Act; and

(c) The amount received by a partner on his retirement are in the nature of capital receipt and the tax on the same is to be discharged by the Appellant under Section 45(4) of the Act is a settled position in view of the decision of Apex Court in Prashant S. Joshi Vs. The Income Tax Officer and Union of India (UOI), ."

10. As against the above, Mr. Suresh Kumar, learned Counsel appearing for the Revenue in support of the impugned order submits as under:--

"(a) The impugned order of the Tribunal calls for no interference as the same is a well reasoned order;

(b) The amount received by the Appellant is not on capital account as it is income under goodwill. This is because, the Appellant has not contributed in any manner and the goodwill of the firm having been a partner only for one year; and

(c) The decision of the Apex Court in Mohanbhai Pamabhai (supra) would have no application as the present case dealt with a retirement of a partner and not

dissolution of the firm consequently Section 45(4) of the Act being relied upon by the Appellant, is without basis."

11. The Assessing Officer has taxed an amount of Rs. 1,70,000/- out of Rs. 1,75,000/- received by the Appellant on his retirement from the firm w.e.f. 1st April, 1991. This on the ground that it is casual and nonrecurring. Further, he holds it is a capital receipt or a capital gain.

12. The crux of the dispute is the application of Section 10(3) of the Act to the present facts. A bare analysis of Section 10 of the Act would reveal that the incomes specified therein are not to be included in the total income. Amongst the income listed in sub-section 3 thereof is any receipt which is not in excess of Rs. 5,000/- in the aggregate when they are casual and non-recurring in nature. Further, this clause would have no application in case they arise out of capital gains chargeable to tax under Section 45 of the Act or arise from exercise of business or profession.

13. In the present case, the CIT(A) held that the amount of Rs. 1,75,000/- paid by the firm to the Appellant was the amount of goodwill in the firm attributable to the Appellant. This payment of goodwill is as held by the CIT(A) not a casual receipt. Thus, not taxable under Section 10(3) of the Act. Alternatively, it held that in view of the decision of the Apex Court Mohanbhai Pamabhai (supra), it cannot be taxed as capital gains. On further appeal, the Tribunal by the impugned order has set aside the order of the CIT(A) by holding that the amount of Rs. 1,75,000/- received by the Appellant is not on account of goodwill. This conclusion was arrived at by proceeding on the basis of goodwill cannot be generated within a period of one year. Besides, the Appellant is not entitled to the goodwill as he had not contributed any capital when he came into the firm. Further, reliance is placed upon certain clauses of a Deed of Partnership-cum-Retirement dated 3rd April, 1991 to conclude that the amount of Rs. 1,75,000/- is not an amount received as goodwill.

14. We find substance in the submission of Mr. Joshi, the learned Counsel appearing for the Appellant that the impugned order has proceeded on mere assumptions and presumptions to conclude that no goodwill could have been generated by the Appellant. The first presumption is that goodwill cannot be generated within one year. No basis for this conclusion. No universal rule of time taken to generate goodwill. It differs from business to business, besides upon the ability of the person doing the business. Second presumption that Appellant not entitled to goodwill as did not contribute any capital. No basis for this conclusion. In this case, the Appellant joined the business as working partner and his contribution was in running the business by which he would have contributed to goodwill of firm. Third presumption that retiring partners would have no right to a goodwill of a business as that is available only when the business is sold as whole and continuing entity. We are at a loss from where does the Tribunal gets this position in law. Lastly, the impugned order relies upon the Deed of Partnership-cum-Retirement dated 3rd April, 1991 and in particular clause 15 thereof which states that no goodwill will

accrue to or belong to a retiring partners. This clause dealt with the re-constituted firm which came into force on 3rd April, 1991. It was clauses 1 to 7 of the Agreement dated 3rd April, 1991 which dealt with the erstwhile partnership firm from which the Appellant retired. In clause 5 thereof, it has been specifically provided that:--

" ....

The retiring partners and continuing partner of the old firm shall be paid a sum of Rs. 5,00,000/- in addition to the amounts standing to the credit of their capital account as on 31st March, 1991. It is further agreed that the said sum of Rs. 5,00,000/- shall be distributed amongst the Retiring Partners and Continuing Partner in their respective Profit sharing ratio of the old firm. The Retiring Partners shall not have any right whatsoever in the assets of the said Partnership."

The aforesaid clause was completely ignored by the impugned order of the Tribunal.

15. In the circumstances, the impugned order upsetting the finding of the CIT(A) is on a factually erroneous basis as pointed out herein above and cannot be sustained. The fact that the amount of Rs. 1,75,000/- paid to the Appellant by the firm was in the nature of payment of goodwill is also supported by the fact that the firm considered only the amount of Rs. 1,75,000/- being a part of Rs. 5 lakhs as attributable to Appellant goodwill. This amount was on account of having paid the retiring partners their contribution to the goodwill of the firm. Accordingly, we hold that the amount of Rs. 1,75,000/- paid to Appellant is goodwill. Once we reach a conclusion that the amount of Rs. 1,75,000/- was received by the Appellant in consideration of the goodwill left behind in the firm, then without anything more, the receipt of the above amount cannot be said to be casual for the purposes of Section 10(3) of the Act. In fact, the CIT(A) in his order holds that the amount received by the Appellant being a portion of the goodwill, cannot be said to be casual. The goodwill the firm possesses is inherent in it. It is at the time when the Appellant retired that the same was quantified to enable the firm to exploit the goodwill left behind by the retiring partner. For the purposes of Section 10(3) of the Act applying not only should the receipt qualify as income but it has also to be casual and non-recurring. The word ''casual'' came up for consideration in Rm. Ar. Ar. Rm. Ar. Ramanathan Chettiar Vs. Commissioner of Income Tax, Madras, and observed as under:--
"The expression casual has not been defined in the Act and must therefore be construed in its plain and ordinary sense. According to shorter oxford English Dictionary, the word ''casual'' is defined to mean "(i) subject to or produced by chance; accidental, fortuitous, (ii) coming at uncertain time; not to be calculated on, unsettled." A receipt of interest which is foreseen and anticipated cannot be regarded as casual even if it is not likely to recur again."

Therefore, the amount of Rs. 1,75,000/- received by the Appellant not being casual as it was always foreseen and anticipated prior to retirement. It has only been

quantified at the time of retirement of the Appellant. Thus, the receipt is not hit by Section 10(3) of the Act.

16. Before parting, we would like to clarify that because of the view we have taken on the above issue, it is not necessary to deal with the other submissions made by the parties.

17. Accordingly, we answer the substantial question of law framed for our consideration in the affirmative i.e. in favour of the Appellant- Assessee and against the Respondent-Revenue.

18. Appeal disposed of in the above terms. No order as to costs.