

(1987) 04 BOM CK 0058

Bombay High Court

Case No: Wealth-tax Reference No. 91 of 1975

Commissioner of Wealth-tax

APPELLANT

Vs

V.M. Shah

RESPONDENT

Date of Decision: April 6, 1987

Acts Referred:

- Income Tax Act, 1961 - Section 36
- Wealth Tax Act, 1957 - Section 2, 3, 5, 7, 7(1)
- Wealth Tax Rules, 1957 - Rule 2(1), 2A, 2C

Citation: (1987) 63 CTR 225 : (1988) 170 ITR 17

Hon'ble Judges: T.D. Sugla, J; Bharucha, J

Bench: Division Bench

Judgement

Bharucha, J.

This reference concerns the uncollected fees of a practising chartered accountant and the issue to be considered is whether these fees form an asset upon which wealth-tax may be collected. The questions raised at the instance of the Revenue read thus :

"(1) Whether, on the facts and in the circumstances of the case, the Wealth-tax Officer was entitled to include the outstanding fees in the balance-sheet ?

(2) If question No. (1) is answered in the affirmative, whether liabilities should also be adjusted in the balance-sheet on accrual basis ?"

2. The assessment years with which we are concerned are the assessment years 1964-65 to 1969-70. The assessee was during the previous years relevant to these assessment years, a partner of the firm of M/s. C. M. Shah & Co., Chartered Accountants, and had a 45% share therein. The firm maintained its accounts on cash basis and upon that basis, drew up its balance-sheets and profit and loss accounts for the years under reference. In his wealth-tax returns for these years, the assessee

valued his 45% share in the firm on the basis of the balance-sheets. The Wealth-tax Officer required the assessee to inform him of the approximate amount of the outstanding bills of the firm at the end of each of the two accounting years. The Wealth-tax Officer included 45% of the figures estimated by the assessee in this behalf in the assessee's net wealth. He did not make any other adjustments in the value of the assessee's share in the firm.

3. The assessee preferred appeals to the Appellate Assistant Commissioner. He excluded the additions made by the Wealth-tax Officer.

4. The Revenue carried the matter to the Income Tax Appellate Tribunal. The Tribunal, following the judgment of the Orissa High Court in [Commissioner of Wealth Tax Vs. Vysyaraju Badreenarayanamoorthy Raju](#), upheld the order of the Appellate Assistant Commissioner and dismissed the appeals.

5. Section 2(e) of the Wealth-tax Act, 1957, defines "assets" as "property of every description, movable or immovable". Section 3 charges to wealth-tax, the net-wealth of the assessee. Section 7, sub-sections (1) and (2)(a) are very relevant and read thus :

"7. Value of assets how to be determined. - (1) Subject to any rules made in this behalf, the value of any asset, other than cash, for the purposes of this Act, shall be estimated to be the price which in the opinion of the Wealth-tax Officer it would fetch if sold in the open market on the valuation date.....

(2) Notwithstanding anything contained in sub-section (1), -

(a) where the assessee is carrying on a business for which accounts are maintained by him regularly, the Wealth-tax Officer may, instead of determining separately the value of each asset held by the assessee in such business, determine the net value of the assets of the business as a whole having regard to the balance-sheet of such business as on the valuation date and making such adjustments therein as may be prescribed..."

6. Rule 2 of the Wealth-tax Rules, 1957, deals with the valuation-of interest in partnership. Sub-rule (1) thereof is relevant and may be quoted :

"2. (1) The value of the interest of a person in a firm of which he is a partner or an association of persons of which he is a member, shall be determined in the manner provided herein. The net wealth of the firm or the association on the valuation date shall first be determined. That portion of the net wealth of the firm or association as is equal to the amount of its capital shall be allocated among the partners or members in the proportion in which capital has been contributed by them. The residue of the net wealth of the firm or association shall be allocated among the partners or members in accordance with the agreement of partnership or association for the distribution of assets in the event of dissolution of the firm or association, or, in the absence of such agreement, in the proportion in which the

partners or members are entitled to share profits. The sum total of the amounts so allocated to a partner or member shall be treated as the value of the interest of that partner or member in the firm or association."

7. Rules 2A and 2C read thus :

"2A. Determination of the net value of assets of business as a whole. - Where the Wealth-tax Officer determines under clause (a) of sub-section (2) of section 7, the net wealth of the assets of the business as a whole having regard to the balance-sheet of such business, he shall make the adjustments specified in rules 2B, 2C, 2D, 2E, 2F and 2G."

"2C. Adjustments in the value of an asset not disclosed in the balance-sheet. - The value of an asset not disclosed in the balance-sheet shall be taken to be -

(a) in the case of a debt due to the assessee, the amount due to the assessee under that debt, and where such amount or part thereof has been allowed as a deduction under clause (vii) of sub-section (1) of section 36 of the Income Tax Act, 1961, in computing the total income of the assessee for the relevant year for the purposes of assessment under that Act, the amount of the debt as reduced by the deduction to be allowed;

(b) in the case of goodwill purchased by the assessee for a price, its market value or the price actually paid by him, whichever is less;

(c) in the case of managing agency rights purchased by the assessee for a price, its market value or the price actually paid by him, whichever is less;

(d) in the case of any other asset, its market value on the valuation date."

8. It is interesting to note that in section 5 which deals with exemptions in respect of certain assets, clause (xa) was introduced by the Finance Act, 1983, with effect from April 1, 1984. It states :

"in the case of an assessee who is carrying on a profession (being legal, medical, engineering or architectural profession or the profession of accountancy or such other profession as is notified by the Central Government in this behalf) and who regularly maintains books of account on the cash system of accounting, the amount of any fee due to him in respect of the service rendered by him in such professional capacity."

9. Mr. Jetly, learned counsel for the Revenue, submitted that the answer to the questions was squarely covered by the decision of the Supreme Court in [Commissioner of Wealth-tax, Orissa Vs. Vysyaraju Badreenarayana Moorthy Raju](#), . (This was the appeal from the judgment of the Orissa High Court upon which the Tribunal had based its decision.) The question to be considered in this case was whether the Wealth-tax Officer was justified in including in the net wealth of the assessee interest due on accrual basis (though not realised) on the outstandings of

his money-lending business, the accounts of the assessee being maintained on cash basis. The Supreme Court noted that u/s 3, wealth-tax was charged for a full assessment year in respect of the net wealth of the assessee on the corresponding valuation date. The definition of the expression "net wealth" was noted as also the definition of the expression "valuation date". The Supreme Court said that the computation of the net wealth of an assessee called for a determination of his assets and debts as on the valuation date. The last date of the previous year as defined under the Income Tax Act was the valuation date. The figure of net wealth of the assessee at the end of the previous year took into account the financial activities of the assessee during that previous year. His financial activities during that period determined how his net wealth on a particular valuation date differed from his net wealth on the immediately preceding valuation date. The system of accounting, mercantile or cash or hybrid, was of no relevance for the purpose of determining the assets of the assessee. That appeared to be plain from the definition of "net wealth" which spoke of "the aggregate value... of all the assets" belonging to the assessee on the valuation date. All the assets of the assessee, barring those expressly excepted by the statute, were to be taken into account, and it was immaterial whether the assessee employed one system of accounting or another. There was clear indication that the assets to be considered were not circumscribed by any consideration of the particular system of accounting adopted by the assessee. The assets were not confined to cash. Where the asset was an asset other than cash, its value if determined pursuant to sub-section (1) of section 7, was the estimated price, which, in the opinion of the Wealth-tax Officer, the asset would fetch if sold in the open market on the valuation date. In other words, it would be the estimated open market value of the rights in the property which constituted the asset. When one spoke of the value of a property, on a legal plane, one referred to the value of the rights in that property. It was apparent that what accrued as a right also fell to be included within the assets of an assessee under the Act. That being so, the conclusion was inescapable that even though the accounts of the assessee were maintained on cash basis, interest due on accrual basis, though not realised, on the outstandings of the money-lending business were liable to be included in the net wealth of the assessee. Taking this view, the Supreme Court overruled several judgments, including, of course, the judgment of the Orissa High Court.

10. Mr. Palkhivala, learned counsel for the assessee, attempted to distinguish the aforementioned judgment by suggesting that it was delivered in a case where the provisions of section 7(1) had been applied. There is a misapprehension here. A reading of the judgment of the Orissa High Court shows that it was a case where the provisions of section 7(2)(a) had been applied. In any event, the Supreme Court's judgment is cast in wide terms and would apply regardless of whether the assessment was made under the provisions of section 7(1) or (2).

11. Mr. Palkhivala drew our attention to rule 2A whereunder, when the Wealth-tax Officer determines u/s 7(2)(a), as here, the net value of the assets of the business as

a whole, having regard to its balance-sheet, he is obliged to make the adjustments set out in rules 2B to 2G. Rule 2C is what is relevant here. It sets out what the value of an asset not disclosed in the balance-sheet should be taken to be. Provision is expressly made in respect of debts due to an assessee, goodwill purchased by an assessee and managing agency rights purchased by an assessee. In any other case, it is provided that the value of the undisclosed asset should be taken to be its market value on the valuation date. Mr. Palkhivala laid stress on the words "assets not disclosed in the balance-sheet", and, particularly, the word "disclosed". In his submission, rule 2C could only be applied in regard to an asset which ought to have been disclosed in the balance-sheet but had not been disclosed. "Disclosed", in his submission, implied, in the context, that the asset ought to have been disclosed in the balance-sheet according to the ordinary principles of accounting. Thus, the sale price of immovable property would be required to be disclosed in a balance-sheet kept on cash basis, though not realised, because it related to the capital account. This did not apply to fees for professional services rendered which had not been received. They were not required to be disclosed because they related to income and, on cash basis, income which had not been received was not liable to be shown in the balance-sheet.

12. Income not received is not liable to be shown in the balance-sheet maintained on cash basis (See [Raja Mohan Raja Bahadur Vs. The Commissioner of Income Tax, U.P.](#)). The point really is whether the words "asset not disclosed in the balance-sheet" can be read in the manner in which Mr. Palkhivala invites us to do. u/s 2(e), assets include property of every description, movable or immovable. What has to be seen in the context of rule 2C, in our opinion, is whether any asset has not been shown in the balance-sheet. If there is an asset as defined and it has not, for good reason or otherwise, been shown in the balance-sheet, the Wealth-tax Officer is entitled to apply the provisions of rule 2C. The word "disclosed" therein only means shown. It must follow that the Wealth-tax Officer was entitled in the instant case to apply the provisions of rule 2C. It may well be true that, upon this interpretation, the assessee would not be entitled to claim a deduction in respect of his Income Tax liability upon the outstanding fees and that he would, therefore, be taxed on an amount of wealth which is unrealistic. Even so, we cannot place upon the word "disclosed" in rule 2C any meaning other than its ordinary dictionary meaning.

13. Mr. Palkhivala fairly stated that he would not press for an answer to the second question.

14. In the result, the first question is answered in the affirmative and in favour of the Revenue.

15. No order as to costs.