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**(1984) 10 KL CK 0016**

**In the High Court Of Kerala**

**Case No :** Income Tax R. No's. 84 to 86 and 125 of 1979 and 71 to 77 of 1981

Commissioner of Income Tax

APPELLANT

Vs

Parthas Trust

RESPONDENT

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**Date of Decision :** 21-10-1984

**Acts Referred:**

Income Tax Act, 1961 — Section 160(1), 161  
Trusts Act, 1882 — Section 7

**Citation :** (1984) 10 KL CK 0016

**Hon'ble Judges :** K. Bhaskaran, Acting C.J.; M.P. Menon, J

**Bench :** Division Bench

**Advocate :** P.K.R. Menon and N.R.K. Nair, for the Appellant; G. Sivarajan, C.S. Balagangadharan and Joseph J. Theyenkeril, for the Respondent

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## **Judgement**

K. Bhaskaran, Actg. C.J.

1. We would first deal with ITRs Nos. 84 to 86 of 1979. The question referred to this court in ITR No. 125 of 1979 being identical to the one in ITRs Nos. 84 to 86 of 1979, we would answer the questions referred in ITR No. 125 of 1979 in the light of the conclusions reached in ITRs Nos. 84 to 86 of 1979. The important question referred to this court in ITRs Nos. 71 to 77 of 1981 is also identical to the one in ITRs Nos. 84 to 86 of 1979, and applying the conclusions reached in ITRs Nos. 84 to 86 of 1979, we would answer the questions referred in ITRs Nos. 71 to 77 of 1981.

2. The Income Tax Appellate Tribunal, Cochin Bench, at the instance of the Revenue, has drawn up a statement of the case and referred the following question in ITRs Nos. 84 to 86 of 1979 to this court u/s 256(1) of the Income Tax Act, 1961 ;

" Whether, on the facts and in the circumstances of the case, there was a valid trust so that the trustees could be assessed in their representative capacity u/s 160(1)(iv) in respect of the income of each beneficiary as claimed by the

assessee ? "

3. The short facts, relevant for the purpose of the case, could be stated as follows: The assessee, the Parthas Trust, Kottayam, is a private trust, of which the author (hereinafter referred to as " the founder ") is Smt. Ramachandru Ammal, the widow of Lakshmana Reddiar, the founder of the two business houses known as " Parthas Textiles, Kottayam " and " Parthas Textiles, Attingal ". The firm which conducted the business at Kottayam and in its branches, had 7 partners, all of them being the sons of the said Lakshmana Reddiar (now deceased), and the firm which conducted the business at Attingal had six partners, three of them being his sons, two being his daughters-in-law and one being his brother-in-law. The two firms together had 10 persons as partners, the three sons of Lakshmana Reddiar being common partners in the said firms. There are two partners admitted to the benefits of the partnership in the Kottayam firm; and one among them (Sivakumar) is a partner in the Attingal firm also. There are altogether 28 beneficiaries of the trust; and they included the partners of the two firms mentioned above, and other relatives like the grandchildren, nephews, nieces and daughters-in-law of the late Lakshmana Reddiar.

4. On July 21, 1971, Sri Veeriah Mohan Raj, one of the partners of the Kottayam firm, made an agreement with the said Smt. Ramachandru Ammal (the founder) to hand over the business to her as a going concern to enable her to form a trust for the benefit of the family members. The transfer was to be effected on any date not later than August 17, 1971. An agreement in identical terms was entered into by Sri Nagarajulu on behalf of the Attingal firm with the said Smt. Ramachandru Ammal (the founder). On August 3, 1971, the beneficiaries who were not partners of either of the firms, but were having their accounts in the books of the Kottayam firm, individually wrote to that firm authorising it to debit to their accounts and pay certain amounts to the founder. The founder in her turn on the same day wrote to the Kottayam firm requiring it to pay a sum of Rs. 1,40,000 to her on the strength of the letters of authorisation. The founder herself authorised a payment of Rs. 18,200 which was to be the subject-matter of the trust; and that was to provide contribution to four minors. The founder who had no account with the Kottayam firm till August 3, 1971, paid in cash a sum of Rs. 15,400; and that is evidenced by a journal entry in the books of the Kottayam firm which showed that that payment was intended for the trust fund for Sivakumar and Indumathy, minor daughters of the founder. She had also gifted Rs. 2,000 each to the minors, Raghunathan and Ravichandran, towards the trust fund. In the accounts maintained in Tamil, the payments in favour of the founder instead of having been credited to her account and then by a transfer credited to the trust account, were straightaway credited to the trust fund. Necessary entries in the books of account of the Kottayam firm were made on the basis of the authorisation letters. The contributions on behalf of the beneficiaries who were minors were made in the form of gifts. For instance, on receipt of the authorisation letter from Viswanathan, the Kottayam firm debited

his account with Rs. 2,000 on August 3, 1971. Corresponding credit was given to Parthas Trust--Rs. 1,600 to the founder and Rs. 400 to Arjunan. Though on August 4, 1971, a cheque for Rs. 1,40,000 was drawn payable to Parthas Trust, the said cheque was not presented for payment. The persons who issued the cheques were, however, debited with the amounts and credit given to the trust in the books of the Kottayam firm. The trust deed was made out and registered on August 4, 1971. The deed declared that Smt. Rama-chandru Animal was the founder of the trust, her son, Mohan Raj, her brother, Srinivasa Reddiar, and one Sri Varada Venkata Raju were the trustees. The preamble to the trust mentioned 28 persons as beneficiaries, of which 12 were minors. According to the deed, the 28 persons had agreed with the founder to deliver to her the business assets of the two firms and a sum of Rs. 1,40,000. It specified the shares of the beneficiaries and generally outlined the rights and duties of the trustees. The trust was to be determined on August 16, 1978 ; the income of the trust was to be used for the maintenance, welfare and comfortable living of the beneficiaries (annexures C and D at pages 10 to 20 of the paper book are the trust deed and the rectification deed respectively). On August 6, 1971, in pursuance of the declaration in the trust deed, the partners of the two firms (including the minors admitted to the benefits of the partnership and represented by their guardians) entered into an agreement with the trustees that they would assign the goodwill, the trade name " Parthas Textiles", the book debts, securities for the debts and the benefit of the contracts with effect from August 17, 1971, to the trust. On August 17, 1971, the assets and liabilities as per the agreement of August 6, 1971, were taken over by the trustees. These agreements, witnessing such take-over, were signed by the-managing partners on behalf of the firms. The two firms had certain immovable properties. The managing partners of the respective firms entered into an agreement for sale in respect of those properties. The title deeds were given over to the trustees; and they were given possession of the properties. They specifically agreed to execute a registered deed as and when demanded by the trustees. The transfer, however, had not been registered. From August 17, 1971, onwards, the trustees conducted the business as successors to the two firms. The books of account" were closed on March 31, 1972 ; and the trustees filed their Income Tax returns for the assessment year 1972-73, in which they claimed that they were assessable u/s 161 of the Income Tax Act, since the beneficiaries under the trust were known, and their shares were ascertainable. Similar claims were made for the assessment years 1973-74 and 1974-75 also. The Income Tax Officer rejected these claims and assessed them as an association of persons (vide annexures G-1, G-2 and G-3 assessment orders at pages 35 to 49 of the paper book). The assessee's appeal was allowed by the Appellate Assistant Commissioner (vide annexures H-1, H-2 and H-3 at pages 50 to 63 of the paper book) and the decision of the Appellate Assistant Commissioner was confirmed by the Tribunal in second appeal (vide annexure I at pages 64 to 75 of the paper book).

5. In rejecting the assessee's claim to have the assessment u/s 161 read with

Section 160(1)(iv), the Income Tax Officer gave three reasons :

- (i) the founder had no property to be transferred to the trust;
- (ii) the properties of the minors had been made the subject-matter of the trust without satisfying the conditions of Section 7(b) of the Trusts Act;
- (iii) the immovable properties have been made the subject-matter of the trust without a valid transfer.

6. The Appellate Assistant Commissioner found that (i) when the trust deed was considered as a whole, the minors were not the authors of the trust; (ii) the immovable properties were not the subject-matter of the trust; and (iii) Sections 5 and 6 of the Trusts Act had been satisfied. Having found that the beneficiaries under the trust were known and their shares were ascertainable, the Appellate Assistant Commissioner held that the assessment was to be u/s 161 of the Income Tax Act. The Tribunal upheld the findings of the Appellate Assistant Commissioner giving reasons in paragraphs 18 to 25 of the order (annexure H-1). Shri N. R. K. Nair, counsel for the Revenue, submitted that it could be seen that Smt. Ramachandru Amrnal, who claimed to be the founder of the trust, had no money to be contributed or transferred to the trust, and, therefore, the trust founded by the beneficiaries without the founder having contributed anything to it was invalid. We find that there is no factual foundation for this submission. On August 3, 1971, a sum of Rs. 1,40,000 was made available by the two firms to the founder ; and that had become her property, before the trust came into existence on August 4, 1971, The fact that the cheque for Rs. 1,40,000 was not presented for payment is not material, inasmuch as the fact of credit having been given to that amount to the trust on behalf of Smt. Ramachandru Animal, in whose favour the cheque was issued, is borne out by the relevant entries in the books of account of the Kottayam firm. The procedure adopted in giving credit in the books of account, written in Tamil, has already been explained. That is to say, instead of crediting the account of the founder, and then debiting it to her account by transfer, and, lastly, crediting the account of the trust, a short-cut method, whereby the account of the trust was credited straightaway on the basis of the directions given by Smt. Ramachandru Ammal, with respect to the authorisation letters, was adopted. We, therefore, fail to understand how the Income Tax Officer came to the conclusion that the founder contributed no amount to the trust fund.

7. Equally untenable is the reasoning of the Income Tax Officer that the minors, among the beneficiaries, had made contributions to the trust fund ; and that it was not valid for not having obtained the consent of the principal civil court of original jurisdiction as required u/s 7(b) of the Indian Trusts Act, We have already noticed, while narrating the facts of the case, that the amounts towards the corpus of the trust, on behalf of the minors, was contributed by their guardians, not by them. That would, therefore, mean that there was no need for obtaining the consent of the principal civil court in that behalf, inasmuch as no

amount of the minors was used for the creation of trust. As a matter of fact, in paragraph 3 of the assessment order, annexure G-1, at page 36, the Income Tax Officer himself has stated as follows :

" Among the authors of the trust, 12 persons are minors and they have transferred properties through their guardians. u/s 7(b) of the Trusts Act, a trust by or on behalf of a minor can be created only with the permission of the principal civil court of original jurisdiction. In response to a letter issued from this office enquiring whether the court's sanction has been obtained, the assessee's authorised representative, Sri L. Rengamani, C. A., filed a written reply. The matter was discussed with him also. In the reply, it is submitted that the minors have not transferred the property. It is further represented that majors have transferred property to the trust for the minors with the specific direction that the funds are transferred for the corpus of the trust. He also represented that Smt. Ramachandru Ammal has transferred sums in respect of her two minor children, K. L. Sivakumar and K. L. Indumathy, In support of the assesseds claim he filed copies of the journal entries by which the transfer entries for the corpus of the trust were made. These journal entries filed were verified by me with reference to the books produced and found correct. It was also submitted by the representative that for this transfer of the sum, no court sanction is necessary. It was also argued by the representative that the transfer of the business of the two firms was made after the formation of the trust, i. e., the trust was formed on August 4, 1971, and the transfers were made on August 6, 1971, and August 17, 1971. Hence, it was argued by the assessee's representative that the subsequent act does not affect the validity of the trust." (emphasis\* supplied)

8. Section 7(b) of the Trusts Act, reads as follows:

" 7. Who may create trusts.--A trust may be created--...

(b) with the permission of a principal civil court of original jurisdiction, by or on behalf of a minor. "

9. This, as we have already found, has no application to the present case, inasmuch as the funds were made available by the majors and no contribution was made to the funds of the trust by the minors themselves.

10. The Income Tax Officer is seen to have taken the view that in paragraph 2 of annexure "C" trust deed, the minors by themselves or through their natural guardians had agreed to transfer and assign the sums of money to the trustees upon trust. Under Clause 17 thereof, the trustees accepted the trust and acknowledged receipts of the sum from each of the minors as well. It is, in this context, one has to bear in mind that the clauses in a deed have to be read and considered as a whole, as otherwise a distorted version of the idea sought to be conveyed might result. As it has already been pointed out, the journal entries showed that the contributions to the corpus of the trust fund so far as the minors were concerned, were made by the majors ; and these were done on August 6, 1971.. and August 17, 1971, after annexure "C" trust deed was made out and

registered on August A, 1971. Sections of the Trusts Act lays down :

" A trust is an obligation annexed to the ownership of property and arising out of a confidence reposed in and accepted by the owner, or declared and accepted by him, for the benefit of another, or of another and the owner. "

11. Section 4 defines " lawful purpose " thus :

" A trust may be created for any lawful purpose. The purpose of a trust is lawful unless it is (a) forbidden by law, or (b) is of such a nature that, if permitted, it would defeat the provisions of any law, or (c) is fraudulent, or (d) involves or implies injury to the person or property of another, or (e) the court regards it as immoral or opposed to public policy."

12. For a trust to be unlawful and, therefore, void, it has to be shown that the deed is vitiated by any of the circumstances stated above. It has not been shown that the formation of the trust is forbidden by any law, or that it would defeat the provisions of the law, or that it is fraudulent, or that it involves or implies injury to the property of another or that it is immoral or opposed to public policy.

13. It was contended by Sri Nair, placing reliance on a Division Bench ruling of the Sind High Court in *Ismail Jakira & Co. v. Burmah Shell Provident Trust Ltd.*, AIR 1942 Sin 47, that the mere fact that a cheque was issued in favour of the founder, in the absence of proof of it having been encashed, would not make Smt. Ramachandru Animal, the founder of the trust. On a careful reading of the decision in the above case, we find that the decision has absolutely no relevance to the present case. That was a case in which one Abdul Rahman Barkatullah, an employee of Messrs. Burmah-Shell Oil Storage and Distributing Co. of India Ltd., had contributed to the company's provident fund for its employees, called the Labour Provident Fund. On October 11, 1934, the plaintiff in the suit attached a certain sum out of the moneys lying to the credit of Abdul Rahman in the fund. On October 21, 1934, Abdul Rahman retired from the service of the company, whereupon the company paid to Abdul Rahman the entire sum that was due to him in accordance with the Provident Fund Rules. In 1936, the plaintiff applied for the sale of the moneys attached by the prohibitory order in the suit in the hands of the defendant-company. At the auction sale held on April 27, 1936, the plaintiffs were permitted to bid; they purchased the debt in question and brought a suit for recovery of Rs. 81-14-3 against the defendant company contending that the defendant-company was bound to withhold the said sum from Abdul Rahman. The judge of the Small Causes Court raised two points for determination, viz:

(i) Was a debt due to Abdul Rahman on the date of attachment, viz., October 11, 1934? If so, was it attachable, and to what extent ?

(ii) If the debt was only partly attachable, can the plaintiff succeed in obtaining the relief sought ?

14. The learned judge found on the first point that there was no debt in the

hands of the defendants over which the debtor had a disposing power, and that there was nothing in the hands of the defendants which could be attached. On the second point, no finding was recorded as it was unnecessary. The defendants had contended in answer to the plaintiffs' suit that, firstly, Abdul Rahman Barkatullah had created a trust within the meaning of Section 3, the Trusts Act, and that, secondly, in any case what was attached was not a debt within the meaning of Section 60(1), C. P. C. The learned judge quoted the following passage set out by Kennedy J. C. in 18 S. L. R. 311 : AIR 1942 Sin 47:

"Nor is it a trust. Quite apart from any question of the validity of the instrument to create a trust, there is the consideration that as said before, Master was at perfect liberty to withdraw the whole amount if he retired or to nominate a new nominee. Neither the trust fund nor was the beneficiary therefore clearly indicated. But these are essentials of a trust. I think then that as far as the ordinary law goes, this fund or the right to recover it (for it is really a debt due by the fund to Master) was part of his estate. It is true that there were many limitations to his interest and that his claim was liable to be defeated, but none of these contingencies occurred, and the fund was properly payable to him or to his representatives at the time of his death. "

15. After quoting the above passage, the learned judge held (at page 50):

" We think therefore that there was here a valid attachment and a valid sale, and that the defendants are liable to the plaintiffs for this sum of Rs. 81-14-3, and the plaintiffs are entitled to a decree for that amount. There is nothing in the paper book to show that interest on this was claimed. We make therefore no order as to interest. The revision application is allowed with costs accordingly, "

16. The above said facts and the decision rendered on these facts have no relevance at all to the present case.

17. Another decision relied on by Shri Nair is the one by a learned single judge of the Madras High Court in C. D. Sankara Narayanan v. Egmore Benefit Society (Third Branch) Ltd. AIR 1964 Mad 256. That decision has no application to the facts of the present case. In that decision, what was held was (headnote):

"Where a property not belonging to a testator is included in a will, the executor or executrix, as the case may be, cannot be deemed to have been constituted a trustee as regards his or her obligations towards the beneficiary in respect of that property as, in law, nothing authorises a testator to bequeath a property which he could not have alienated inter vivos and consequently the executrix was not precluded from setting up a title to the property in question as the property in fact belonged to her and she had dealt with it as an owner even during the lifetime of the testator. In the circumstance no trust at all is created and the question of estoppel does not arise. "

18. On behalf of the assessee, the decision of the Division Bench of this court reported" in Commissioner of Income Tax Vs. V.S. Kumaraswamy Reddiar Trust,

was cited. In that case, on almost identical facts, this court held that the trust was valid ; and the assessment was to be u/s 161 of the Income Tax Act.

19. The only other alleged infirmity pointed out by the Income Tax Officer is that the immovable properties belonging to the firms were transferred to the trust and that was not made under a registered document. It is true that in the trust deed there is a recital that the immovable properties would be transferred ; that possession thereof had been given to the trustees ; and that the necessary document would be executed as and when required. The document, however, has not been executed. Inasmuch as the corpus of the trust fund was only a sum of Rs. 1,40,000, the fact that some immovable properties also were sought to be transferred, but that had not taken place actually, could not in any way vitiate the trust. Moreover, no trust is seen to have been declared of the immovable properties, the declaration having been confined to Rs. 1,40,000, which had become the property of the founder before the trust deed was made out and got registered on August 4, 1971.

20. For the foregoing reasons, we answer the question referred to us in all the references in ITRs Nos. 84 to 86 of 1979 in the affirmative, that is, in favour of the assessee and against the Revenue.

21. In view of our decision in ITRs Nos. 84 to 86 of 1979, we answer the question in ITR No. 125 of 1979 also in the affirmative, that is, in favour of the assessee and against the Revenue.

22. In ITRs Nos. 71 to 77 of 1981, the question dealt with in the above ITRs Nos. 84 to 86 and 125 of 1979, has been split up into various questions and over and above these, some other minor questions also have been included. As per orders of this court in O. P. No. 3125 of 1979E, the following questions of law were referred to this court u/s 256(2) for the assessment year 1972-73 ;

"(1) Whether, on the facts and in the circumstances of the case, the Tribunal is right in law in holding that it was Ramachandru Ammal and not the 28 beneficiaries who is the real author of the trust ?

(2) Whether, on the facts and in the circumstances of the case, even if the trust is valid (without conceding), what is the status in which the trustees should be assessed ?

(3) Whether, on the facts and in the circumstances of the case and particularly in view of the finding of the Tribunal that the cheque for Rs. 1.4 lakhs was never encashed, the Tribunal is right in law and fact in finding that Ramachandru Ammal had become the owner of Rs. 1,40,000 and she could declare a trust thereon ?

(4) Whether, on the facts and in the circumstances of the case, and in view of the finding recorded by the Tribunal that "according to the deed these twenty-eight persons had agreed with the founder to deliver to her the business assets of the two firms.....", the Tribunal is right in law and fact in holding that minors"

properties have not been subjected to the trust ?

(5) Whether, on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal is right in law in holding that the claim for deduction of Rs. 10,333 on account of the liability towards gratuity is proper and allowable ? "

23. As per the order in O.P. Nos. 3146 of 1979G and 3223 of 1979A dated October 23, 1980, and O.P. No. 4251 of 1979F dated December 1, 1980, the following questions were referred to this court u/s 256(2) for the assessment years 1973-74, 1974-75 and 1975-76 :

(1) Whether, on the facts and in the circumstances of the case, the Tribunal is right in law in holding that it was Ramachandru Ammal and not the 28 beneficiaries who is the real author of the trust ?

(2) Whether, on the facts and in the circumstances of the case, even if the trust is valid (without conceding), what is the status in which the trustees should be assessed ?

(3) Whether, on the facts and in the circumstances of the case and particularly in view of the finding of the Tribunal that the cheque for Rs. 1"4 lakhs was never encashed, the Tribunal is right in law and fact in finding that Ramachandru Ammal had become the owner of Rs. 1,40,000 and she could declare a trust thereon ?

(4) Whether, on the facts and in the circumstances of the case, and in view of the finding recorded by the Tribunal that " according to the deed these twenty-eight persons had agreed with the founder to deliver to her the business assets of the two firms.....", the Tribunal is right in law and fact in holding that minors" properties have not been subjected to the trust ?

24. In O. P. Nos. 397 of 1979L and 394 of 1979L dated October 23, 1980, the following questions of law were referred to this court u/s 256(2) for the respective assessment years 1972-73, 1973-74 and 1974-75 :

25. Assessment year 1972-73 :

" Whether, on the facts and in the circumstances of the case, the bad debt of Rs. 9,539 was an allowable deduction in the assessment of the assessee for the assessment year 1972-73 either u/s 36(2) or Section 37 of the Income Tax Act, 1961 ? "

26. Assessment year 1973-74:

" Whether, on the facts and in the circumstances of the case, the bad debt of Rs. 19,825 was an allowable deduction in the assessment of the assessee for the assessment year 1973-74 either u/s 36(2) or Section 37 of the Income Tax Act, 1961 ? "

27. Assessment year 1974-75 :

" Whether, on the facts and in the circumstances of the case, the bad debt of Rs. 12,600 was an allowable deduction in the assessment of the assessee for the assessment year 1974-75 either u/s 36(2) or Section 37(2) of the Income Tax Act, 1961 ? "

28. In the light of the conclusions reached by us in ITRs Nos. 84 to 86 of 1979, we answer questions Nos. 1, 3, 4 and 5 referred to this court pursuant to the direction in O.P. No. 3125 of 1979E and questions Nos. 1, 3 and 4 referred to this court pursuant to the direction in O.P. Nos. 3146 of 1979G, 3223 of 1979A and 4251 of 1979F in the affirmative, that is, in favour of the assessee and against the Revenue. On question No. 2 in the reference pursuant to the direction in O.P. No. 3125 of 1979E and question No. 2 pursuant to the direction in O.P. Nos. 3146 of 1979G, 3223 of 1979A and 4251 of 1979F, we hold that the trustees are liable to be assessed as representative assesseees.

29. The questions referred to this court pursuant to the direction in O.P. Nos. 397 of 1979L and 394 of 1979L relate to the assessment years 1972-73, 1973-74 and 1974-75 and concerning the deductions on account of the alleged bad debts. These questions are answered in the negative, that is, in favour of the Revenue and against the assessee, in view of the findings on facts by the Tribunal, agreeing with the Income Tax Officer, that the conditions u/s 36(2) or 37 of the Income Tax Act have not been satisfied. The parties would bear their respective costs.

30. A copy of this judgment under the seal of the High Court and the signature of the Registrar will be, forwarded to the Income Tax Appellate Tribunal, Cochin Bench.