

(1969) 05 CAL CK 0017

In the Calcutta High Court

Case No : Income-tax Reference No. 10 of 1966

Chhaganlal Baid

APPELLANT

Vs

Commissioner of Income Tax

RESPONDENT

Date of Decision : 22-05-1969

Acts Referred:

Income Tax Act, 1922 — Section 16(3)

Citation : (1971) 79 ITR 258

Hon'ble Judges : Sankar Prasad Mitra, J; Sabyasachi Mukharji, J

Bench : Division Bench

Advocate : Anil Mitra, S.K. Banerjee and R.N. Bajoria, for the Appellant; B.L. Pal and Manas Roy, for the Respondent

Judgement

Sabyasachi Mukharji, J.—This reference arises out of the assessments made for the assessment years 1958-59, 1959-60, 1960-61 and 1961-62 for which the corresponding accounting periods were 2014 R. N. (9th April, 1957, to 28th March, 1958), 2015 R.N. (29th March, 1958, to 16th April, 1959), 2016 R. N. (17th April, 1959, to 4th April, 1960) and 2017 R. N. (5th April, 1960, to 25th March, 1961), respectively. The assessee, Sri Chhaganlal Baid, has been assessed for these years in the status of an individual. The assessee is the owner of premises, No. 91, Harrison Road, and No. 6, Sambhu Chatterjee Street, Calcutta, both the holding numbers denote one property which is a cinema house and which has been leased out by the assessee. The rent reserved under the lease is Rs. 4,500 per month or Rs. 54,000 for the whole year. In January, 1958, the assessee had six sons who were as follows:

1. Kharag Singh Baid ... 23 years (Major)
2. Bardhaman Baid ... 19 years (Major)
3. Surendra Kumar Baid ... 12 years (Minor)
4. Mahendra Kumar Baid ... 8 years (Minor)

5. Narendra Kumar Baid ... 6 years (Minor)

6. Rabindra Kumar Baid ... 4 years (Minor)

2. By four several identical deeds of trust, all dated and executed on the 15th January, 1958, the assessee transferred unto his two major sons Kharag Singh Baid and Bardhaman Baid, 1/6th part of the share of furniture, goods, chattels, effects and machinery in and upon the said premises as mentioned in the said deeds for each of his four minor sons. The trustees were directed to collect the rents, issues and profits of the trust property and, in the first instance, to pay all rates and taxes, land revenue, collection charges, cost and expenses of repairs and maintenance of the property, legal expenses for collection of rents and all other outgoings whatsoever concerning the same and to hold the balance of the net income of the trust property in trust for the benefit and absolute use of each of his four sons. The trust deed which has been annexed in the paper book is an incorrect one. By consent of the parties a copy of the correct trust deed has been exhibited in this case. Clause (2) of the said trust deed provides as follows:

" (2) The trustees shall hold the balance of the net income of the trust properties in trust for the benefit and absolute use of the said beneficiary Mahendra Kumar Baid until the youngest son of the said settlor attains the age of 18 years. On the attainment of the age of 18 years by the said youngest son of the settlor the accumulated income of the said property in the hands of the trustees (if any) after disbursement of such sums as might have been advanced by the trustees from time to time for the maintenance, education, advancement or benefit of the said beneficiary in terms of Clause (4) hereof will be handed over to the said beneficiary by the said trustees for his absolute use and benefit and the trustees shall also convey and transfer the said trust property to the said beneficiary for his absolute use and benefit."

3. Clause (4) of the said trust deed is as follows :

" (4) The trustees shall be entitled to advance and spend such sum or sums of money out of the income of the said trust property for the maintenance, education, advancement or benefit of the said beneficiary as the trustees may in their discretion deem fit but so that the amount to be advanced for the maintenance, education, advancement or benefit of the said beneficiary shall not on any account exceed the amount of the income."

4. For the assessment years 1958-59, 1959-60, 1960-61 and 1961-62, the Income Tax Officer held that the transfer of the assets to the trustees by the assessee had not been made for adequate consideration and accordingly the income of the beneficiaries under the trust deeds were to be assessed in the hands of the assessee u/s 16(3) of the Indian Income Tax Act, 1922.

5. The assessee preferred appeals before the Appellate Assistant Commissioner, who disposed of the same by one consolidated order dated 29th June, 1963. It was contended by the assessee that the income from the trust could not be

included in the assessee's total income u/s 16(3) of the Indian Income Tax Act, 1922, as under the terms of the trust deeds no part of the income of the trust arose to the minor beneficiaries and no part thereof was received by the said minors. It was contended that under the terms of the trust deeds, the trustees were directed to accumulate the income after meeting all the outgoings until the youngest son attained the age of 18 years and as no part of such income was utilised for the benefit of the minor beneficiaries, the provisions of Section 16(3)(b) were not applicable to this case. The Appellate Assistant Commissioner referred to Clauses (2) and (4) of the trust deeds and came to the conclusion that the trusts were for the benefit of the minor children of the assessee and held that the income from the trust was, therefore, properly included in the assessee's total income under the provisions of Section 16(3)(b) of the Indian Income Tax Act, 1922.

6. There was a further appeal to the Tribunal. It was contended on behalf of the assessee before the Tribunal that during the accounting years under appeal, no benefits were derived by the minors from the trust as the whole of the trust income was accumulated by the trustees and nothing was advanced for the maintenance and education of the minors in terms of Clause (4) of the trust deed. The Tribunal was of the opinion that under Clauses (2) and (4) of the trust deeds under consideration, the minors acquired beneficial interest in the income during the relevant years and the income of the trustees were correctly included in the total income of the assessee u/s 16(3)(b) of the Indian Income Tax Act, 1922. The Tribunal, therefore, dismissed the appeals.

7. On application being made u/s 66(1) of the Indian Income Tax Act, 1922, the following question has been referred to this court:

" Whether, on the facts and in the circumstances of the case and on a proper construction of the provisions of the relevant trust deeds, the Tribunal was right in holding that the minor beneficiaries acquired beneficial interest in the income of the trust property during the relevant years of account and the income of the trustees under the four deeds of trust in favour of the minor children of the assessee were correctly included in his total income u/s 16(3)(b) of the Indian Income Tax Act, 1922?"

8. Section 16(3)(b) of the Indian Income Tax Act, 1922, with which we are concerned in this reference states that, in computing the total income of an individual for the purpose of the assessment, there shall be included 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 minor child or both. In this case the assessee has transferred certain assets to the trustees. It has not been contended before us that such transfers have taken place for adequate consideration. Income has arisen to the trustee from the said assets which had been transferred by the assessee. The question is whether that income should be included in the total income of the assessee. For the determination of that

question it would be necessary to determine whether such transfer to the trustee was made by the assessee for the benefit of his wife or minor child or both. The provisions of Section 16(3)(b) of the Indian Income Tax Act, 1922, were considered by the Supreme Court in the case of *The Commissioner of Income Tax Bombay Vs. Manilal Dhanji, Bombay*, . In that case what had happened was that the assessee had created a trust in 1953, in respect of the sum of Rs. 25,000, the trustees whereof were four persons including 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 was to receive the income of the corpus increased by the addition of the interest when she attained the age of 18 on 1st February, 1959. She was to receive the income during her lifetime and after her death the corpus was to go to other persons. The income derived from the trust fund amounted to Rs. 410 in the relevant year of account, 1953-54, and the taxing authorities had included this amount in the total income of the assessee purporting to act u/s 16(3)(b) or Section 16(3)(a)(iv) of the Indian Income Tax Act, 1922. The propriety of such inclusion was challenged in reference and the High Court of Bombay held against the department and in favour of the assessee. The appeal went to the Supreme Court therefrom. In its judgment the Supreme Court observed at page 882 of the report:

" On a closer scrutiny, however, it seems to us that Clause (b) must be read in the context of the scheme of Section 16 and the two Clauses (a) and (b) of Sub-section t3) 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 is 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 Section 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."

9. Before that, dealing with the facts of the case at page 880 of the report, the Supreme Court has observed :

" 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 fund and after she attained majority on 1st February, 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 accumulations of trust income during her minority. "

10. It is important to bear in mind that the Supreme Court has emphasised, in explaining the background of the facts in that case, the fact that the minor beneficiary would have no right to the trust income which would arise during the minority of the said beneficiary. The question, therefore, is whether, in the facts of this case in the relevant year of account, the minor beneficiary had any beneficial interest in the income which arose from the assets transferred by the assessee to the trustees. Beneficial interest has been defined by Section 3 of the Indian Trusts Act as the right of the beneficiary against the trustee as owner of that trust property.

11. In the instant case before us, the trustees were enjoined by Clause (2) of the trust deed, to hold the balance of the income for the benefit and absolute use of the beneficiaries until they attained the age of 18 and on the attainment of the age of 18 of the youngest son of the settlor the accumulated income of the trust property in the hands of the trustees, after the disbursements of such sums as contemplated by Clause (4), and the expenses mentioned in Clause (1), should be handed over to the respective beneficiary along with the trust property for the absolute use and benefit of the said beneficiary. Therefore, the beneficiary has a right to the accumulation of the income year by year arising from the trust funds until the beneficiary attains the age of 18 and then the minor would have the trust income which arises during his minority. The question is, can that right be described as beneficial interest or benefit arising to the minor in the relevant year of account u/s 16(3)(b) of the Act. Then there is Clause (4) of the trust deed under which the beneficiary has a right to claim maintenance from the trustees if such maintenance is required or moneys to be spent for the advancement of education or benefit of the beneficiary, if such moneys are required, though such moneys to be spent would be in the discretion of the trustees, subject to the fact that the amount spent should not exceed the amount of the income of the year. Such a clause creates a discretionary trust in favour of the beneficiary. This position will appear from Halsbury's Laws of England, 3rd edition, volume 38, page 876, Article 1479, where it has been observed as follows :

" A trust to apply the income of property for the benefit of a person or object in a special manner or in such a manner as the trustees think fit is an absolute trust for that person or object. A trust to apply the whole or part of the income for a special purpose for the benefit of a person is, however, a trust for him of only so much as is necessary for that purpose; and, if the trustees in such a case are given a discretion as to the amount to be applied they are at liberty to exercise that discretion by limiting the amount."

12. Mr. A.C. Mitra and, following him, Mr. S.K. Banerjee, learned counsel for the

assessee, contended that in view of the language of Clause (2) and Clause (4) of the trust deed, there is no benefit or beneficial interest accruing to the minor child in the relevant accounting year. It was urged on behalf of the assessee that no income or amount has in fact been spent in this year for the benefit of the minor. There is no evidence, it was urged on behalf of the assessee, that the trustees have not properly exercised the discretion in not making any disbursement in the relevant accounting year for the maintenance, education or advancement of the beneficiaries. According to the counsel for the assessee this case, therefore, comes within the ratio of the decision of the Supreme Court in the case of *The Commissioner of Income Tax Bombay Vs. Manilal Dhanji, Bombay*, . Reliance was placed on behalf of the assessee on the decision of *Commissioner of Income Tax, Kerala Vs. Hajee Hassan Yacoob Sait (Deceased) and Others*, , and the decision of this court in *Commissioner of Income Tax v. A.N. Chowdhury* [1969] 71 ITR 326 (Cal.). It was then urged that the trust created by Clause (4) of the deed was a discretionary trust and unless there is evidence that the trustees have improperly or mala fide exercised the discretion, the beneficiaries would have no right and as such there is no scope for arguing that the beneficiaries have any benefit or beneficial interest in the income of the trust property in the relevant accounting year. Reliance was also placed on *In re Vestey's Settlement* [1950] 2 All E.R. 891 (C.A.), and on *In re Bryant* [1894] 1 Ch. 324 (Ch. D.), and also on Section 49 of the Indian Trusts Act.

13. We are unable to accept the contentions made on behalf of the assessee. The clauses in the instant deed of trust, specially Clause (2) and Clause (4), are different from the clauses appearing in the deed of settlement that came up for consideration before the Supreme Court. Firstly, under Clause (2) of the deed of trust in the instant reference before us there is an obligation on the part of the trustees to accumulate the income of the year including the income of the relevant accounting year, after disbursement of costs, charges and expenses as mentioned in Clause (1) of the deed of trust and after disbursement, if any, made for the benefit of the minor as mentioned in Clause (4). The minor on the attainment of majority will be entitled to have this accumulated income including the income of the relevant year in question. This is a factor which is different from the position as noted in the judgment of the Supreme Court and as mentioned hereinbefore. Secondly, in the trust deed in the instant reference there is the clause for making disbursement for the maintenance, advancement or education or benefit of the minor, subject to the discretion of the trustees, even in the relevant accounting year. Such a clause was not there in the trust deed which the Supreme Court had occasion to consider. The case of *Commissioner of Income Tax v. Hajee Hassan Yacoob Sait* was decided mainly on the basis of the decision of the Supreme Court case referred to hereinbefore. It does not appear from the judgment whether there was any clause which their Lordships had to construe in the trust deed like Clause (4) of the trust deed in the instant reference. The clauses set out in the judgment appear to be more or less in similar terms as the trust deed the Supreme Court had occasion to

consider. The decision of this court in the case of Commissioner of Income Tax v. A.N. Chowdhury has not dealt with the construction of the clauses like the clauses which we have to construe in Clause (2) and Clause (4) of the instant reference. The said decision was not concerned with the question whether the minor beneficiaries derived any interest or benefit in the year of account under consideration in that case. In that view of the matter, we do not think that the said decision can be availed of in aid of the argument in support of the assessee.

14. The two English decisions relied on behalf of the assessee also do not help us to resolve the controversy in the present case. In the case, *In re Bryant*, what had happened was, the testator had declared that, from and after the decease or marriage again of his wife, who was a tenant for life of the whole estate during the widowhood, and also one of the trustees, his trustees should apply the whole or such part as they should think fit, of the income of the expectant share of any child, for or towards the maintenance, education or benefit of such child. The wife had married again, whereupon, her income was reduced to a certain extent. The testator's children were quite young and had continued to reside with their mother, who had maintained and educated them as formerly, though the mother had applied to her co-trustees to make her an allowance of ₹300 per annum, out of the testator's residuary estate, towards their maintenance. The co-trustees, in the exercise of their discretion declined to make any such allowance. Thereupon, an application was made on behalf of the infants for an order directing the trustees to pay a reasonable sum for their future maintenance. It was held by Chitty J. that, on the construction of the document, it created a discretionary trust equivalent to a power ; and the co-trustees having, in the bona fide exercise of their discretion, refused to make any allowance for maintenance, the court could not compel the payment and overrule their discretion. In those circumstances, the application was refused. The decision does not deal with the question whether even in a case of discretionary trust the beneficiary has any right against the trustees or acquires any beneficial interest. Moreover, the case was not concerned with the construction of a clause like Clause (2) of the trust deed before us. In *In re Vestey's Settlement: Lloyds Bank Ltd. v. O'Meara* [1950] 2 All E.R. 891 (C.A.), what had happened was that by Clause 7 of a settlement made in 1935, the settlor had directed that, during a specified period, the trustees " shall pay or apply the income " of the trust fund " unto or in any manner for the support or benefit of all or anyone or more " of a named class of persons, " such payment or application" to be made in such shares, in such manner and on such terms, as the trustees should in their discretion think fit. The objects of the discretionary trusts were in that case the members of the settlor's family and consisted, at all material times, of a number of adults and infants. At the end of the specified period under the trust deed the corpus of the trust fund was to be divided among a named class. None of the beneficiaries of the discretionary trust had a vested interest in the corpus, but the infant beneficiaries had contingent reversionary interests therein, such interests being contingent on their surviving the end of the specified period. By a resolution

made on the 2nd of February, 1949, and purporting to be in exercise of their discretionary power under Clause 7, the trustees decided that, after the payment of certain sums to the adult beneficiaries, the balance of the income which they decided to make available for immediate distribution in each half year " shall belong " in specified shares to each of the infant beneficiaries, and they then proceeded to allocate the shares for the half year ending September 30, 1948. They then resolved that, as none of the income falling in that half year to the infant beneficiaries under the first part of their resolution was required for the maintenance of the infants, " that income should be accumulated in accordance with Section 31 of the Trustee Act, 1925". By a resolution dated April 29, 1949, the trustees resolved "to divide " the balance of the income of the half year ending March 31, 1949, among the infant beneficiaries, and for the same reasons as before, that the income should be accumulated. It was held that the allocations made by the trustees were within the power of the trustees under Clause 7 of the deed of settlement. It was further held that as the infants had merely contingent reversionary interests in the corpus of the fund and the reversionary interests in the corpus did not carry the intermediate income and were thus excluded from the application of Section 31 of the Trustee Act, 1925. It was further observed that under the terms of the discretionary trust, no infant had any share or interest in the income unless and until the trustees, in the exercise of their discretion, decided to pay or apply to or for the support or benefit of that infant some part of the income from time to time in hand, but, on a sum of income being allocated to him under the trustees' discretion, the infant became absolutely entitled to it, and, therefore, Section 31 of the Trustee Act, 1925, did not apply to that sum. It has to be observed that the court found that on the construction of the deed the infant had no right on the intermediate income. As mentioned before, under Clause (2) of the trust deed before us, the infant beneficiary would have the accumulated income including the income of the relevant year in question on the attainment of majority. Furthermore, the question whether a beneficiary in the case of a discretionary trust would have the right to compel the trustees to exercise the discretion or compel the performance of the trust, did not fall for consideration in that case. The case depended upon the construction of the clauses which were different from the clauses in the present reference, and on the provisions of Section 31 of the Trustee Act of 1925.

15. Section 16(3)(b) of the Indian Income Tax Act, 1922, creates an artificial liability. It has, therefore, to be strictly construed. The purpose of the enactment of this section was to defeat the endeavour on the part of the taxpayer to avoid or reduce the liability of taxation by means of settlements or trusts. The controversy in this case has to be resolved by reference to Section 16(3)(b) of the Indian Income Tax Act, 1922, the terms of the trust, and the provisions of the Indian Trusts Act. Under the terms of the trust deed in the instant case before us the beneficiary has a right to get the income of the trust property accumulated year by year, and after the disbursements of costs, charges and expenses as mentioned in Clause (1) and of such sums, if any, made by the

trustees in their discretion under Clause (4) of the trust deed. That benefit accrues or arises to the assessee, viz., the right to have the income accumulated in the year relevant for the present assessment. It is not a case of deferred benefit, i.e., the benefit arises in the year of account but the enjoyment of that right is postponed. Then under Clause (4) there is a discretionary trust. But even in a case where there is a discretionary trust the beneficiary has a beneficial interest, in the sense of a right to compel proper exercise of discretion by the trustee if such a need arises. That right the minor beneficiary had even in the relevant accounting year. Section 49 of the Indian Trusts Act confirms that right of the beneficiary and does not nullify it. The fact that in a particular year there was no need to exercise that right or that right was in fact not exercised is immaterial for the determination of the question whether the beneficiary had that right or not. Therefore, it appears that in the year of account the minor derived certain benefits from the trust property, he had the right of accumulation of income of the year subject to disbursement for his advancement, maintenance or education, if any, made by the trustees in their discretion. The minor beneficiary had also the right to enforce disbursement and compel exercise of discretion by the trustees in the year relevant for the present purpose in case there was need for his benefit or education or advancement or maintenance. This would be benefit derived by the minor under the trust deed and the beneficial interest accrued to the minor are the income of the trust property in the relevant year of account.

16. In that view of the matter we are of the opinion that the Tribunal was right in its conclusion and the answer to the question referred to his court must be in the affirmative. The assessee will pay the costs of this reference.

Shankar Prasad Mitra, J.

17. I agree.