BOMBAY HIGH COURT

Commissioner of Income-Tax

Vs

Home Industries

(V Tulzapurkar, C.J. Desai, J.)

25.02.1977

JUDGMENT

Tulzapurkar, Actg. C.J.

1. In this reference made by the Income-tax Appellate Tribunal under section 66(1) of the Indian Income-tax Act, 1922 the following question has been referred to us for our determinatio :

> "Whether, on the facts and in the circumstances of the case, there is any transfer or sale of goodwill to the private limited company so as to attract section 12B(1) of the Indian Income-tax Act, 1922 ?"

2. The, question relates to the assessment year 1960-61, the previous year being the period from January 1, 1959, to April 9, 1959. The assessee-firm, M/s. Home Industries & Co., consisting of three partners with equal shares was constituted on January 2, 1947, to carry on the business of manufacturing and selling of textile auxiliaries and certain chemicals on terms and conditions recorded in the deed of partnership executed by the three partners on December 9, 1949. From April 19 his business was taken over by a private limited company (M/s. Hico Products Private Ltd.,) with all assets and liabilities and goodwill. The assets and liabilities of the firm were transferred to the limited company at book value while the goodwill was valued at Rs. 4,89,000. Initially there was no goodwill account in the books of the firm but, at the time of the transfer, goodwill account was debited in the books with Rs. 4,89,000 and each of the partners' account was credited with Rs. 1,63,000 representing each one's share in the goodwill. In other words, the consideration for the goodwill was divided equally between the three partners. The capital of the private limited company (M/s. Hico Products Pvt. Ltd.,) was Rs. 5 lakhs divided into 5,000 ordinary shares of Rs. 100 each; 4,998 shares were distributed among the three partners, each one being allotted 1,666 shares while the remaining 2 shares were allotted to and held by two persons (one each) as the nominees for all the three partners. A declaration was also filed before

the Registrar of Companies showing the two persons as the nominees.

3. On the aforesaid facts in the assessment for 1960-61 (accounting period being January 1, 1959, to April 9, 1959) a question arose whether the aforesaid transaction was liable to tax on capital gains under section 12B of the Indian Income-tax Act, 1922. On behalf of the assessee-firm it was claimed that there was no transfer or sale of any capital the company was substantially and really a mere readjustment made by the partners to enable them to carry on their business as a company rather than as a firm and no profit or gain in the commercial sensea was made by thereby, and in support of such claim reliance was placed on the two decisions of this *cour : Commissioner of Income-tax v. Sir Homi Mehta's Executors*[1] and *Rogers & Co. v. Commissioner of Income-tax*[2] The Income-tax Officer negatived the claim made on behalf of the assessee and in doing so distinguished the two decisions, particularly the latter, on facts. He held that the capital gains arising from the transfer of goodwill was taxable. He computed the assessable capital gain at Rs. 3,64,830 after deducting the value of goodwill as on January 1, 1954, valued at Rs. 1,24,170. This assessment, on appeal, was confirmed by the Appellate Assistant Commissioner. The assessee-firm carried the matter in further appeal to the Tribunal. Before the Tribunal the self-same contention was raised, namely, that the transaction of formation of a private limited company by the erstwhile partners and vesting of assets in the company was merely a procedure adopted for readjustment of the business position of the partners and that no profit or gain in the commercial sense arose and that the two decisions cited above fully covered their case. On behalf of the revenue it was contended that the transactions of the company were the real transactions, that the transfer of assets resulted in gain as shown by the accounts and that the two decisions relied upon were not applicable to section 12B. The Tribunal, following the ratio of the two decisions cited on behalf of the assessee-firm, held that there was no sale or transfer within the scope of section 12B(1) of the Act in this case and that there was no profit or gain in the transaction under consideration. The Tribunal further held that the provisions of section 12B(1) were not applicable and, therefore, directed that the sum of Rs. 3,64,830 should be deleted from the assessment. At the instance of the Commissioner of Income-tax the question set out at the commencement of this judgment has been referred to us by the Tribunal for our opinion.

4. Mr. Joshi appearing for the revenue has pointed out that the view taken by this court in the case of Sir Homi Mehta's Executors [1955] 28 ITR 928 (Bom)(SUPRA)and in the case of *Rogers and Co. v. Commissioner of Income-tax [1958] 34 ITR 336 (Bom)(SUPRA)* has been expressly disapproved by the Supreme Court in circumstances of *Income-tax v. B M Kharwar and* as such the view taken by the Tribunal in the instant case which is based upon the aforesaid two decisions of this court would not be sustainable. He pointed out that in Kharwar's case the

Supreme Court has taken the view that where machinery of a factory belonging to a firm is transferred to a private limited company, assuming that thereby readjustment of the business relationship was intended, the liability to be taxed under the second proviso to section 10(2)(vii) of the Indian Income-tax Act, 1922, in respect of the readjustment has to be determined according to the strict legal form of the transaction; that the company is a legal entity distinct from the partnership under the general law, the transfer of the machinery is by the firm to the company, and the legal effect of the transaction is to convey for consideration the rights of the firm in the machinery to the company and that if the transaction results in excess realisation over the written down value of the machinery to the firm., the liability to tax, if any, arising under the Act cannot be avoided merely because in consequence of the transfer the interest of the partners in the machinery is substituted by the interest in the shares of the partners in the machinery is substituted by the interest in the shares of the company which owned the machinery. He also pointed out that the Supreme Court has made general observations in this case to the effect that the Supreme Court has made general observations in this case to the effect that it is now well settled that the taxing authorities are not entitled, in determining whether a receipt is liable to be taxed, to ignore the legal character of the transaction which is the source of the receipt and to proceed on what they regard as "the substance of the matter"; the taxing authority is entitled, and is indeed bound to determine the true legal relation resulting from a transaction. If the parties have chosen to conceal by a device the legal relation, it is open to the taxing authorities to unravel the device and to determine the true character of the relationship. But the legal effect of a transaction cannot be displaced by probing into the "substance of the transaction", and this principle applied alike to cases in which the legal relation is recorded in a formal decided oncument, and to cases where it has to be gathered from evidence order and documentary-and conduct of the parties to the transaction. Relying on this decision Mr. Joshi contended before us that the ratio of the two Bombay decisions, which had been applied by the Tribunal to the instant case arising under section 12B of the Act, itself having been disapproved by the Supreme Court, the view of the Tribunal that there was no transfer or sale of the goodwill in the commercial sense in the instant case will have to be rejected and the question referred to us will have to be answered in the affirmative and in favour of the revenue.

5. Mr. Dastur, appearing for the assessee, fairly conceded before us that in view of the Supreme Court decision in Kharwar's case the view of the Tribunal that there was no transfer or sale of goodwill to Hico Products Pvt. Ltd., in the commercial sense and that there was no question of capital gain arising to the assessee-firm will have to be regarded an unsustainable. But, according to him, that would to be the end of the matter, for he urged that the ultimate order of the Tribunal that the sum of Rs. 3,64,830 representing the so-called capital gain is not liable to be included in the assessment is sustainable on another ground. He urged that a self-generated or self-created

goodwill is not a capital asset, the transfer of which will give rise to chargeable capital gain, having regard to the scheme of section 12B of the Indian Income-tax Act, 1922, which implies that there should be acquisition of an asset at the given point of time and for some monetary cost and he urged that since in the instant case no goodwill been gifted to it but it was generated or earned and came into existence as a result of efforts and trading activities of the assessee-firm, there was no actual cost of that asset to the assessee that could be deducted from the consideration received by the assessee-firm from the private limited company for the transfer of goodwill and, therefore, no chargeable capital gains could be said to have been made by the assessee-firm when it transferred the goodwill of the firm to a private limited company. According to Mr. Dastur, the Tribunal's final order deleting the amount of Rs. 3,64,830 from the assessment of the assessee-firm could be sustained on this ground. Mr. Joshi for the revenue raised a preliminary objection that such a ground was neither raised before the Tribunal nor was it dealt with by the Tribunal nor had it been referred by the Tribunal to this court, and as such the assessee-firm should not be allowed to raise the same for the first time in this reference before this court. It is not possible to uphold this objection of Mr. Joshi for the simple reason that though it is true that such a ground was not raised before the Tribunal and had not been dealt with by it, it cannot be said that it is not covered by the question that has been framed and referred to us by the Tribunal. In our view, the form in which the question has been framed is sufficiently wide to take in this ground and the assessee-firm would be entitled to raise it before us. The question as framed runs thus

6. "Whether, on the facts and in the circumstances of the case, there is any transfer or sale of goodwill to be private limited company so as to attract section 12B(1) of the Indian Income-tax Act, 1922 ?" and in our view, the question thus framed not merely touches the aspect as to whether there is any "transfer or sale" of the goodwill to the private limited company under the transaction in question but also embraces the aspect as to whether there is capital gains tax liability at all and this is implicit in the words "so as to attract section 12B(1) of the Act" occurring in the question. Moreover, the new ground raised by Mr. Dastur is nothing but another aspect of the principal as to whether the assessee-firm could be said to have dealt with a capital asset, the transfer of which will give rise to chargeable capital gains justifying the addition of Rs. 3,64,830 in the assessable income of the assessee-firm and the contention raised by Mr. Dastur being purely a legal contention which is capable of being disposed of on a consideration of the legal provision contained in section 12B of the Act and on the facts which are already on record, we do not see any reason why the should not be allowed to raise this new ground. The only additional material that was taken on record, we do not see any reason why the assessee should not be allowed to raise this new ground. The only additional material that was taken on record by us was a true copy of the deed of partnership dated December 9, 1949, recording the terms and

conditions on which the three partners of the assessee-firm had agreed to and did carry on their business and that was merely for the purpose of confirming the position that the partnership business had been commenced by the three partners in January, 1947, a fact clearly mentioned in the statement of case. We must mention here that Mr. Joshi for the revenue in all fairness consented to such copy of deed of partnership going on record, which we have marked, by consent of parties, as exhibit D-1 in the reference.

7. It is well-settled position that when the main question is under issue before the Tribunal there is no further limitation imposed by section 66(1) of the Act that the reference should be limited to those aspects of the question which had been argued before the Tribunal and if a different aspect of the same question is sought to be raised for the first time before the High Court, it would be permissible to the High Court to allow such aspect being argued before it even if that aspect has not been argued before the Tribunal. If necessary, a reference may be made to two decisions of the Supreme Court, one in *Ogale Glass Works Ltd.,'s case*[3] and the other in Scindia Steam Navigation Co. Ltd.,'s case and in particular the following observations of the Supreme Court in the latter case appearing at page 612 are apposit :

> "Now a question of law might be a simple one, having its impact at one point, or it may be a complex one, trenching over an area with approaches leading to different points therein. Such a question might involve more than one aspect, requiring to be tackled from different standpoints. All that section 66(1) requires is that the question of law which is referred to the court for decision and which the court is to decide must be the question which was in issue before the Tribunal. Where the question itself was under issue, there is no further limitation imposed by the section that the reference should be limited to those aspects of the question which had been argued before the Tribunal. It will be an over-refinement of the position to hold that each aspect of a question is itself a distinct question for the purpose of section 66(1) of the Act. That was the view taken by this court in *Commissioner of Income-tax v. Ogale Glass Works Ltd., [1954] 25 ITR 529 (SC(Supra))* and in *Zoraster & Co. v. Commissioner of Income-tax an*d we agree with it. As the question on which the parties were at issue, which was referred to the court under section 66(1) and decided by it under section 66(5), is whether the sum of Rs. 9,26,532 is liable to be included in the taxable income of the respondents, the ground on which the respondents contested their liability before the High Court was one which was within the scope of the question, and the High Court rightly entertained it."

8. Coming to the merits of the point on brhslf of the sssessee-firm, Mr. Dastur has stated that two factual aspects become clear in view of the two documents on record, the deed of partnership dated December 9, 1949, and the agreement for sale dated April 9, 1959, whereunder the entire

business together with its goodwill was transferred by the assessee-firm to the private limited company, M/s Hico Products Pvt. Ltd., namely, (a) it is not a case where the assessee-firm had purchased for consideration any goodwill or had obtained it under any gift but the assessee-firm after commencing its business from January 2, 1947, onwards had built it up by its own exertion and trading activities, and (b) there was initially no goodwill account in the books of the firm but only on conversion the goodwill was valued at Rs. 4,89,000 and the goodwill account was debited in the books, with the partners' accounts being credited with Rs. 1,63,000 each, representing each one's share in goodwill and, according to him, the question at issue will have to be considered having regard to these aforesaid admitted facts which appear clear on record. He contended that though the goodwill of the firm would fall within the definition of "capital asset" as given in section 2(4A) of the 1922 Act, a self-created or self-generated goodwill (which it is in the instant case) would not be capital asset the transfer of which will give rise to the chargeable capital gain because, according to him, to attract capital gains the asset must be capable of being held by the assessee independently, must be capable of independent transfer and must be such as can be said to have been acquired at a given point of time for certain actual cost expressed in monetary terms and these aspects become clear if the scheme of section 12B of the 1922 Act is carefully analysed. he pointed out that section 12B, which deals with taxation of capital gains, makes it very clear that the capital asset, capital gains arising from the sale or transfer of which is sought to be taxed thereunder, must be an asset which is capable of being acquired at a given point of time and for a cost expressed in monetary terms. He also urged that the scheme of the said section does not imply taxation of gross receipts upon transfer of the asset but merely the profit or gain arising upon such transfer. According to him, further, the scheme of the section also implies an identifiable asset capable of identifiable improvement and assessment of cost relatable to such improvement. In this behalf he particularly relied upon the provisions contained in section 12B(1) and (2) together with the provisos thereto of the 1922 Act. He also emphasised that the position was the same even under the relevant sections of the Income-tax Act 1961. He, therefore, urged that since in the instant case, the goodwill of the assessee-firm could not be said to be a capital asset which had been acquired at a given point of time or which could be said to have been acquired for some cost expressed in monetary terms, the transfer thereof under the transaction in question would not give rise to chargeable capital gains. In support of his aforesaid submission he placed reliance upon the decisions of five different High Courts which have taken the view that a self-created or self-generated goodwill upon its transfer will not attract the capital gains tax liability, namely *Commissioner of Income-tax v. K Rathnam Nadar*[4] decided by the *Madras High Court, Commissioner of Income-tax v. Chunilal Prabhudas & Co*[5]. decided by the Calcutta High Court, Jagdev Singh Mumick v. Commissioner of Income-tax , decided by the Delhi High Court, the Full Bench decision of the Kerala High Court in *Commissioner of Income-tax v. E C Jacob*[6] and *Commissioner of Income-tax v. B C Srinivasa Setty*[7] decided by the

9. On the other hand, Mr. Joshi for the revenue pointed out that the definition of the expression "capital asset" as given in section 2(4A) of the 1922 Act and the definition of that expression as given in section 2(14) of the 1961 Act is of the widest amplitude since according to these two definitions the expression "capital asset" has been defined to mean" property of any kind held by an assessee whether or not connected with his business or profession" and then follow three types of specified properties which are excluded from that definition with which the court is not concerned in this case and according to him though goodwill is an intangible asset and may not be capable of being held independently by an assessee in the sense that it always goes with the business of the assessee, it none the less falls within the definition of the expression "capital asset". He further pointed out that under section 6 of the 1922 Act as well as section 14 of the 1961 Act "capital gains" has been enumerated as one of the heads of income and both under section 12B(1) of the 1922 Act as well as under section 45 of the 1961 Act any profits or gains arising from transfer of capital asset effected in the previous year have been rendered taxable under the heading "capital gains". He, therefore, urged that the goodwill of the assessee-firm in the instant case must be regarded as capital asset falling within the relevant definition and since there was transfer of that goodwill from the assessee-firm to a private limited company under the transaction dated April 9, 1959, any profit or gain arising from such transfer must be regarded as exigible to capital gains tax under section 12B of the 1922 Act. He contended that section 12B(1) was a charging provision whereas sub-sections (2), (3) and (4) of section 12B contain machinery provisions where the manner of computing capital gains had been indicated and that the machinery provisions should not be allowed to control the charging provision as contained in section 12B(1). According to him, therefore, the fact that in computing capital gains certain deductions, such as expenditure incurred solely in connection with the transfer and the actual cost to the assessee of the capital asset, are required to be made from the full value of consideration for which the transfer of an asset is made does not mean that if the capital asset has not cost anything in terms of money to the assessee, the chargeability to capital gains tax would not arise but in such a case the whole of the consideration received by the assessee while effecting transfer of an asset will have to be regarded as the capital gains made by him upon such transfer and will have to be bought to tax under section 12B(1) of the 1922 Act. He, therefore, urged that in the instant case at the option of the assessee-firm instead of deducting actual cost at zero as on January 2, 1947, when the business was commenced by the assessee-firm, the actual cost was valued by the Income-tax Officer, as on January 1, 1954, at Rs. 1,24,170 and after deducting the said value as representing the actual cost from the total consideration of Rs. 4,89,000 the Income-tax Officer had rightly computed the capital gains at Rs. 3,64,830 and had included the sum in the total assessable income of the assessee-firm. In support of his contention strong reliance was

placed by mr. Joshi upon a decision of the Gujarat High Court in *Commissioner of Income-tax v. Mohanbhai Pamabhai*[9] a decision rendered under the relevant provisions of the 1961 Act.

10. Before dealing with the relevant provisions contained in the 1922 Act as well as the 1961 Act, it would be desirable to set out a few undisputed facts which emerge very clearly on record. It was not disputed before us that the assessee-firm (M/s Home Industries & Co.) commenced its partnership business of manufacturing and selling textile auxiliaries, industrial and allied chemicals and process work of bleaching and printing at Lady Hardinge Road, with effect from January 2, 1947. In other words, the three partners constituting the assessee-firm had not taken over from any existing concern its business for being carried on in partnership by them but the three partners themselves started their fresh business in partnership in January, 1947. This aspect becomes clear from the recital as well as clause 2 of the deed of partnership dated December 9, 1949, which has been produced at exhibit D-1 in this reference. There is also a statement to that effect in the statement of case submitted by the Tribunal to this court. It was also not disputed before us that the books of account of the assessee-firm initially did not contain any goodwill account but that such goodwill account came to be opened only at the time of transfer of the said business by the assessee to the private limited company, which also becomes clear from the books of account that were written up to April 9, 1959, and they were produced before the Income-tax Officer during the assessment proceedings. Indisputably, the firm was converted into a private limited company and under the agreement of sale dated April 9, 1949, the entire assets and liabilities of the firm were taken over by the limited company at book value. At the time of such transfer, goodwill was separately valued at Rs. 4,89,000 and the goodwill account was debited in the books while the partners' accounts were credited with Rs. 1,63,000, each representing each one's share in the goodwill. A copy of the agreement for sale dated April 9, 1959, being annexure, exhibit D, to the statement of case, clearly shows that all the undertakings, property, assets, debts liabilities, engagements and contracts of the business of Home Industries & Co. together with goodwill as a going concern was taken over by the private limited company Hico Products Pvt. Ltd., for a total consideration of Rs. 10,33,122 out of which a sum of Rs. 4,89,000 represented consideration for the goodwill received by the assessee-firm created or generated by the trading activities of the assessee-firm and probably by the name which the firm had earned and the goodwill it had created among its customers. It grew along with the business which was carried on by the assessee-firm right up to April 9, 1959, on which day the business together with the goodwill was transferred by the assessee-firm to the private limited company. In other words, two aspects become very clear, namely, that the goodwill of the assessee-firm, though a capital asset of the firm, could not be said to have been acquired by it at any particular point of time and the same could not be said to have it whether this type of capital asset of the assessee-firm is one whose transfer will give rise to chargeable capital gains under section

12B(1) of the 1922 Act.

11. At this stage it would be desirable to refer to the provisions of the relevant sections of the 1922 Act. Section 2(4A) defines the expression "capital asset" thu :

> "'capital asset' means property of any kind held by an assessee, whether or not connected with his business, profession or vocation, but does not include -
>
> (i) any stock-in-trade, consumable stores or raw materials held for the purposes of his business, profession or vocation;
>
> (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) any land from which the income derived is agricultural income."

12. Section 6, which occurs in chapter III of the Act, deals with taxable income and it enumerates six different heads of income chargeable to income-tax and clause(vi) refers to "capital gains" as one of the heads of income chargeable to income-tax. Then comes the material provision, viz., section 12B, under which "capital gains" have been rendered exigible to income-tax. Section 12B has for its marginal note the expression "capital gains". It may be stated that capital gains were brought under taxation, for the first time, by the Income-tax and Excess Profits Tax (Amendment) Act, 1947, which introduced section 12B into the Income-tax Act, a tax on capital gains arising after March 31, 1946. This levy was for all practical purposes abolished by the Indian Finance Act, 1949, which confined the operation of this section to capital gains arising before April 1, 1957, by the Finance Act, 1956, which substituted the present section 12B. The material provisions of section 12B run as follow :

> "12B. Capital gains. - (1) The tax shall be payable by an assessee under the head 'capital gains' in respect of any profits or gains arising from the sale, exchange, relinquishment or transfer of a capital asset effected after the day of March 31, 1956, and such profits and gains shall be deemed to be income of the previous year in which the sale, exchange relinquishment or transfer took plac :
>
> Provided that any distribution of capital assets on the total or partial partition of a Hindu undivided family or under a deed of gift, bequest or will shall not for the purposes of this section be treated as a sale, exchange, relinquishment or transfer of the capital assets.
>
> Provided...

(2) the amount of a capital gain shall be computed after making the following deductions from the full value of the consideration for which the sale, exchange, relinquishment or transfer of the capital asset is made, namel :-

(i) expenditure incurred solely in connection with such sale, exchange relinquishment or transfer;

(ii) the actual cost to the assessee of the capital asset, including any expenditure of a capital nature incurred and borne by him in making any additions or alterations thereto, but excluding any expenditure in respect of which any allowance is admissible under any provision of sections 8, 9, 10 and 12;

Provided...

Provided...

Provided further that where the capital asset became the property of the assessee, or of the previous owner where the cost of the capital asset to the previous owner is to be taken in accordance with sub-section (3), before the day of January 1, 1954, he may, on proof of the fair market value thereof on on the said date to the satisfaction of the Income-tax Officer, substitute for the actual cost such fair market value which shall be reduced by the amount of depreciation, if any, allowed to the assessee after the said date and increased or diminished, as the case may be, any adjustment made under clause (vii) of sub-section (2) of section 1 :

Provided...

(3) Where any capital asset became the property of the assessee by succession, inheritance or devolution or on any distribution of capital assets on the total or partial partition of a Hindu undivided family or on the dissolution of a firm or other association of persons or on the liquidation of a company or under a deed of gift, or transfer on irrevocable trust, its actual cost allowable to him for the purposes of shall apply accordingly; and where the actual cost to the previous owner cannot be ascertained, the fair market value at the date on which the capital asset became the property of the previous owner shall be deemed to be the actual cost thereo :

Provided that where the capital asset became the property of the assessee -

(i) before the day of April 19, 1956, under a deed of gift or on the partition of a Hindu undivided family, the actual cost allowable to him shall be the fair market value of the

capital asset on the date of the gift or the date of the partition, as the case may be, if such value is greater than the actual cost to the previous owner or to the fair market value thereof on the day of January 1, 1954, where the third proviso to sub-section (2) applies;

(ii) on or after the day of April 1, 1956, on the partition of a Hindu undivided family, the cost allowable to him shall be the fair market value on the date of the partition."

13. Though we are concerned in the instant case with the aforesaid relevant provisions which are to be found in the 1922 Act, we would also set out here the relevant corresponding provisions of the 1961 Act as some of the decisions, on which reliance has been placed before us, have been rendered in the light of such provisions. Section 2(14) defines the expression "Capital gains" but since the said definition is almost in identical terms as the definition contained in section 2(4A) of the 1922 Act it need not be set out verbatim. Section 14 of the 1961 Act also enumerates different heads of income and includes capital gains as one of the heads of income therein. Section 45, which is equivalent to section 12B(1) of the old Act, runs thu :

"45. (1) Any profits or gains arising from the transfer of a capital asset effect in the previous year shall, save as otherwise provided in sections 53, 54, 54B and 54D be chargeable to income-tax under the head 'Capital gains', and shall be deemed to be the income of the previous year in which the transfer took place."

14. Section 46 provides that notwithstanding anything contained in section 45 where the assets of a company are distributed to its shareholders on its liquidation, such distribution shall not be regarded as a transfer by the company for the purpose of section 45. Section 47 provides that nothing contained in section 45 shall apply to certain transfers mentioned therein, such a : any distribution of capital assets on the total or partial partition of a Hindu undivided family; any distribution of capital assets on the dissolution of a firm; and any transfer of a capital asset under a gift or will or in irrevocable trust, etc.,

15. Section 48 has for its margin the expression "Mode of computation and deductions" and it is almost similar or equivalent to sub-section (2) of section 12B of the old Act. It runs thu :

"48. The income chargeable under the head 'Capital gains' shall be computed by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, namel :-

(i) expenditure incurred wholly and exclusively in connection with such transfe :

(ii) the cost of acquisition of the capital asset and the cost of any improvement thereto."

16. Section 49 deals with the aspect as to how the cost of acquisition of an asset to an assessee will have to be valued in certain modes of acquisition of the asset and the provisions thereof are similar or equivalent to some of the provisions contained in section 12B(3) of the 1922 Act.

17. Now, there are five or six aspects of goodwill which have been pressed into service by Mr. Dastur in support of his contention that self-created or self-generated goodwill would not be a capital asset the transfer of which will give rise to chargeable capital gains under the scheme of section 12B of the 1922 Act. According to him, the position arising from sale or transfer of such type of goodwill will be the same even under the 1961 Act. In the first place, having regard to the definition of "capital asset" given in section 2(4A) of the 1922 Act, he urged that though goodwill may fall within the wide ambit of the words "property of any kind" and may come within the expression "capital asset", that definition itself suggests that the asset must be capable of being held by the assessee independently and must be capable of being independently transferred by the assessee and since the goodwill invariably must go with the business to which it is attached, it is not capital asset which is capable of being independently held transferred by the assessee; secondly, he emphasised the aspect that the goodwill is an intangible asset; thirdly, he urged that the scheme of section 12B implies acquisition of capital asset by the assessee at some particular point of time; fourthly, he urged that the said scheme also implies acquisition of capital asset by the assessee at some particular point of time; fourthly, he urged that the said scheme also fifthly, the said scheme also implies that the capital asset is capable of improvement and assessment of cost relatable to such improvement of asset, which, in other words, means that it must be an identifiable asset capable of identifiable improvement; and, lastly, he urged that the scheme of section 12B does not imply taxation on gross receipts and for these aspects he relied on sub-sections (2) and (3) of section 12B. He pointed out that in cases where there is a gift of the capital asset the actual cost is taken to be the actual cost to the previous owner under sub-section (3). He stated that if in a given case the assessee had himself purchased a going concern from its previous owner and had paid consideration for the goodwill thereof and if such an assessee were to transfer or sell such concern to a third party, either immediately after purchasing the same or after running the same for few years and if in such latter transfer he receives some consideration for the goodwill, then, it might be a case where the transfer of the goodwill may give rise to chargeable capital gain, though he was not prepared to concede that position, obviously because such question has not arisen in the instant case before us. He, however, pointed out that in the instant case the goodwill which had been transferred by the assessee-firm to the private limited company was an intangible, self-created or self-generated asset which had been built up by the firm by its own efforts and trading activities, that it had not been acquired at any particular point of time nor it had cost anything to the firm in terms of money and that it had been sold by the firm along with its business as a going concern to the private limited company

and, therefore, the transaction in question would not give rise to chargeable capital gain.

18. In support of his aforesaid contentions reliance was placed by him upon the decisions of five different High Courts mentioned above. He pointed out that in K. Rathnam Nadar's case [1969] 71 ITR 433 (Mad) (supra) the Madras High Court has taken the view that goodwill is created by the trading activities of the assessee and probably by the name he has earned and the goodwill he has created among his customers; that goodwill of a firm is an intangible asset and can be compared to a seed which is planted on the date the firm begins its business and sprouts and grows as the firm grows in its dealings, in its stature and in its reputation; it is difficult to say that it costs anything in terms of money for its coming into existence; that though goodwill is a capital asset, in the case of goodwill of a business it cannot be said that it became the capital asset of the firm at any particular point of time; that it is something which goes on slowly growing and perhaps waxing and waning also and that what exactly is the value of the goodwill of a business at any point of time may have to be worked on a proper basis by cost accountants. The court has further held that section 12B(2)(ii) of the 1922 Act suggests that capital gain arises only on the transfer of a capital asset which has actually cost to the assessee something; that such actual cost in the contest of the Income-tax Act being cost in terms of money, it cannot apply to transfer of capital assets which did not cost anything to the assessee in terms of money in its creation or acquisition. He further pointed out that the Calcutta High Court in Chunilal Prabhudas [1970] 76 ITR 566 (Cal)(Supra) has taken the view that in order that there should be taxable capital gain within the meaning of section 12B of the Income-tax Act, there has to b : (1) profit or gain, (2) capital asset, (3) the profit or gain must arise out of the transfer, and (4)"sale, exchange and relinquishment or transfer"; and that it is difficult to apply these tests to the case of goodwill. Goodwill is not any kind of usual capital asset with which a business is started. It is not a capital asset which can be divided into parts, fragments or fractions or entered on the stock-book or register of capital assets nor can it, like capital asset which can be divided into parts, fragments or fractions or entered on the stock-book or register of capital assets nor can it, like capital asset, exist independently without the business itself and have any value apart from the business usually associated with capital asset. Unlike capital assets, goodwill, as an asset, is indivisible and cannot be sold, transferred or dealt with in fragments or fractions. On the interpretation of section 2(4A), section 2(6C) and section 12B and on their express words and tenor, goodwill does not come within the obvious meaning of capital asset. To bring goodwill within the meaning of capital asset and make it taxable would be to tax by implication or by analogy, or by a forced and artificial construction. He pointed out that in Jagdev Singh Mumick's case the Delhi High Court, following the Madras decision in K. Rathnam Nadar's case [1969] 71 ITR 433 (Mad)(Supra) , held that the amount of Rs. 50,000 which was received by the assessee for the goodwill which he transferred along with his business as a going concern to a private limited

company was not liable to be taxed as a capital gain under section 12B of the 1922 Act.

19. Strong reliance was placed by Mr. Dastur upon the full Bench decision of the Kerala High Court in E C Jacob's case [1973] 89 ITR 88 (Ker) [FB](supra). In that case the assessee had been practising as a chartered accountant under the firm name. J. & W., from 1951. During the relevant accounting year, the assessee took in as partner one V, on July 15, 1965. The assessee's share in the business was 75% and V's share was 25%. The goodwill of the business was valued at Rs. 32,000 and V paid the assessee Rs. 8,000 for his share of the goodwill. The firm was dissolved on October 19, 1965, when the assessee retired from the firm and the assessee received Rs. 24,000 towards his share of the goodwill of the firm. The firm was dissolved on October 19, 1965, when the assessee retired from the firm and the assessee received Rs. 24,000 towards his share of the goodwill of the firm. The Income-tax Officer held that the entire amount of Rs. 32,000 received by the assessee was taxable as "capital gains". On second appeal, the Appellate Tribunal held that the amount was not taxable. On a reference, the Full Bench of the High Court held that the Appellate Tribunal was correct in holding that the amount could not be subjected to tax as capital gains. The court took the view that what is charged under section 45 of the 1961 Act is the "profit or gain arising from the transfer of a capital asset". In computing the "profit or gain" in accordance with the provisions of section 48 of the Act, the cost of the acquisition of the capital asset and the cost of any improvement thereto have to be deducted from the full value of the consideration for the transfer of the capital asset. In the context of the Income-tax Act, the expression "cost of acquisition" signifies some expenditure or outlay in terms of money by the assessee in the creation or acquisition of the concerned capital asset. It was by his personal effort spread over a number of years that the assessee built up the goodwill in dispute. It is impossible to estimate even roughly the money he could have spent in building up his professional reputation. The cost of aacquisition was thus incapable of determination. The Full Bench also went on to point out that under section 55(1)(b) of the Act."cost of any improvement" means "all expenditure of a capital nature incurred by making any addition or alteration to the capital asset". The expenditure contemplated is expenditure in terms of money."Goodwill" is an asset that gains in value by lapse of time; and in the case of the goodwill of a profession, such augmentation is essentially attributable to the personal efforts, skill or sacrifice of the owner. It is not possible in such cases to evaluate the increase in value in terms of money. Thus, in the case of certain categories of transfers of "goodwill", it is not possible to determine the "cost of acquisition" and the "cost of improvement" referred to in section 48(ii) for the purpose of computation of "capital gains" under section 45 of the Act. Therefore, the amount received by the assessee towards the value of goodwill was not assessable to tax under section 48 of the 1961 Act. Mr. Dastur fairly pointed out that, in this case, the Full Bench of the Kerala High Court has referred to a case where transfer of goodwill would attract the tax on capital gains made in such transfer and such a

case has been referred to in the following observations at page 93 of the report [1973] 89 ITR 88 (Ker) [FB].

> "It is possible to envisage a case where a person purchases the goodwill of a business or profession for a definite amount and without any further addition to its value by his own efforts later on sells it for a higher price and thereby secures a determinate profit or gain. In such a case, goodwill is hardly distinguishable from any other capital asset and there is nothing in section 45 or other relevant provisions of the Income-tax Act that excludes such profits or gains from liability to assessment.
>
> Lastly, he relied upon the decision of the Karnataka High Court in B C Srinivasa Setty's case [1974] 96 ITR 667 (Kar). In that case the question that was referred to the High Court ran thu :

"Whether, on the facts and in the circumstances of the case, the Tribunal was right in holding that no capital gains could arise under section 45of the Income-tax Act, 1961, on the transfer by the assessee-firm of its goodwill to the newly constituted firm ?"

20. It is true that as against the decisions rendered by the High Courts of Madras, Calcutta, Delhi and Kerala, the contrary view taken by the Gujarat High Court in Mohanbhai Pamabhai's case [1973] 91 ITR 393 (Guj)(Supra) was also brought to the notice of the Karnataka High Court but the Karnataka High Court answered the questioned referred to it in the affirmative and held that the value of the consideration received by the assessee-firm for transfer of its goodwill was not liable to capital gains tax under section 45 of the 1961 Act for two or three reasons. In the first place, the court pointed out that against the decision of the madras High Court in Rathnam Nadar's case [1969] 71 ITR 433 (Mad)(supra) the department had preferred an appeal to the Supreme Court and long before the date of hearing of that appeal before the Supreme Court, the Gujarat High Court in Mohanbhai Pamabhai [1973] 91 ITR 393 (Guj)(supra) had taken a contrary view dissenting from the view taken by the High Courts of madras and Calcutta and as such the department could not have been unaware of the Gujarat High Court decision and the department could have pressed that decision for acceptance by the Supreme Court as correctly interpreting the law, but when the department did not press its appeal (preferred against Madras High Court decision in Rathnam Nadar's case [1969[71 ITR 433 (Mad)(supra) as laying down the correct law. Secondly, the Karnataka High Court has observed that the uniformity of construction of All-India tax law by the various High Courts is eminently desirable and that since the department could be said to have accepted the ratio of the decision in Rathnam Nadar's case [1969] 71 ITR 433 (Mad)(Supra) as laying down the correct law, in view of its conduct in not pressing the appeal, it would be proper to answer the question by falling in line with the

interpretation given by the madras, Calcutta and Delhi High Courts. Thirdly, the Karnataka High Court has pointed out that when two views are possible on a question concerning the interpretation of a tax law, the one which is fair both to the assessee and the department should be followed and, according to it, the view that capital gains tax is not attracted to transfer of goodwill is a fair and just interpretation. It has gone on to observe that, "if the view of the Gujarat High Court in Mohanbhai Pamabhai's case [1973] 91 ITR 393 (Guj(Supra) is correct, the cost of acquisition of goodwill being nil, the full value of the consideration for its transfer has to be brought to charge to capital gains tax. Such a levy will not be a tax on profits or gains but, in substance, a tax on the capital value of the asset. The capital value of goodwill is charged to tax under the Wealth-tax Act, 1957. Wealth-tax is an annual recurring tax. When there is an annual recurring tax on the capital value of goodwill, it will be unfair to levy another tax calling it as capital gains on the same value of the goodwill in the same assessment year, merely because the goodwill has been transferred for consideration". Relying on the aforesaid authorities Mr. Dastur urged that in the instant case the goodwill being a self-created asset should be regarded as not capital asset the transfer of which will give rise to chargeable capital gains and as such the question referred to us should be answered in the negative, in favour of the assessee.

21. Mr. Joshi, on the other hand, contended that all the conditions requisite for levying capital gains tax under section 12B of the 1922 Act were satisfied in the instant case and, therefore, there was no reason why the capital gain made by the assessee-firm while transferring the goodwill of its business to the private limited company should not be brought to tax under the said provision. He pointed out that the expression "capital asset" has been defined in section 2(4A) of the act in a very wide language as meaning "property of any kind held by an a assessee, whether or not connected with his business, profession or vocation; and it could not be disputed that the goodwill of the assessee-firm would be the property falling within the said definition; secondly, he pointed out that there was a transfer of that goodwill from the assessee-firm to a private limited company under the transaction dated April 9, 1959, for consideration and as such any profit or gain arising from such transfer would be exigible to the capital gains tax under section 12B of Act. He contended that neither the aspect that it is an intangible asset not the aspect that it is incapable of being held or transferred independently of the business to which it is attached will make any difference to tax on profit or gain arising from the transfer thereof. He further contended that a clear distinction exists between the charging provision of taxing enactment (section 12B(1)) and the machinery provision contained in such enactment (section 12B(2)) and it is well-settled that the machinery provision cannot control the charging provision. He, therefore, urged that the fact that in computing capital gains certain deduction, such as, expenditure incurred solely in connection with the transfer [clause (i) of sub-section (2) of section 12B] and the actual cost to the assessee of the capital asset [clause (ii) of sub-section (2)

of section 12B] are required to be made from the full value of consideration for which the transfer of asset is effected does not mean that if the capital asset has not cost anything in terms of money to the assessee, the chargeability to capital gains tax would not arise. But, according to him, in such a case the whole of the consideration received by the assessee while effecting the transfer of asset will have to be regarded as capital gain made by him upon such transfer and will have to be brought to tax under the charging provision contained in section 12B(1) of the Act. He pointed out that if the contention urged on behalf of the assessee-firm in this behalf of the assessee-firm in this behalf were to be accepted, the same will have to be applied to the deduction contemplated by clause (i) of sub-section (2) of section 12B, which would bring about a result never intended by the legislature. According to him, if in a given case no expenditure of any kind is incurred in connection with such sale or transfer of capital asset, it could be urged that taxability of profit or gain made by transfer of a capital asset under section 12B(1) shall not arise, which could never have been intended by the legislature. According to him, therefore, the mere fact that the goodwill has not cost anything to the assessee-firm in terms of money in the instant case could not be a ground for not attracting the provisions of section 12B(1) to the transaction in question. He pointed out that under the 1922 Act the entire provision relating to capital gains tax has been enacted in section 12B of the Act, but even so, it is clear that the charging provision is to be found in sub-section (1) of section 12B while what is contained in sub-section (2) and the other sub-sections of section 12B will have to be regarded as machinery provisions. This aspect of the matter will become clear if the provisions of the 1951 Act are borne in mind. Under the 1961 Act, the charging provision is to be found in a separate section viz., section 45, while the machinery provision is to be found in another separate section, viz., section 48, and the provisions of section 48 correspond to the provisions contained in sub-section (2) of section 12B of the 1922 Act. According to Mr. Joshi, this aspect of the matter appears to have been overlooked and in any case not expressly referred to in any of the decisions on which Mr. Dastur has relied. In support of his submissions Mr. Joshi strongly relied upon the decision of the Gujarat High Court in commissioner of Income-tax v. Mohanbhai Pamabhai [1973] 91 ITR 393 (Guj)(supra). He pointed out that the Gujarat High Court has not accepted the view of the Madras High Court in Rathnam Nadar's ase [1969] 71 ITR 433 (Mad)(supra)as also the view of the Calcutta jurisdiction in Chunilal Prabhudas's case [1970] 76 ITR 566 (Cal)(supra) but has categorically taken a contrary view. He further pointed out that, according to the Gujarat High Court, the charging provision was to be fund in section 45 of the 1961 Act, whereas section 48 dealt with the topic of deductions to be made while computing capital gains and according to that court the charging provision in section 45 was not confined to those cases where the capital asset had cost something to the assessee in terms of money in acquiring it and that there was nothing in any of the section relating to capital gains which indicated that the charging provision should be construed in a narrow manner by excluding self-created capital asset or capital asset which cost

nothing t the assessee in terms of money in acquiring it. If further held that section 48 provided for deductions from the value of capital asset "the cst of acquisition of the capital asset" and the word "acquired", according to its plain natural meaning, was a word with very wide import that it shall not be confined to obtaining of a thing from a third party but the creation or production of a capital asset was not foreign to the concept of "acquisition" and that even where the capital asset is self-created it would be covered by section 48 and goodwill of a business was such a capital asset. He also relied on a decision of this court in *Daulatran Nayar's case*[9] which, according to him, concludes the issue against the assessee and in favour of the revenue.

22. After giving our anxious consideration to the rival submissions that were put forward by counsel on either side as well as the several decisions that were cited at the Bar, we are inclined to agree with the view taken by the Madras High Court in Rathnam Nadar's case [1969] 71 ITR 433 (Mad)(Supra) and by the Full Bench of the Kerala High Court in E. C. Jacob's case [1973] 89 ITR 88 (Ker) [FB](supra). Looking at the issue purely from point of view of proper construction of the relevant provisions of the 1922 Act (being section 12B) and of the 1961 Act (being group of sections - sections 45 to 55 of the Act) it appears to us clear that there is sufficient warrant in the charging provision itself (in both the Acts) to exclude the self-created or self-generated goodwill (of the type with which we are concerned in this case) from the charge and for that purpose recourse to the machinery provision would be unnecessary, though what is contained in the machinery provision could strengthen the inference clearly arising from the charging provision. But, before we discuss the charging provision as well as the machinery provision (contained in both the Acts), we would at the outset indicate which out of the five or six aspects of goodwill which have been pressed into the service of Mr. Dastur will, according to us, have no bearing on the determination of the issue before us.

23. There cannot be any dispute that the definition of the expression "capital asset" given in sections 2(4A) of 1922 Act, (as also in section 2(14) of the 1961 Act) is of the widest amplitude, for, according to that definition "capital asset" means "property of any kind" and goodwill certainly falls within the ambit of the words "property of any kind" and as such comes within the expression "capital asset", but though the definition says that capital asset means "property of any kind held by an assessee", there is nothing in the definition to indicate that it must be held independently by an assessee nor is there anything to suggest that the same must be capable of being transferred independently as was contended for by Mr. Dastur. It is true that goodwill, as a "capital asset", is incapable of being either held independently or transferred independently by the owner thereof but the same is invariably attached to his business and is usually sold or transferred by him along with the business as a going concern but that would not render it such a capital asset, the transfer whereof would not give rise to chargeable capital gain. Secondly, it is

true that goodwill is an intangible asset but, in our view, such characteristic will not make it a capital asset, the transfer whereof will give rise to no chargeable capital gains. A transfer of an intangible asset for consideration can give rise to chargeable capital gain; for instance, the right of an easement is an intangible property and, normally, such wight goes with the dominant tenement and if, while transferring the dominant tenement, some specific consideration were to be received for the transfer of right of easement, it is conceivable that capital gain chargeable to tax under the charging provision would arise. However, the aspects that in the case of self-created or self-generated goodwill it is impossible to say that it has been acquired at any particular point of time and that the acquisition of such capital asset costs nothing to the owner of business in terms of money seem to us to be a very important aspect which have a bearing on the question as to whether the transfer of such capital asset should give rise to chargeable capital gains or not. Similarly, the aspect that the capital asset in question must be such that it is capable of improvement at an ascertainable cost in terms of money would be equally important. As has been pointed out by the Madras High Court Court in Rathnam Nadar; s case [1969] 71 ITR 433 (Mad)(Supra), such goodwill is created by trading activities by the assessee and probably by the name he has earned and the goodwill he has created among his customers and comparing it to a seed, it is observed that goodwill is planted on the date the firm begins its business and sprouts and grows as the firm grows in its dealings, in its stature and in its reputation and, therefore, it is not possible to say that it becomes capital asset of the firm at any particular point of time and that it is something which goes on slowly growing and perhaps waxing and waning also. It is also clear that it is very difficult to say that it costs anything in terms of money for coming into existence. Further, as has been pointed out by the Kerala High Court in E C Jacob's case [1973] 89 ITR 88 (Ker) [FB], normally, goodwill is an asset that gains in value by lapse of time and in the case of the goodwill of a profession, such augmentation is essentially attributable to the personal efforts, skill or sacrifice of the owner and it is not possible in such cases to evaluate the increase in value in terms of money and in this sense it is not possible to determine be "cost of acquisition" and the "cost of improvement" in terms of money. We might also indicate that according to good commercial and accounting practice, a self-created goodwill does not usually appear in the books and in fact when it arises by purchase, then only the figure representing the value thereof is entered in the books and in this behalf in William Pickles' Text Book on Accountancy (3rd edition p. 623), the following passage occur :

> "The books of account may or may not record a figure for goodwill; in fact, unless arising by purchase, goodwill does not usually appear in the books, it being regarded as contrary to good accounting practice to write up a created goodwill.
>
> Even if the record be made it may not represent the true value because of the inherent

difficulties of valuation, particularly as from time to time the asset is susceptible to extreme fluctuations..."

24. The question is whether a self-created or self-generated goodwill, possessing the aforesaid peculiarities, is such a capital asset that its transfer will give rise to chargeable capital gains ? In other words, the question is whether transfer of such goodwill is intended to be included in or excluded from the purview of the charging provision imposing the incidence of capital gains tax ? From this angle we shall consider the charging provision which is to be found in section 12B(1) of the 1922 Act as well as section 45 of the 1961 Act.

25. Under sub-section (1) of section 12B it has been provided that tax shall be payable by an assessee under the head "capital gains" in respect of any "profits or gains" arising from the sale, exchange relinquishment or transfer of a capital asset effect after March 31, 1956, and such "profits and gains" shall be deemed to be income of the previous year in which the sale, exchange, relinquishment or transfer took place. The wording of section 45 of the 1961 Act is almost similar and under section 45 it is provided tha :

"Any profits or gains arising from the transfer of a capital asset effected in the previous year shall, save as otherwise provided in section 52, 54, 54B and 54D be chargeable to income-tax under the head 'capital gains', and shall be deemed to be the income of the previous year in which the trafer took place."

26. It will appear clear on a reading of both the charging provisions that the incidence of tax is on "profits or gains" arising from the transfer or sale of a capital asset. In other words, the charging provision in both the Acts makes it very clear that there must be profit or gain which must arise from the transfer or sale of capital asset and it is such "profit or gain" that is chargeable to tax. The concept of "profit or gain" arising from transfer or sale necessarily implies that there is something received in excess of the cost of the capital asset which is transferred or sold. Profit or gain arising from sale has a necessary reference to the difference between the cost of price of the asset and the sale price of the asset. In other words, it is not necessary to have any recourse to the machinery provision contained in sub-section (2) of section 12B of the 1922 Act, or section 48 of the 1961 Act, in order to come to the conclusion that the incidence of tax contemplated by the charging provision necessarily refers to the difference between the cost price and the selling price of a particular capital asset, the profit or gain arising from transfer of which is the subject-matter of the charge. The charging provision in both the Acts, therefore, itself brings in a the concept of actual cost to the assessee of the capital asset and what is done by the machinery provision which is contained in sub-section (2) of section 12B of the 1922 Act, and section 48 of the 1961 act, is to elaborate that concept and lay down the mode or method by which such profit or gain is to be

computed; the machinery provision reiterates what is contained in the charging provision and goes on to indicate that capital gain is to be arrived at after deducting the actual cost from the full value of the consideration for which the transfer of the capital asset is made. If the capital asset is such that it has cost nothing in terms of money to the assessee, the charging provision must be interpreted as being not referable to such capital asset, and self-created or self-generated goodwill being such asset will be outside the purview of the charging provision. Mr. Joshi's contention that the machinery provision should not be allowed to control or effect the charging provision becomes irrelevant and inapplicable. Moreover, the argument that if the self-created or self-generated goodwill has cost nothing to the assessee, then the actual cost to the assessee should be treated as zero and the entire consideration received for the goodwill should be regarded as capital gain made upon transfer of that asset, would run counter to the scheme of section 12B, for the scheme of that section does not imply taxation on gross receipt but implies a charge only on the profit or gain arising from the transfer of that asset. Therefore, on a proper interpretation of the charging provision itself, it seems to us clear that the concept of actual cost expressed in terms of money to the assessee of the capital asset at some particular point of time would be a necessary ingredient before the Since we have come to the conclusion that self-created or self-generated goodwill is not capital asset which could be said to have been acquired by the assessee-firm at any particular point of the time and is not a capital asset which could be said to have cost something in terms of money to the assessee, such goodwill will not be a capital asset the transfer of which will give rise to chargeable capital gain under either section 12B(1) of the 1922 Act or section 45 of the 1961 Act.

27. As regards the Gujarat High Court decision in Mohanbhai Pamabhai's case [1973] 91 ITR 393 (Guj)(Supra), on which strong reliance was placed by Mr. Joshi, two or three aspects may be mentioned. In the first place, the decision on the concerned point is clearly obiter. It may be stated that two contentions were raised on behalf of the assessee who had retired from the partnership firm of Prajapati Tiles Company; the first was that the retirement of the assessee from the partnership amounted to dissolution of the firm within the meaning of section 47(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 and the second was that goodwill being a self-created asset which had cost nothing to the firm and its partners in terms of money its transfer 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 gain. The Tribunal negatived the first contention but accepted the second. On a reference the High Court reversed the Tribunal's view on the first contention and held that when an assessee

retired from a firm there was no transfer of interest of any of the assessees with the goodwill of the firm and, in that view of the matter, it was really unnecessary for the High Court to examine the validity of the second contention but since the second contention had been fully argued before it, the court thought it desirable to express its opinion upon it. This has been expressly stated by the court in the following terms (at page 405 :

> "This decision as regards the first contention renders it unnecesssary for us to examine the validity of 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."

28. This will clearly show that the decision on the question whether goodwill which was a self-created asset and had cost nothing to the firm and its partners in the terms of money was a capital asset the transfer whereof would give rise to chargeable capital gains under section 45 was clearly obiter. Secondly, though the decisions of the Madras High Court and the Calcutta High Court have been expressly dissented from by the Gujarat High Court, the Gujarat High Court does not seem to have considered the question whether, irrespective of the machinery provision which is to be found in section 48 of the 1961 Act, the charging section, viz., section 45, itself implies the concept of "actual cost" to the assessee of the capital asset as being a relevant aspect for bringing in chargeability to tax under the charging provision; thirdly, the Gujarat High Court seems to have proceeded on an elaborate discussion of the exact connotation of the expression "acquired" and has gone on to observe that the said expression is not confined to obtaining of a thing from a third party and creation of 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. In our view, the relevant aspect which needs to be emphasised is whether the concept of "actual cost" of the capital asset to the assessee is implied in the charging provision itself of not and if it is implicit therein, then, the charge or the incidence of capital gains tax cannot fall upon such types of capital asset as would cost nothing to the assessee for acquiring the same. Such capital asset which cost nothing to the assessee in terms of money will have to be regarded as being nothing to the assessee in terms of money will have to be regarded as being outside the purview of the charging provision itself.

29. Reliance by Mr. Joshi upon the decision of this court in Daulatran Nayar's case [1976] 105 ITR 843 (Bom) (supra)is misconceived. The question that arose for consideration in that case was whether the assessee was entitled to substitution of the market value of the asset as on January 1, 1954, for the "actual cost" as envisaged in the third proviso to section 12B(2) and the question was answered in favour of the assessee on the certain assumptions and concessions made in the case. The facts of the case shortly stated have been thes : The assessee was a partner in a partnership of eight partners, in which each of the partners had an equal share in the profits

and losses; the business of the firm was taken over by a limited company of the same name as from July 1, 1959; the firm received the sum of Rs. 5 lakhs towards goodwill of the business from the limited company; our of this amount, a sum of Rs. 62,500 was credited in the account of each of the partners of the firm in the books of the firm; for the assessment year 1960-61, the Income-tax Officer held that the entire amount of Rs. 62,500 credited to the assessee, without any deduction under section 12B(2) of the 1922 Act, was a capital gain liable to tax. On appeal, the Appellate Assistant Commissioner accepted the assessee's contention that the assessee and his partners were entitled to the substitution of the market value of the asset as on January 1, 1954, for the "actual cost" as envisaged in the third proviso to section 12B(2). The Appellate Assistant Commissioner determined such fair market value at a figure higher than Rs. 5 lakhs and, therefore, according to him, there was no capital gain at all made on the sale of the goodwill at Rs. 5 lakhs. He, accordingly, held that no capital gains tax was chargeable and allowed the appeal. The Tribunal affirmed the order of the Appellate Assistant Commissioner. In the reference made to the High Court the precise question referred for opinion wa : "Whether, on the facts and in the circumstances of the case, the assessee was entitled to substitute the fair market value of the goodwill on January 1, 1954, under the third proviso to section 12B(2) of the 1922 Act ?" and the answer to the question depended upon the proper interpretation of the expression "became the property of the assessee" occurring in the third proviso to section 12B(2) and the court took the view that the expression was not confined to acquisition of the property by the assessee from a third party or acquisition for some price paid and the capital asset could become the property of the assessee within the meaning of the third proviso, even if it was acquired by self-generation and in that view of the matter this court held that the assessee was entitled to substitute the fair market value of the goodwill as on January 1, 1954, under the third proviso to section 12B(2). However, it must be pointed out that the aforesaid decision was rendered by this court on certain assumptions and concessions made at the Bar, namely, that it was assumed that the goodwill, though a self-generating asset, is a capital asset to which section 12B would apply and on the further assumption that there was a transfer of this capital asset when the business of the firm was taken over by a limited company. This will become clear from the following observations which appear at page 845 of the report-See [1976] 105 ITR 843 (Bom)(Supra)

> "A the outset we would like to observe that we shall proceed to deal with and answer the question referred to us for opinion the assumption that the goodwill though a self-generating asset is a capital asset and on further assumption that there was a transfer of this capital asset when the business of the firm was taken over by the limited company."

30. In other words, this court proceeded to determine the question referred to it in that case on two assumptions indicated above and, therefore, it cannot be said that this court really decided

the question whether a self-created or self-generated goodwill is a capital asset, the transfer of which would give rise to chargeable capital gains-a question which has been specifically raised before us in the instant case. The decision and all the observations made in Daulatran Nayar's case [1976] 105 ITR 843 (Bom)(Supra) cannot, therefore, be taken to have decided the issue that has arisen in the instant case before us especially when on that precise issue the court proceeded on an assumption or concession made at the Bar. That decision, therefore, cannot avail the revenue.

31. For the reasons indicated above, we are inclined to accept the view of the Madras High Court in Rathnam Nadar's case [1969] 71 ITR 433 (Mad)(Supra) and the view of the Kerala High Court in the Full Bench decision in E. C. Jacob's case [1973] 89 ITR 88 (ker) [FB]. Having regard to the above discussion, the question referred to us will have to be answered in favour of the. Question is accordingly answered in the negative and in favour of the assessee. Department will pay the costs of the reference to the assessee.

Cases Referred.

1[1955] 28 ITR 928 (Bom)
2[1958] 34 ITR 336 (Bom)
3[1954] 25 ITR 529 (SC)
4[1969] 71 ITR 433 (Mad)
5[1970] 76 ITR 566 (Cal)
6[1973] 89 ITR 88 (Ker) [FB]
7[1974] 96 ITR 667 (Kar)
8[1973] 91 ITR 393 (Guj)
9[1976] 105 ITR 843 (Bom)