

BOMBAY HIGH COURT

Ramji Keshavji

Vs

Commissioner of Income-Tax

(Kania, J.)

07.09.1944

JUDGMENT

Kania, J.

1. This is a reference made by the Income-tax Appellate Tribunal under Section 66 (1) of the Indian Income-tax Act. The relevant facts are these. The assessee had a son Shivji by his first wife, a son Vassanji by his second wife, his third wife Kamalabai and three sons and three daughters by the said wife. Disputes arose in the family about the rights of the adult sons, and High Court Suit No. 1836 was filed by Vassanji against the assessee and the other members of the family claiming that all the estate in the hands of the assessee was joint family property and the parties were entitled to their rights on that footing. After the litigation had gone on for some time, a consent decree was taken on December 23, 1938. Under that consent decree it was inter alia declared that all the properties in the possession of the assessee were his self-acquired properties. It was further declared that in respect of the Ulster Road House in Bombay a trust deed should be executed in accordance with the draft which was annexed as schedule "C" to the consent decree. By the consent decree it was further provided that defendant No. 6 (i.e., the wife of the assessee) should be paid the net income of the said Ulster Road property from and after January 1, 1939. In pursuance of the said consent decree the assessee, who was defendant No. 1 in that litigation, executed a trust deed in respect of Ulster Road property. The relevant portions of the deed can be briefly summarized as follows. By the trust deed the assessee transferred the Ulster Road property to the trustees. In doing that he used the following words :-

"And all the estate right title interest property claim and demand whatsoever of him the settlor of in and to the said premises and every part thereof except and reserving unto the settlor the right to occupy during his lifetime the portion of the said premises and also the garage on the said premises occupied by him..."

In respect of the income it was provided that the trustees should collect the rents and after paying the necessary charges of collection and the premia for insurance during the lifetime of Kamalabai, pay the balance to Kamalabai for the during her lifetime and down to her death,

subject to the obligations during the lifetime of the settlor to maintain thereout during their respective minorities her children by the settlor so long as they reside with her and so run the household at Nasik in the manner and to the extent as the said Kamalabai may deem fit. Under clause 4 it was provided that from and after the death of the said Kamalabai the said trustees shall pay the balance (hereinafter called "the said income") of the said rents, interest, dividends and other income of the said trust premises after meeting the costs and expenses referred to above to the settlor for and during his lifetime if he shall survive her. Under clauses 5 it was provided as follows :-

"Provided always that the said trustees shall from time to time at the request in writing of the said Kamalabai and after her death at the request in writing of the settlor if he shall survive her realise from the said trust premises and pay to her or to the settlor (as the case may be) such sum or sums of money as she or he may require them to realise for the purpose of enabling her or him to meet and defray the expenses of any auspicious or inauspicious occasion in respect of all or any of the settlors children by the said Bai Kamalabai not herein otherwise expressly provided for or the expenses of any protracted illness of the said Bai Kamalabai or the settlor or any of their children or of any other member of the settlors family or the expenses relating to the preservation or improvement of health by means of a change of air or otherwise of the said Bai Kamalabai or of the settlor or any of their children or any such member as aforesaid but so nevertheless that the aggregate of the surplus so realised and paid as aforesaid to the said Bai Kamalabai or to the settlor shall not in any six consecutive months exceed the sum of Rupees two thousand nor exceed in any event whatever the total sum of Rupees ten thousand."

In connection with the assessment for 1941-42, while calculating the assessee's income for the year ending on March 31, 1941, the department sought to include the income of the Ulster Road property in his total income. On these facts it was contended on behalf of the assessee that the income of the Ulster Road property should not be included in his income. He sought the protection of proviso 3 to Section 16 (1) (c) of the Indian Income-tax Act. On behalf of the Commissioner it is contended that proviso 3 is inapplicable and the case is covered by proviso 1 to Section 16 (1) (c). The question, therefore, is what is the exact effect of Section 16 (1) (c) in respect of the trust deed in question? It is not disputed that there is no power of revocation reserved to the settlor under this trust deed.

Section 16 deals with the question of what should be included in computing the total income of an assessee. Section 16 (1) (c) deals with transfers effected by the settlor. The first part of Section 16 (1) (c) is not applicable. The second part is in these terms :

"all income arising to any person by virtue of a revocable transfer of assets shall be

deemed to be income of the transferor."

Therefore the substantive portion of Section 16 (1) (c) provides that the income derived from a revocable transfer of assets is deemed to be the income of the transferor. That is followed by the 1st proviso which enacts that for the purposes of that clause a settlement shall be deemed to be revocable if it contains any provision for the retransfer directly or indirectly of the income or assets to the settlor or a right to reassume power directly or indirectly over the income or assets. Relying on this proviso, it is argued on behalf of the Commissioner that because in this settlement there are provisions which give the settlor direct or indirect benefit in the income or assets, it is a revocable transfer within the meaning of Section 16 (1) (c). Against that it is contended on behalf of the assessee that there are on such provisions in this settlement which amount to a transfer of income or assets to the settlor. I shall consider next each of the grounds urged on behalf of the Commissioner in this connection. The first is that the settlor has retained the use of a portion of the property for himself and the use of the garage. Against that it is sufficient to observe that this is not a retransfer or resumption of the power, contemplated by the proviso. The words "retransfer or reassume" necessarily involve a second transaction of a later time. The only question which can be debated in respect of this clause is whether at the moment of settlement his whole property less this right of residence was transferred, or the whole property was transferred and the settlor retained this right for himself. In any event there is no question of retransfer because after the settlement there is no further step taken to alter the position of the parties in respect of this right of occupancy. The second ground urged is that under clause 3 of the deed of trust the settlor has provided for the maintenance of his wife and children and, therefore, he gets the benefit, directly or indirectly, of the income or assets. I may point out that this again is not a retransfer or reassumption of the power over the income. In my opinion, the argument that by this clause the settlor has retained for himself a benefit, because his obligation to maintain his wife and children to the extent of the income of this property is fulfilled, is unsound. To carry to its logical conclusion, the contention of the commissioner must be that, even after a man's wife and children have established in a Court of law a right of separate residence and maintenance, and under an order of the Court he is ordered to settle separate property for the maintenance, and residence of his wife and children, and although in those circumstances the settlor has got no control over the income or the disposal because he is by this arrangement absolved from the legal obligation of maintaining his wife and children, he derives benefit from that and is thus directly or indirectly retransferring the income to himself. In my opinion, this contention is quite unsound. He may be free from a legal obligation, but he is retransferring nothing to himself. I do not think that the Indian Income-tax Act ever contemplated that the income which is so settled and which has so gone completely out of the control of the settlor, is still to be computed in the total income of the assessee. Under clause 4 of

the deed of trust the income during the lifetime of the wife is settled on her. It is provided that after her death, if the settlor is alive, the same shall be paid to him for and during his lifetime. On behalf of the Commissioner it was contended that this amounted to a retransfer directly or indirectly of the income of the property or in any event a re-assumption of the power over the income or assets. The question is whether a contingent claim which may arise under a settlement, is covered by the proviso. Speaking for myself, I should very much hesitate before accepting this contention of the Commissioner which imports into the proviso words which are not there. The settlor does not get a retransfer of the income or assets or a re-assumption of the power over the income or assets by reason of the proviso alone. He gets it by reason of the proviso, coupled with a contingency, which may or may not happen. It is only on the occurrence of the contingencies that he acquires the right and it appears arguable that this proviso does not cover such a case. It is not necessary to enlarge on this aspect of the construction of clause 4 of the deed of trust, because in our opinion this reference can be decided on the construction of proviso 3 to Section 16 (1) (c). On behalf of the Commissioner reliance was placed on the provisions found in clause 5 of the deed of trust, for the same contention. In my opinion, that contention has no substance, because all the powers reserved under clause 5 are for payment of the income or sale proceeds to Kamalabai and not to the settlor. It is true that under the provisions Kamalabai is given a right to apply to the trustees for payment for a change of air of the settlor, or if there is protracted illness of the settlor. It is still a right which is given to Kamalabai and the amount is to be paid to Kamalabai. It is the volition of Kamalabai alone which can bring into operation, first the application, and, secondly, if it is acceded to, the payment to her. In my opinion, under the circumstances the provisions of clause 5 do not amount to a retransfer of the assets or income or a re-assumption of the power directly or indirectly to the settlor. The relevant and material provision is contained in proviso 3 to Section 16 (1) (c). The question is whether proviso 3 applies only to the substantive provisions of Section 16 (1) (c), or is a proviso to that sub-section and also to proviso 1, which I have discussed above. On behalf of the Commissioner it is urged that proviso 3 governs only the substantive provisions of sub-section (c). According to that contention the law provides that if there is a revocable trust, provided firstly it is made not revocable for a period exceeding six years or not revocable during the lifetime of the person (meaning the person for whose benefit under the trust deed the income is settled) and secondly from which income the settlor derives no direct or indirect benefit, the income is not to be considered the income of the settlor. On behalf of the Commissioner it is urged that in the present case this is not a revocable transfer of assets on the face of the settlement itself, and therefore the case is not covered by the substantive provision of Section 16 (1) (c). This particular settlement is deemed a revocable settlement by reason of proviso 1 to that sub-section. It was, therefore, argued that on the true construction of proviso 3 it does not apply to such a settlement at all. In my opinion this contention is unsound. The scheme of Section 16 (1) (c) appears to be tins. The

first stage is that when there is a revocable transfer of assets, the income derived from such assets is still to be considered the income of the settlor. The law next specifies by proviso 1 what would be deemed a revocable transfer, in spite of the deed being apparently irrevocable. The relevant question for that proviso is this : Is this transfer revocable because it fulfills the conditions contained in the proviso ? The answer to that question can be only, it is revocable, or it is not. If the answer is in the negative, no further discussion can arise because, on the face of it, the deed is not revocable and, therefore, it does not come under Section 16 (1) (c). If, however, the answer to the question is in the affirmative, the deed although ostensibly irrevocable, is deemed to be revocable, and thus becomes a revocable transfer of assets, within the meaning of the substantive provision of Section 16 (1) (c). Having reached that stage, the law proceeds to consider further what is found in proviso 3. The scheme appears to be that although in fact, after reading the provisions of Section 16 (1) (c) with proviso 1, the transfer is revocable, the law of the settlor, provided the settlement is to revocable for a period exceeding six years or during the lifetime of the person for whom the income is settled, and, further, from which income the settlor derives no direct or indirect benefit. The questions which the Court has to ask under proviso 3 are these : This being a revocable transfer of assets, is it made not revocable for a period exceeding six years or during the lifetime of the person for whose benefit the income is settled ? In the present case the relevant questions is : Is it made not revocable during the lifetime of Kamalabai (in the present case the person) ? The answer to that is in the affirmative. The next question is : Whether in the income which is settled during the lifetime of Kamalabai the settlor has any direct or indirect benefit ? The grounds on which direct or indirect benefit is claimed as resulting to the settlor, have been mentioned and dealt with by me in discussing the effect of proviso 1. In my opinion, on reading this settlement, no direct or direct benefit in the income, accruing during the lifetime of Kamalabai, is retained by the settlor for himself. The answer to the second question is therefore in the negative. Under the circumstances it is therefore clear that proviso 3 applies, and the income payable to Kamalabai and settled for her benefit during her natural life is not income of the assessee under Section 16 (1) (c). The answer to the question submitted by the Income-tax Appellate Tribunal for the Courts opinion would, therefore, be in the negative.

The Commissioner to pay the costs of the reference.

Chagla, J. - I agree.

The deed of trust that we have in this reference is an irrevocable deed of trust inasmuch as the settlor has not reserved to himself any power of revocation under the deed. But one of the provisions of the trust deed is that on the death of Kamalabai, the wife of the settlor, and in the event of the settlor surviving his wife, the income is to be paid to him by the trustees. To that extent there is a provision for retransfer of the income to the settlor. It is true that the provision

for retransfer is contingent in its nature. But with respect to my learned brother, in my opinion, on a plain reading of the section, the words of the section are wide enough to cover even a provision for retransfer which is contingent in its nature. Proviso 1 to the section when it refers to any provision does not in any way qualify the nature or the character of the provision. If we find in the trust deed that there is a provision for retransfer, to my mind the proviso would apply whether the nature of the provision is that it postpones the retransfer on a contingency happening or it provides for the retransfer on a certain event happening. Therefore the question that we have got to determine is, as under the first proviso of sub-clause (c) of Section 16 (1) the deed of settlement must be deemed to be a revocable deed, whether the third proviso to that sub-clause takes the deed outside the operation of the sub-clause, and in order to determine that question, we have got to reconcile the substantive provisions of sub-clause (c) of Section 16, proviso 1 and proviso 3. Now in my opinion subclause (c) of section 16 refers to all revocable transfers - transfers which are revocable in fact - transfers in which there is a provision for revocation on the part of the settlor. The proviso 1 then extends the definition of a revocable transfer and it provides that where in a deed of transfer there is a provision for retransfer directly or indirectly of the income or assets to the settlor, or where such a deed in any way gives the settlor the right to reassume power directly or indirectly over the income or assets, such a deed must be deemed to be a revocable transfer. Whereas proviso 1 extends the definition of a revocable transfer, proviso 3 contains a limitation - a limitation of time which applies both to revocable transfers under the substantive provisions of sub-clause (c) and also to those which are deemed to be revocable transfers within the meaning of proviso 1. What proviso 3 lays down is that when you have a deed which is not revocable for a period exceeding six years or during the lifetime of the person who is the beneficiary and for whose benefit the property is settled, then such a deed does not come within the operation of sub-clause (c) of section 16 (1), provided the other conditions, with which I need not deal at present are also satisfied. Therefore if you take a deed which is revocable in fact which contains a power of revocation, then if under that deed the power of revocation is postponed for a period exceeding six years or beyond the lifetime of the person benefited, then proviso 3 applies. If you take a deed which is deemed to be revocable within the meaning of proviso 1, then if the provision for retransfer or the right to reassume power does not come into operation till after the period which exceeds six years or beyond the lifetime of the person benefited, then also proviso 3 applies. I do not think there is any warrant for the contention put forward by Mr. Setalvad that proviso 3 only applies to the substantive provisions of sub-clause (c) and does not apply to proviso 1. If that argument were to be accepted, it would result in this glaring inconsistency. If you have a deed which contains a provision for revocation which can only come into effect after a period of six years, other conditions being satisfied, then such a deed would fall under proviso 3 and would be saved from the operation of sub-section (c) although after six years the settlor could revoke the trust and would have complete power of

disposal over the income and the corpus of the trust estate. But if you have a trust deed which contains a provision for retransfer to the settlor after a period of six years, that deed would not fall under proviso 3 and would come within the ambit of sub-clause (c) of Section 16 (1). I do not think that it would be right or proper to give a construction to this sub-clause and to the two provisos which would lead to such glaring results. In my opinion, agreeing with my learned brother, the only way to reconcile the substantive provisions of sub-clause (c), proviso 1 and proviso 3, is to hold that proviso 3 contains a limitation which applies as much to the substantive provisions of sub-clause (c) as to proviso 1. With regard to the other question whether the settlor has any direct or indirect benefit in the income arising under this deed of settlement, I agree that for the reasons given by my learned brother the settlor has no such direct or indirect benefit. I, therefore, agree that the question raised in the reference should be answered in the manner suggested.

Reference answered accordingly.