The Commissioner Of Income-Tax Bombay vs Manilal Dhanji, Bombay on 31 January, 1962

Equivalent citations: 1963 AIR 433, 1962 SCR SUPL. (2) 902, AIR 1963 SUPREME COURT 433

Author: S.K. Das

Bench: S.K. Das, M. Hidayatullah, J.C. Shah

PETITIONER:
THE COMMISSIONER OF INCOME-TAX BOMBAY

Vs.

RESPONDENT:
MANILAL DHANJI, BOMBAY

DATE OF JUDGMENT:
31/01/1962

BENCH:
DAS, S.K.
BENCH:
DAS, S.K.
HIDAYATULLAH, M.
SHAH, J.C.

CITATION:
1963 AIR 433 1962 SCR Supl. (2) 902
CITATOR INFO :
R 1971 SC2463 (13)
R 1972 SC 7 (16)
RF 1985 SC1698 (29)
F 1987 SC 107 (8)

ACT:
Income Tax-Trust created in favour of minor child-No benefit accruing to minor in accounting year-Whether income from trust taxable as income of assessee-Trust by assessees father-Assessee directed to use income for benefit of himself, his wife and children-Whether income taxable as income of assessee-Indian Income-tax Act 1922 (XI of 1922) ss. 16(3) 41(1)-Indian Trusts Act, 1882 (11 of 1882) s. 8.

HEADNOTE:

In 1953 the assessee created a trust in respect of a sum of money and provided that the interest on that amount was to be accumulated and added to the corpus and that his minor daughter C was to receive the income from the corpus increased by the addition of interest when she attained the age of 18 years. In the relevant account year, when C was still a minor, the income derived from the trust fund was Rs. 410 Earlier in 1941, the assessee's father had created a trust in respect of certain shares and money directing the trustees to pay the net interest and income thereof to the assessee "for the maintenance of himself and his wife and for the maintenance, education and benefit of all his children till his death". In the relevant account year a sum of Rs. 14,170 accrued as income in the hands of the assessee from the said trust funds,

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The taxing authorities included both these incomes in the total income of the assessee.

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Held, that neither of these two incomes could be included in the total income of the assessee.

Under s. 16(3)(b) of the Indian Income-tax Act, upon which the authorities relied, the assessee could only be taxed on the income from the trust funds for the benefit of his minor child if in the year of account the minor child either received the income or it accrued to her or she had a beneficial interest in the income in the relevant year of account. In the present case though there was income in the hands of the trustees and they were liable to pay tax thereon, there was no benefit to the minor child in that year. As such the sum of Rs. 410 did not form part of the total income of the assessee.

The trust deed of 1941 created two trusts, the one requiring the trustees to pay the income from the trust funds to the assessee and the second requiring the assessee to spend the income for the maintenance of himself and his wife and for the maintenance, education and benefit of his children. It was not a case where the settler merely expressed a wish or desire or hope but he gave as direction which created a trust in respect of the income in the hands of the assessee in favour of himself, his wife and children. The assessee did not create the second trust in respect of the beneficial interest which he held under the trust of 1941 and s. 8 of the Indian

Trusts Act which forbade the creating of such a trust was inapplicable. The assessee was a trustee and not the sole beneficiary; and since the shares of the beneficiaries were Indeterminate it was open to the Department to levy and recover tax at the maximum rate from the assessee as trustee under the first proviso to s.41(1) but the Department was not entitled to include the sum of Rs. 14,170 in the total income of the assesse as though he was the sole beneficiary under the trust deed.

JUDGMENT:

CIVIL APPELLATE JURISDICTION: Civil Appeal No. 323 of 196. Appeal from the judgment and order dated September 25, 1958, of the Bombay High Court in I.T.R. No. 3 of 1958.

K. N. Rajagopal Sastri and D. Gupta, for the appellant.

R. J. Kolah, J. B. Dadachanji, O. C. Mathur and Ravinder Narain, for the respondent.

1962. January 31. The Judgment of the Court was delivered by S. K. DAS, J.-The Commissioner of Income-tax, Bombay City I, has preferred this appeal to this Court on a certificate of fitness granted by the High Court of Bombay under s. 66A (2) of the Indian Income-tax Act, 1922.

The assessee, who is the respondent before us, was assessed to income-tax as an individual in respect of his income for the assessment year 1954-55. The taxing authorities included in the assessee's total income for the year to sums, namely, a sum of Rs. 410/- and a sum of Rs. 14,170/-. It was stated that these two sums accrued in the relevant account year in the following circumstances. On January 12, 1953 the assessee created a trust in respect of a sum of Rs, 25,000/-, the trustees whereof were the Central Bank Executor & Trustee Co., the assessee himself his wife and brother. The scheme of the trust-deed was that the said sum of Rs. 25,000/- was set apart by the assessee and it was provided that the interest on that amount should be accumulated and added to the corpus and a minor daughter of the assessee, named Chandrika, was to receive the income from the corpus increased by the addition of interest, when she attained the age of 18 on February 1, 1959. She was to receive the income during her life time and after her death the corpus was to go to persons with whom we are not concerned. The income derived from the said trust fund amounted to Rs. 410/- in the relevant account year and the taxing authorities included this amount in the total income of the assessee, purporting to act under s. 16(3)(b) and/or s. 16(3)(a)(iv) of the Income-tax Act. As regards the second sum of Rs. 14,170/- it appears that on December 1, 1941, the assessee's father had created a trust in respect of some shares and a cash sum of Rs. 30,000/- for the benefit of his four sons including the assessee. The trustees were the Central Bank Executor and Trustee Co. Ltd., the assessee himself and one other person. The said trustees were to hold the trust funds upon trust to pay the net interest and income thereof to the assessee "for the maintenance of himself and his wife and for the maintenance, education and benefit of all his children till his death". The sum of Rs.

14,170/-. it was stated, accrued as income in the hands of the assessee in the relevant account year from the said trust funds. The view of the taxing authorities and the Income- tax Appellate Tribunal was that under the aforesaid provision of the trust deed the assessee was the sole beneficiary and that the amount was received by him for his own benefit and he was not accountable to any one in respect of the amount and, therefore, this amount was liable to be included in his total income.

On behalf of the assessee the contention was that the sum of Rs. 410/- aforesaid was not liable to be included in the total income of the assessee inasmuch as Chandrika, the minor daughter of the assessee, had no right to the income nor any beneficial interest therein in the relevant year of account under the provisions of the trust deed and, therefore, neither s. 16(2)(a)(iv) nor s. 16(3)(b) applied to the case. As to the sum of Rs. 14,170/- the case of the assessee was that it should not be included in his total income as the sole beneficiary, because the beneficiaries under the trust settlement were not only the assessee but his wife and children as well. It was contended that the assessee received the amount in trust for himself and his wife and children and it was open to the Department to proceed under the first proviso to s. 41 (1) of the Income-tax Act and recover tax on a separate assessment made on the assessee as a trustee in respect of the said sum at the maximum rate, because the individual shares of the beneficiaries on whose behalf the money was receivable were indeterminate and not known.

The Income-tax Appellate Tribunal, on an appeal by the assessee, did not accept these contentions. The Tribunal was then moved to state a case to the High Court on two questions of law those questions were:

> "1. Whether the sum of Rs. 410/- is properly includible in the assessee's total income either in accordance with the provisions of section 16(3)(b) and/or section 16(3)(a)(iv) of the Indian Income-tax Act, 1922?
>
> 2. Whether the sum of Rs. 14,170/- is properly includible in the total income of the assessee as the sole beneficiary thereof under the trust settlement made on 1-12-1941 by Dhanji Devsi?"

On being satisfied that these questions of law arose out of the order of the Tribunal dated April 24, 1957, the Tribunal stated a case under s. 66(1) of the Income-tax Act. The High Court answered both the questions in favour of the assessee by its judgment and order dated September 25, 1958. There after the High Court granted a certificate of fitness under s. 66A(2) of the Income-tax Act and, as we have already stated, the present appeal has been brought to this Court on the strength of that certificate.

We proceed now to deal with the first question which relates to the sum of Rs. 410/-. The question is whether this sum was properly includible in the assessee's total income under the provisions of s. 16(3)(b) of the Income-tax Act, because Mr. Rajagopal Sastri appearing for the appellant has not pressed the claim which was made before the Tribunal on behalf of the Department under the provisions of s. 16(3)(a)(iv). Before we go to the provisions of s. 16(3)(b) it is advisable to set out the material portions of cls. 3 and 4 of the trust-deed of January 12, 1953. Those clauses were in these

terms:

> "3. The Trustees shall hold and stand possessed of the trust fund and the investments for the time being representing the same and receive the income, divided, interest and rents thereof and invest the same and the resulting income, dividend, interest and rents thereof so as to accumulate at compound interest to the intent that such accumulations shall be added to the principal trust fund until the settler's daughter Chandrika shall attain the age of eighteen years which age she will attain on the 1st February 1959 and after the expiration of the above named period the Trustees shall deal with and dispose of the trust fund as hereinafter stated.
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> 4. The Trustees shall hold and stand possessed of the trust fund and the accumulations thereof upon trust to pay the net interest and income thereof after deducting all out goings and charges for collection to the said Chandrika for her life for her maintenance..."

It is clear from these clauses that during the minority of Chandrika, the income from the trust funds was to be accumulated and added to the trust funds and after the attained majority on February 1, 1959, she was to get only the income from the enlarged trust funds. Now, in the relevant year of account Chandrika was still a minor and under the terms of the trust deed she had no right to the trust income nor any beneficial interest therein; she could neither receive nor enjoy the income. She did not derive any benefit whatsoever from the trust funds during her minority and even after she attained majority, she did not have any right to the trust income which arose during her minority and her only right was to enjoy the income arising from the enlarged trust funds, i. e., the original trust funds and the accumulations of trust income during her minority. Therefore, the sum of Rs. 410/-was not the income of Chandrika, but was the income of the trustees and the income was impressed with a trust, namely, that it should be added to the trust corpus. The question is, does s. 16(3)(b) apply to such a case ?

We shall presently read s. 16(3), but before we do so it is necessary to refer to the scheme of s. 16 of the Income-tax Act. The section deals with the computation of total income as defined in s. 2(15) of the Act, and provides that what sums are to be included or excluded in determining the total income. The definition of total income in s. 2(15) involves two elements-(a) the income must comprise the total amount of income, profits and gains referred to in s. 4(1), and (b) it must be computed in the manner laid down in the Act. The exemption granted under the Act is of two kinds; certain classes of income are exempted from tax and also excluded from the computation of total income, while certain other classes of income exempted from tax are to be included in the assessee's total income. Now cl. (a) of sub-s. (i) of s. 16 provides the sums exempted from tax under certain provisions of the Act should be included in the assessee's total income. Clause (b) lays down the mode of computing a partner's share in the profit or loss of the firm. Under cl. (c) income which arises to any person by virtue of any settlement or disposition from assets remaining the property of the settler or disponer etc. is taxed as his income. The object of the legislation is clearly designed to overtake and circumvent a tendency on the part of the tax-payers to endeavour to avoid or reduce tax liability by means of settlements. Sub-section (2) deals with grossing up of dividend etc. Then we

come to sub- s. (3). This sub-section aims at foiling an individual's attempt to avoid or reduce the incidence of tax by transferring his assets to his wife or minor child or admitting his wife as a partner or admitting his minor child to the benefits of a partnership in a firm in which such individual is a partner. The sub-section creates an artificial liability to tax and must be strictly construed. Now, let us read the sub-section.

> "16. (3) In computing the total income of any individual for the purpose of assessment there shall be included:
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> (a) so much of the income of a wife or minor child of such individual as arises directly or indirectly:
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> (i) from the membership of the wife in a firm of which her husband is a partner;
>
> (ii) from the admission of the minor to the benefits of partnership in a firm of which such individual is a partner;
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> (iii)from assets transferred directly or indirectly to the wife by the husband otherwise than for adequate consideration or in connection with an agreement to live apart; or
>
> (iv) from assets transferred directly or indirectly to the minor child, not being a married daughter by such individual otherwise than for adequate consideration; and
>
> (b) so much of the income of any person or association of persons as arises from assets transferred otherwise than for adequate consideration to the person or association by such individual for the benefit of his wife or a minor child or both."

The argument on behalf of the appellant is that the conditions laid down in cl. (b) of sub-s. (3) of s. 16 are fulfilled in the present case and therefore the Department was intitled to include in the total income of the assessee so much of the income in the hands of the trustees as arose from the assets transferred by the assessee for the benefit of his minor child. It is pointed out that the conditions laid down in cl.(b)are-(1) that there must be income in the hands of any person or association of persons (trustees in the present cases;) (2) the income must arise from assets transferred otherwise than for adequate consideration to the trustees; and (3) the transfer must be for the benefit of the minor child. It is argued that when the conditions are fulfilled and the only exceptional case, namely, where the transfer is for adequate consideration is out of the way, cl. (b) must apply and the Department is entitled to include the income in the hands of the trustees in computing the total income of the individual assessee who made the transfer.

At first sight the argument appears to be attractive and supported by the words used in the clause. On a closer scrutiny, however; it seems to us that cl. (b) must be read in the context of the scheme of 16 and the two clauses (a) and (b) of sub-s. (3) thereof must be read together. So read the only reasonable interpretation appears to be the one which the High Court accepted, namely, that the scheme of the section requires that an assessee can only be taxed on the income from a trust fund

for the benefit of his minor child, provided that in the year of account the minor child derives some benefit under the trust deed either he receives the income, or the income accrues to him, or he has a beneficial interest in the income in the relevant year of account. But if no income accrues, or no benefit derived and there is no income at all (so far as the minor child is concerned), then it is not consistent with the scheme of s. 16 that the income or benefit which is non-existent so far as the minor child is concerned, will be included in the income of his father. Take, for example, a case where the assets were transferred otherwise than for adequate consideration for the benefit of a minor child, but the child has attained majority before the relevant year of account. After the child attains majority the sub-section would cease to apply and the income from assets transferred for the benefit of the child would no longer be taxable in the parent's hands. The reason must be that in the relevant year of account there is no benefit to the minor child by the transfer, even though the transfer was originally made for the benefit of the child. The same principle may be illustrated by another example which has been dealt with by the High Court. Take a case where there are intermediate beneficiaries before the minor gets the benefit under the trust deed. In such a case the learned Advocate for the Department conceded in the High Court that cl. (b) of sub-s. (3) of s. 16 would not be attracted till the minor derived benefit under the trust deed. Mr. Rajagopal Sastri did not make any such concession before us; but seems to us that principle underlying the illustration is incontestable. If the minor derives no benefit in the relevant year of account, it can hardly be said that for that year the transfer was for the benefit of the minor child. Section 4, the charging section, of the Income-taxs Act makes it clear that what is taxed is the total income of the relevant account year, and total income, according to s. 2 (15), is the income, profits and gains referred to in sub-s. (1) of s. 4 and computed in the manner laid down in the Act. In other words, the tax is levied on a yearly basis. It is true that in the present case there was income in the hands of the trustees and the trustees were liable to pay tax thereon. That, however, is not the question before us. The question before us is whether such income in the hands of the trustees could be included in the total income of the assessee under cl. (b) of sub- s.(3) of s. 16. In our opinion, when cl. (b) of sub-s. (3) of s. 16 talks of benefit of the minor child it refers to benefit which arises or accrues to the minor in the year of account. If there be no such benefit, the income cannot be included in the total income of the individual who made the transfer. There is a third type of case which also illustrate the same principle. If only a portion of the income of the trust is reserved for the minor child, cl, (b) would apply and that portion of the income which is set apart for the benefit for the child would be taxable in the hands of the settler. All these illustrations only establish the principle that the minor child must derive some benefit in the relevant year of account before cl. (b) would apply.

Furthermore, we are also of the view that cls. (a) and (b) of the sub-section must be read together, Clause (a) begins with the expression "so much of the income of a wife or minor child of such individual as arises directly or indirectly", and this is followed by the four circumstances numbered (i), (ii), (iii) and (iv). There is no doubt that so far as cl. (a) is concerned, there must be income of the wife or minor child. Mr. Rajagopal Sastri has not disputed this. The obvious intention of the Legislature in enacting cl. (b) was to see that the provisions of cl. (a) were not defeated by the assessee creating a trust and in order to deal with that mischief it enacted cl. (b). Instead of the expression "so much of the income of a wife or minor child" the expression used in cl. (b) is "so much of the income of any person or association of persons etc.". Obviously, when a trust is created the income is income in the hands of the trustees. But the underlying principle in the two cls. (a) and

(b) appears to be the same, namely, there must be income of the wife or minor child under cl.(a) and there must be some benefit derived by the wife or minor child in the year of account under cl.(b). This is consistent with the scheme of s. 16 and particularly sub-s. (3) thereof. which is intended to foil an individual's attempt to avoid or reduce the incidence of tax by transferring his assets to his wife or minor child etc. When, however, the minor child derives no benefit under the trust deed in the year of account, it is not consistent with the scheme of s. 16 to say that even though there is no accrual of and income or benefit in the year of account in favour of the minor child, yet the income must be included in the total income of the individual concerned.

Our attention has been drawn to s. 64 of the Income-tax Act, 1961 (43 of 1961). That section corresponds to s. 16 of the Income-tax Act, 1922 and cl. (v) of s. 64 has made the position clear by using the expression 'immediate or deferred benefit" so that even a benefit which is postponed and does not arise in the year of account will not entitle the Department to include the income in the hands of the trustees in the total income of the settler. We do not, however, think that the Act of 1961 can be taken as declaratory of the law which excited previously; nor can s 64 (v) be taken as determinative of the true scope and effect of cl. (b) of sub-s. (3) of s. 16. The Legislature may have thought fit in its wisdom to widen the scope of the law that existed previous to it so as to take in deferred benefits as well. We think that we must interpret cl. (b) of sub-s. (3) of the context of the section as it occurs in the Income-tax Act of 1922.

We have been referred to two English decisions Dale v. Mitcalfe (1) and Mauray v. Commissioners of Inland Revenue (2). One of the decision Dale v. Mitcalfe (1) related to s. 25 of the English Income Tax Act, 1918 (8 & 9 Geo. V. C.

40) and the other related to s. 20(1)(c) of the English Finance Act 1922 (12 and 13 Geo V. C. 17). Those provisions were differently worded and appear in a different context and decisions of the English Courts given on provisions differently worded and appearing in a different context are not, in our opinion, helpful in determining the true scope and effect of cl. (b) sub-s. (3) of s. 16 of the Income-tax Act, 1922.

We have therefore, come to the conclusion that on a true construction of cl. (b) of sub-s. (3) of s. (3), the view expressed by the High Court was correct and the sum of Rs. 410/- did not form part of the total income of the assessee. The High Court correctly answered the first question referred to it.

We now turn to the second question. The relevant clause of the trust deed of December 1, 1941 is cl. 7 which reads as follows:

> "The trustees shall hold and stand possessed of the Trust Fund mentioned in the second Schedule hereto and the accumulations thereof referred to in clause 3 thereof upon Trust to pay the net interest and income thereof to the Settler's son MANILAL for the maintenance of himself, his wife and for the maintenance, education and benefit of all his children till his death."

The question before us is whether under this clause the income received by the assessee is impressed with a trust in favour of himself, his wife and children to whom he is accountable as a trustee for the amount received. In other words, the question is whether the trust deed of December 1, 1941, created two trusts, the one requiring the trustees to pay the income from the trusts funds to the assessee and the second requiring the assessee to spend the income for the maintenance of himself and his wife and for the maintenance, education and benefit of his children. In cases where property is given to a parent or other person standing or regarded as in loco parentis, with a direction touching the maintenance of the children, the question often arises whether the settler intended to impose a trust by the direction or whether the direction was only the motive of the gift. The line between the two classes of cases has not been drawn always very firmly. It is, however, clear that in construing provisions of this kind the Court will not enforce or treat as obligatory a mere wish or desire or hope on the part of the settler that the donee of the fund should or would ought to or is expected to apply it for the benefit of other persons; on the other hand, the Court does regard as binding and obligatory and does enforce a direction or trust in favour of third parties if such a binding obligation can be clearly ascertained from the document. Instances of cases where no trust is created and of cases where trust is created and detailed at pages 85 and 86 of Lewin on Trusts (15th Edition).

We are unable to hold that in the case before us cl. 7 of the trust deed merely expressed a wish or desire or hope on the part of the settler. We are in agreement with the High Court that the direction contained in cl. 7 created a trust in favour of the assessee, his wife and children. The expression "for the maintenance of himself and his wife and for the maintenance, education and benefit of all his children" is not indicative of a mere desire or hope. It imposes a binding and obligatory trust. In re. Booth, Booth v. Booth (1) a testator gave the residue of his estate to his executors, on trust, to pay to his wife or permit her to receive the annual income thereof during her life, "for her use and benefit and for the maintenance and education of my children". It was held that the wife took the income subject to a trust for the maintenance and education of the children. A similar view was expressed in Raikes v. Ward (1) and Woods v. Woods (2) On behalf of the appellant our attention was drawn to s. 8 of the Indian Trusts Act, 1882 (II of 1882) which states that the subject matter of a trust must be property transferable to the beneficiary and it must not be merely beneficial interest under a subsisting trust. It is contended that the assessee held a beneficial interest in the income from the trust funds under the trust deed of December 1, 1941, and in respect of beneficial interest another trust could not be created in favour of himself, his wife and children. We think that this argument proceeds on a misconception. The assessee did not create a second trust in respect of the beneficial interest which he held under the trust deed of December 1, 1914. The assessee father created two trusts by that trust deed, one requiring the trustees to pay the trust income to the assessee and the other requiring the assessee, who was himself a trustee, to spend the income for the maintenance, education and benefit of his children. It is not disputed that by a single document more than one trust may be created. It is not, therefore, true to say that the subject matter of the trust in the present case was merely a beneficial interest under a subsisting trust.

Under s. 41 of the Income-tax Act it was open to the Department either to tax; the trustees of the trust deed or to tax those on whose behalf the trustees had received the amount. The true position of the assessee in this case was that he was a trustee and not the sole beneficiary under the trust deed.

He held the income on trust for himself, his wife and his children. The shares of the beneficiaries were indeterminate and therefore under the first proviso to s. 41(1) of the Income-tax Act, it was open to the Department to levy and recover the tax at the maximum rate from the assessee; but that did not entitle the Department to include the sum of Rs. 14,170/- in the total income of the assessee as though he was the sole beneficiary under the trust deed, Mr. Rajagopal Sastri made it clear that the intention of the Department was to include the sum in the total income of the assessee in order to levy and charge super-tax on him. This, we do not think, the Department was entitled to do. In respect of the sum of Rs. 14,170/- the assessee was a trustee, within the meaning of s. 41 of the Income-tax Act, appointed under a trust declared by a duly executed instrument in writing and as such trustee he had the right to contend that his assessment in respect of the money received by him not as a beneficiary but as a trustee could only be made under the first proviso to s. 41 (1). We have, therefore, come to the conclusion that on the second question also the answer given by the High Court was correct.

The result, therefore, is that the appeal fails and is dismissed with costs.

Appeal dismissed.