

(1958) 09 CAL CK 0016
In the Calcutta High Court
Case No : Income-tax Reference No. 9 of 1953

PROVAT KUMAR MITTER

APPELLANT

Vs

COMMISSIONER OF Income Tax, WEST BENGAL.

RESPONDENT

Date of Decision : 18-09-1958

Acts Referred:

Contract Act, 1872 — Section 25

Income Tax Act, 1961 — Section 16(1)(c), 16(3)

Citation : AIR 1958 Cal 434 : (1959) 37 ITR 91

Hon'ble Judges : Chakravartti, C.J.;Guha, J

Bench : Full Bench

Judgement

CHAKRAVARTTI, C.J. - Three questions have been referred in this case and they arise out of the following facts. The assessee, Sri Provat Kumar Mitter, is the registered holder of 500 ordinary shares of the Calcutta Agency Ltd. By a written instrument, dated the 19th January, 1953, he settled on his wife, Sm. Ena Mitter, the right, title and interest to all dividends and sums of money which might be declared or might become due on account or in respect of those shares for the term of her natural life. The material portion of the instrument is short. After reciting that the settlor was desirous of making a provision for his wife, the instrument proceeds as follows :

"This deed witnesseth that for a effecting the said desire and in consideration of the natural love and affection of the settlor for the beneficiary, the settlor, as the beneficial owner, assigns unto the beneficiary the right, title and interest to every dividend and sum of money which may be declared or become due and payable on account of or in respect of the said shares (not being the price or value thereof) and further hereby covenants with the beneficiary to hand over and/or endorse over to the beneficiary any dividend warrant or any other document of title to such dividend or sum of money as aforesaid and to instruct the said company to pay any such dividend or such sum of money to the beneficiary to hold the same unto the beneficiary absolutely during the term of her natural life."

The instrument states further that during the term of the natural life of the wife, the husband shall have no right, title or interest in the dividends of the monies or any benefit therefrom.

It will be noticed that the shares themselves remained the property of the settlor and it was only the income which was sought to be settled or assigned.

During the accounting year ended on the 31st March, 1953, the dividend declared on the shares was Rs. 12,000. In assessing the settlor for the assessment year 1953-54, the Income Tax Officer included the dividend in his income under, as he said, the provisions of sections 16(1) (c) and 16(3) of the Indian Income Tax Act. The settlors contention was that since the settlement was for the lifetime of the beneficiary the third proviso to section 16(1) (c) would apply and the dividend which had come to belong to the beneficiary could not be deemed to be his income. He, accordingly, appealed to the Appellate Assistant Commissioner. Before that authority, the Income Tax Officer put forward a somewhat extra-ordinary ground to which he adhered even before the Appellate Tribunal in the subsequent proceedings before that body. He contended for, that proviso was to be ignored altogether, because it virtually superseded the main clause of section 16(1) (c). A further contention advanced by him was that since the shares were continuing to stand in the name of the settlor and the dividends had been declared in his name, the transfer of the dividends to the beneficiary was only an application of the dividend income, and therefore, the settlor could not claim exemption from being taxed on it as a part of his own income. The Appellate Assistant Commissioner gave effect to both of those contentions.

In further appeal before the Income Tax Appellate Tribunal, the settlor again relied on the third proviso to section 16(1) (c) of the Act and the Departmental Representative took his old two points as also a further point. The further point was that the deed by which the dividends had been transferred was altogether invalid inasmuch as it was an unregistered instrument and, therefore, no valid transfer of the dividend income had been effected by it.

The Tribunal had no difficulty in rejecting the Departments contention as to the third proviso to section 16(1) (c). They did not see how the proviso could be ignored or why it was said that it was altogether repugnant to the main clause of the section. For some reason or other, which does not appear from the appellate order, the Tribunal expressed no opinion as to the contention that the transfer of the dividend income was not a diversion of it before it had become the income of the settlor, but was merely its application by him after he had received it. The Tribunal, however, gave effect to the third contention of the Department. At the initial stages of the argument before them it was stated that the deed was, in fact, registered, but they called for the deed and found that it was an unregistered instrument. Since it was an unregistered instrument, the Tribunal thought that section 25 of the Contract Act applied and the agreement being an agreement made for natural love and affection and for no other consideration between parties standing in near relation to each other, they held that it was

altogether void in the absence of registration of the deed. Both the settlor and the Commissioner, thereafter, asked the Tribunal to refer to this court the questions which had respectively been decided adversely to them. The Tribunal acceded to the request and they referred two questions at the instance of the Commissioner and one at the instance of the assessee. The questions referred are as follows :

"(1) Whether the deed dated January 19, 1953, assigning the dividends to accrue merely on account of natural love and affection is void as it is not register ?

(2) Whether the third proviso to section 16(1) (c) is repugnant to the main clause of section 16(1) (c) and the general scheme of the Act, and should not be given effect t ?

(3) Whether, on the facts and in the circumstances of the case, the payment of dividend income to the assessee's wife Mrs. Ena Mitter, under the covenant in the deed of assignment dated January 19, 1953, was merely a case of application of the assessee's income ?"

I shall take the questions in the order in which they have been referred.

In holding that the deed was void because it was not registered, the Tribunal proceeded on the footing that section 25 of the Contract Act applied. In this, in my view, they were clearly wrong, because the deed is a unilateral document and does not contain any contract at all. In all material respects, it is similar to the deed on which the Judicial Committee pronounced in the case of *Gopal Saran Narain Singh v. Sita Devi*. The only person who executed the deed was Sri Provat Kumar Mitter. His wife was not a party to it all. The nature of the disposition again is the nature of a gift, although the settlor purports to bind himself to do certain things. Those, however, are in the nature of voluntary covenants of a unilateral character and cannot convert the transaction into a contract. It was said that there was a contract because the covenants were promises which, on being accepted, became agreements, but even then the acceptance is not to be found in the deed and what the deed evidences are only the promises. Whether the deed was otherwise valid or not or whether the transfer sought to be made by it was effective or ineffective, it cannot, in my opinion, be said that it is bad for want of registration.

Mr. Meyear contended that if the deed was held not to be bad for want of registration on the ground that the disposition it incorporated was a gift then the deed would be altogether void for another reason. It purported to assign to the assessee's wife the right, title and interest to every dividend and sum of money which might be declared or might become due on account or in respect of the shares and, therefore, it purported to make a gift of non-existing or future property which could not legally be done. He called attention to the definition of gift, as contained in section 122 of the Transfer of Property Act, where it is clearly stated that gift is transfer of existing property, movable or immovable. We

were also referred to section 24 of the same Act which lays down that a gift, comprising both existing and future property, is void as to the latter. It seems to me, however, that the definition of gift may not completely dispose of the matter, because it has further to be considered whether what was sought to be transferred was an actionable claim. "Actionable claim", as defined in section 3 of the Transfer of Property Act, includes a claim to any beneficial interest in movable property not in the possession, either actual or constructive of the claimant, whether such beneficial interest be existent, accruing, conditional or contingent. u/s 130(1) of the Act, the transfer of an actionable claim, whether with or without consideration, may be effected only by the execution of an instrument in writing, but no registration is required. Whether the benefit transferred is an actionable claim or not we need not consider, because in my view we must limit ourselves to the question asked. The question asked is whether the deed is void for want of registration. In answering that question, it is, in my view, not open to us or to the parties to digress into any other question as to whether the deed is otherwise void and of no legal effect. It will be sufficient to say that, whether regarded as a deed of gift or regarded as a deed of transfer with respect to an actionable claim, the deed in the present case did not require registration to make it valid, quite apart from the question whether it was otherwise legally inoperative and void. The answer to the first question must, therefore, be in the assessee's favour.

Mr. Meyer did not seek to support the Department's contention reflected in the second question. It may be conceded that the third proviso to section 16(1) (c) read in the right of the main clause, is somewhat odd, because after saying in an absolute form that all income arising to any person by virtue of a settlement or disposition, whether revocable or not, shall be deemed to be the income of the settlor or dispenser, the section goes on to say by the third proviso that income arising by virtue of a settlement or a disposition which is irrevocable for a certain period will not come under the ambit of the section. Yet, the third proviso does not rob the main clause of the entirety of its contents. Taken along with the third proviso, the main clause means that income arising to any person by virtue of a settlement or disposition which is revocable within six years will have the effect laid down. If the main clause is saved at least to this extent after full effect has been given to the third proviso, there can be no reason for holding that the proviso is altogether repugnant to the main clause and, therefore, since the two cannot stand together, the proviso must fail. The answer to the second question also must, therefore, be against the department.

To proceed now to the third question, it is unfortunate that it should have received no attention from the Tribunal in their appellate order, because, to my mind, it is this question which raises the crucial point in the case. The Department's case is that the transfer in the present case was merely an application of the assessee's income to the purpose mentioned in the deed, whereas the assessee contends that if the third proviso to section 16(1) (c) applies, as in his submission it does, then the income cannot be deemed to be

his income by reason of the express direction of the statute to the contrary. In order to appreciate these rival contentions, it is necessary, to my mind, to see first what the scheme of section 16(1) (c) is and what it actually provides. It appears to me that section 16(1) (c) has not always been approached from the correct standpoint and the confusion which has, at times, arisen was caused, because an approach was made to the section from a wrong angle. It is first to be seen who is the person whom the section contemplates. Clearly, it is the person who has received some income and it is equally clear that what the section is doing is to lay down certain principles which should be applied in computing the total income received by him. To come at once to the terms of the section, it begins by speaking of "all income arising to any person." The person contemplated by these words is the person to whom some income has arisen and who has received it. When one remembers that the section is concerned with laying down the principles which will have to be applied in computing the total income of a particular person to whom some income has arisen, one will at once understand that what section 16(1) (c) is concerned with is the exclusion of the income from the total income of that person at least as much as the inclusion of it in the total income of the person who has made the settlement or the disposition or the transfer. The section provides that certain income which has arisen to a certain person by virtue of a settlement or disposition shall not be included in his total income in certain circumstances, but shall be included in the income of the settlor or the dispenser. It is quite clear that but for this provision, the income would have to be included in the total income of the person to whom it has arisen. It is equally clear that under the general law the income concerned is not the income of the settlor or dispenser in the case contemplated, because had it been so, it would be entirely unnecessary and entirely inappropriate to provide that in the circumstances stated in the section, the income shall be "deemed to be" his income. Nothing which is somebody's own income requires to be deemed to be so. It is his income already in truth and in law. Section 16(1) (c), therefore, clearly contemplates a case where some income has been assigned by means of a settlement or disposition in such a way that it has ceased to be the income of the settlor or dispenser and had become the income of the beneficiary or the transferee, so that, but for the provisions of this section, it would be rightly assessable in the hands of the latter. To my mind, a settlement or disposition or transfer of income which is of such a character that the income remains the income of the settlor or dispenser and there is only an obligation cast upon him to pay it to the beneficiary is not and cannot be within the contemplation of section 16(1) (c) at all. The reason is clear. In such a case the income is, under the general law, the income of the settlor or dispenser having remained his despite the settlement or disposition and, therefore, it need not or could not be "deemed" to be his income. It is not very easy to conceive a form of settlement or disposition which, in the absence of the transfer of the assets, will make the income, the moment it arises, the income of the beneficiary. But this much is clear that unless the settlement or disposition is of that kind, section 16(1) (c) will not apply at all. One may perhaps conceive of a

case where a particular annuity or income from a particular property is payable by A to B and if B wishes to settle that income on C so as to make it his income, a tripartite agreement between A, B and C may be concluded whereby A will be required to pay the annuity or income to C as soon as it becomes payable and C will be entitled to claim it directly from A in his own right and B will have no right whatsoever to claim it from A in any circumstances. If, on the other hand, the income has to pass through B going to C, it remains, in law, the income of B and therefore, I cannot see what room there can be of section 16(1) (c) to apply in such a case. To put it briefly, section 16(1) (c), to my mind, can be given an intelligible meaning only if it is read as contemplating a settlement or disposition under which the incomes transferred become income of the beneficiary without being required to be paid by the settlor or dispenser under an obligation imposed by him on himself. If the income first arises to the settlor or dispenser and is then to be paid by him to the beneficiary under a covenant which he has created for himself, the case is not within section 16(1) (c) at all, because in such a case there can be no sense in saying that the income shall be deemed in certain circumstances to be the income of the settlor or dispenser or transferor, it being in fact his.

Turning now to the third proviso, it has to be seen what it provides. It is to be noticed in the first instance that while the main clause contemplates a settlement or a disposition of income or a transfer of assets, the third proviso does not mention transfer of assets at all. It is limited to settlement or disposition. Be that as it may, it contemplates a settlement or disposition which is not revocable for a period exceeding six years or during the lifetime of the beneficiary. I am leaving out the other requirements of the proviso, because they are not material in the present case. If those other conditions are satisfied and the settlement or disposition is one which is irrevocable for the period mentioned in the proviso, what is the consequence which follows ? The consequence, according to the proviso itself, is that "this clause," namely, section 16(1) (c), shall not apply to the income arising from the settlement or disposition. If section 16(1) (c) does not apply to the income, what is the consequence ? The consequence will be that the special rule laid down in the section shall be excluded. In other words, the fiction introduced by section 16(1) (c), whereby the income which was not really the income of the settler or disposer would nevertheless be deemed to be his income, will not be applicable if the third proviso applied and, therefore, the ordinary law under which the income is to be included in the total income of the person whose income it is, shall have effect. I have already pointed out that the question of deeming the settlement or disposition to be the income of the settler or disposer can arise only if he has transferred the income in such a manner that it has ceased to be his income altogether and has not merely to be applied by him after he has received it. It follows that if section 16(1) (c), together with the third proviso applied to the present case and the fiction introduced by the main clause of the section was removed, the consequence would be that the matter would be thrown to the

general law and the income would have to be assessed in the hands of the beneficiary whose income it, in law, was. If, on the other hand, the disposition or settlement is such that the income has not been transferred by it to the extent of being made the beneficiary's income as soon as it accrues, the fiction introduced by the main clause of section 16(1) (c) will, to my mind, not be required to be removed by the third proviso because the main clause would exclude itself by its own terms and the case will be altogether outside section 16(1) (c). In such event, the income will be assessable in the hands of the settler because it has remained his income in spite of the obligation under taken to pay it over to the wife.

Turning now to the settlement in the present case, I have already said that for the purposes of the third question, it is not open to us or to any party to consider whether any valid transfer was effected by it. Cases seem to lay down that a claim to a dividend which has been declared is a chose in action under the English law and would probably be an actionable claim under the Indian law. (See *Ann Dalton v. Midland Counties Railway Company* and *Widgery v. Tepper*.) Still, however, claims to dividends which may fall due in future may not be chosen in action, but we need not tarry over that question and shall proceed on the footing that the deed is a valid deed. Even so, what does it provide ? It assigns to the wife the right, title and interest to every dividend and sum of money which may be declared or become due or payable on account of the shares. How is this assignment to take effect ? It is important to remember that the income transferred is dividend income and the company paying the dividend will and can pay it only to the registered shareholder. This seems to have been recognised, because the deed proceeds to say that the settler covenants with the beneficiary to hand over and/or endorse over to the beneficiary any dividend warrant or any other document of title to such dividend or such sum of money as aforesaid and to instruct the company to pay such dividend or sum of money to the beneficiary. It is thus quite clear that what is contemplated is that dividend warrants will be issued in the name of the settler, as they were bound to be, because he continued to be the owner of the shares, and after the dividend warrants had been issued in his name and so after the dividend income had accrued to him he would endorse the warrants, that is to say, would transfer the money to the beneficiary or instruct the company to pay the money to her. It is clear that if the wife had become the owner of the money independently of the husband, there could be no question of his instructing the company to pay the money over to her, because she could claim from the company in her own right. But it is obvious that the income being dividend income will remain to accrue to the settler in the first instance and the deed quite clearly contemplates that the income will be transferred to the beneficiary by the settler after the settler has received it and this will be done each time a dividend is declared and each a dividend warrant is issued. If that is the effect of the deed, and I can view it in no other light, it seems to me that section 16(1) (c) of the Income Tax Act cannot apply at all to the income sought to be transferred by it, because the

income remained the income of the settler or rather remained to accrue to him first in spite of the assignment. If so, the income is clearly assessable in his hands.

As I understand the first part of the section 16(1) (c) its scope and effect is as follows : That part of the section aims at frustrating the device of reducing ones tax liability by transferring the income derived from certain assets to a third party while retaining the ownership of the assets themselves. Obviously, such a section can be needed only for cases where, but for it, the transferred income would be assessable in the hands of the transferor and would not be assessable in the hands of the transferee and such cases, again, can only be cases where the income is effectively transferred *quo income*, so that it ceases to be the income of the transferor and accrues directly to the transferee when it arises. If despite the purported transfer the income remains initially the income of the transferor and it has only to be paid over to the transferee under a binding obligation voluntarily undertaken, it will continue to be assessable in the hands of the transferor under the general charging sections and, therefore, no special provision can be needed to bring it to tax in his hands. In such a case, there is no device on the part of the transferor to avoid tax on the income or the device, even if employed, has not succeeded. Section 16(1) (c), in my view, is not concerned with such a case and its terms show that it is not so concerned. Its concern is with the other type of case where the transfer is such that, by virtue of it, the income is no longer income of the transferor even in the first instance and cannot be taxed in his hands under the general charging sections and so the consequence is that being assessable only in the hands of the transferee, it may not suffer tax at all, if the transferee's total income is found to be below the taxable limit or may have to be taxed at a lower rate. A provision like section 16(1) (c) is needed to avert such a consequence, if it is desired to avert it. In my opinion, the first part of section 16(1) (c) was enacted because the Legislature was of the view that complete and effective transfers of income, as such, without a transfer to the transferee yielding the same, by means of dispositions revocable within six years, were only devices on the part of the transferors to avoid tax on the income and being of that view, it thought that a provision for striking out such devices ought to be made so that one could not avoid tax on such income by merely putting it away in that form in the name of some other person. The Legislature had in contemplation only cases where such a provision was needed, that is to say, cases where by virtue of the nature of the transfer, the income had ceased altogether to be the income of the transferor so that, without such a provision, it could not be brought to tax in his hands.

To turn now to the terms of the section, it begins by speaking of "income arising to any person by virtue of a settlement or disposition" which, read in the light of the third proviso, means a settlement or disposition revocable within six years. Income may arise to a person, by virtue of a settlement or disposition thereof made in his favour, in two ways, according to the terms of the settlement or disposition. It may arise to him directly as his income, yielded to him by the

assets from which the income is derived, without the intervention of the settler or disposer with whom the ownership of the assets remains. Or it may arise to him in the form of having to be paid over to him by the settler or disposer under a binding covenant contained as him income. Section 16(1) (c) is not concerned with the second case but is concerned only with the first. That such is the scope of the section appears, as I have already explained, clearly from the provision that the income which the section has in view "shall be deemed to be the income of the settler or disposer." In the second case mentioned above, the income is in fact the income of the settler or disposer in the first instance and, therefore, it does not require to be made his provision like the section necessary to bring the income to tax in the hands of the settler or disposer. The section applied to the first case and contemplates that case alone, for, there, the income, having ceased to be the income of the settler or disposer under the general charging sections and therefore a special provision is needed to make it assessable in his hands. Section 16(1) (c) supplies such a provision by enacting that in such a case the income shall be deemed to be the income of the settler or disposer.

The true scope of the first part of the section 16(1) (c) being, in my view, what I have explained above, I cannot, with respect, follow the whole of the reasoning in Rangachari v. Commissioner of Income Tax, though with much that was said in that case I find myself in agreement. The learned Judges who decided that case say that the only effect of the third proviso to section 16(1) (c), where it is attracted, is that "this clause", i.e., the main clause of section 16(1) (c), containing a special rule, shall not apply. That, if I may say so with respect, is entirely correct. But the learned Judges go on to say that where the application of the main clause of section 16(1) (c) is excluded by the operations of the third proviso, it does not necessarily follow that the income will not be assessable in the hands of the settler or disposer and that it will be assessable in the hands of the beneficiary or of the settler or disposer according as there has been a diversion of the income or a mere application of it by the settlement or disposition, for which the facts of each will have to be considered. I am unable to agree with this conclusion and the reasoning on which it is based. In my view, the question whether the third proviso will operate in a particular case or not can arise only after the main clause of section 16(1) (c) has initially and prime facie been attracted, for, the function of the proviso is to take out of the main clause certain cases which, so far as the language of the clause goes, would be within terms. The main clause of section 16(1) (c) is intended to apply and can apply, as I have tried to show, only in cases whereby virtue of the settlement or disposition, the income has ceased to be income of the settler or disposer. It follows that there can be room for the application of the third proviso only in such cases and, therefore, where the requirements of the proviso are satisfied and it applies and where, in consequence, the operation of the main clause of section 16(1) (c) and the special rule contained therein is excluded, the result will be that the general law will apply and the beneficiary and being no longer the income of the settler or disposer, will be assessable in the hands of the former.

There can no longer be any debatable question in such a case as to whether there has been a diversion of the income by the settlement or disposition or there is only a provision for its application, because unless the first were the case, section 16(1) (c) would not have been attracted even initially and consequently, the third proviso could not have had any room for its application. By the fact that a case comes initially and prime facie under the main clause of section 16(1) (c) and is then taken out of the clause by the operation of the third proviso, it stands determined that the case is one of the settlement or disposition of the income in such terms that they make it case to be the income of the settler or disposer and make it accrue directly to the beneficiary from the assets and his income. If that question already stands determined, there can be no need of or scope for any further enquiry.

The practical effect of section 16(1) (c), in so far it deals with settlement or dispositions of income is, in my opinion, as follows : If the settlement or disposition merely provides for an application of the income under a binding agreement contained therein after the income has accrued to the settler or disposer, section 16(1) (c) will not apply at all. In such case, the income will be assessed in the hands of the settler or disposer under the general charging provisions, because it is still his income in the first instance and I presume the beneficiary will also be assessable on what he receives, because his receipts under the settlement or disposition will be income receipts. Where, however, the settlement or disposition makes the income a direct income of the beneficiary, that is to say, it becomes his income without passing through the settler or disposer, section 16(1) (c) will be attracted and will have effect, unless the third proviso applies. If it has effect, the income, being deemed to be the income of the settler or dispenser, will be assessable in his hands, but the beneficiary, although he receives the income, will not be assessable by reason of the express direction of the section, presumably for the reason that the Legislature regards the beneficiary in such cases as merely a name-lender. If, however, the third proviso applies, section 16(1) (c) will be excluded and it will not have effect and the income will then be assessable in the hands of the beneficiary under the general charging sections, because under the settlement or disposition it is his income and not the income of the settler or disposer.

Applying these principles to the present case, the conclusion must be that there being only a voluntary covenant entered into by the settler to pay over the dividends received by him to the wife or to instruct the company to pay them to her and the income not having been made the wife's income from the beginning, what the settlement provides for is only an application of the income and, therefore, the income is assessable in the hands of the settler, irrespective of whether the wife is also assessable on her receipts. The case is outside the main clause of section 16(1) (c) and, therefore, the third proviso to the section is also not relevant.

The assessee exhibited a certificate from the company, showing that they had

paid the dividend for a certain year to the wife. In what form that was paid has not been explained, but in view of the terms of the deed it could have been paid over only on an endorsement of the dividend warrant by the settler. The third question must, therefore, be answered in the Departments favour.

In the result, the three questions are answered as follows :

Question No. 1 : "No."

Question No. 2 : "No."

Question No. 3 : "Yes."

In view of the fact that many of the contentions of the Department before the Tribunal were not tenable, we would make no order as to costs.

GUHA, J. - I agree.

Reference answered accordingly.