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C. R. NAGAPPA

v.

THE COMMISSIONER OF INCOME-TAX, MYSORE

September 4, 1968

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[J. C. SHAH, V. RAMASWAMI AND A. N. GROVER, JJ.]

Income-tax Act, 1961, s. 161(1) and (2)—Scope of—Whether trust income must be assessed in the hands of the trustee as 'representative assessee'—Or can be assessed in settlor's hands under s. 64(v) or in the beneficiary's hands.

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The appellant settled certain properties for the benefit of his minor children under several deeds of trust and vested the properties in four trustees of whom he was one. Under each deed of trust a portion of the income of the trust was to be utilized immediately for the benefit of the beneficiaries and the balance accumulated. In the course of the appellant's assessment to income-tax for the year 1962-63, the income arising from the trust properties and used for the immediate benefit of the beneficiaries was included in the appellant's total income. The Commissioner directed under s. 263 of the Act that the income for the deferred benefit of the minor beneficiaries be also included in the appellant's total income.

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It was contended on behalf of the appellant that the Income-tax Officer was bound to assess the income under each deed of trust separately in the hands of the trustees as "representative assessee" and was incompetent in view of the express enactment of s. 161(2) to assess the income in the hands of the appellant or of the beneficiaries; that notwithstanding the express direction in s. 64(v) of the Act to include the income under the trust in the total income of the settlor, the Income-tax Officer was obliged to assess the income used or accumulated for the benefit of minors in the hands of the trustees; and that the assessments on the minor beneficiaries for the year 1962-63 having been completed there was a bar to the assessment of the income in the hands of the appellant for the same year. The Income-tax Appellate Tribunal rejected the appellant's contentions and the High Court, upon a reference, also decided against him. On appeal to this Court,

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HELD, dismissing the appeal :

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It is implicit in the terms of s. 161(1) that the Income-tax Officer may assess a representative assessee as regards income in respect of which he is a representative assessee, but he is not bound to do so. He may assess either the percentage assessee or the person represented by him. The contention that since the trustees were assessable in respect of the income of the beneficiaries under s. 161(1), that income could not by virtue of sub-s. (2) of s. 161 be assessed in the hands of the beneficiary is contrary to the plain terms of s. 166. Sub-section (2) of s. 161, which was presumably intended to remove a conflict of judicial opinion, does not purport to deny the Income-tax Officer the option to assess the income in the hands of the person represented by the representative assessee: it merely enacts that when a representative assessee is assessed to tax in exercise of the option of the revenue, he shall be assessed under Ch. XV and shall not in respect of that income be assessed under any other provision of the Act. [982 E-F; 983 A-B; 984 F-G]

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By the express injunction in s. 64(v) income which accrues from the assets settled by the appellant upon the trustees for the benefit of his

minor children was liable to be included in his total income. Section 161(1) predicates the existence of income liable to tax: where income from a trust is made exigible to tax in the hands of the settlor, it cannot be brought to tax in the hands of the beneficiary or the trustee, for the income is already charged to tax in the hands of the settlor. If the income cannot be brought to tax under sub-s. (1) of s. 161, there is no scope for the application of sub-s. (2). [1984 D-F]

Although in the present case, the minors were assessed to tax for the assessment year 1962-63 that assessment will not affect the validity of the inclusion of the trust income in the assessment made on the appellant under s. 64(v).

Case law referred to.

CIVIL APPELLATE JURISDICTION : Civil Appeal No. 1374 of 1967.

Appeals by special leave from the judgment and order dated December 15, 1966 of the Mysore High Court in I.T.R.C. No. 7 of 1966.

K. Srinivasan and R. Gopalakrishnan, for the appellant.

T. A. Ramachandran, R. N. Sachthey and B. D. Sharma, for the respondent.

The Judgment of the Court was delivered by

Shah, J. C. R. Nagappa executed on April 14, 1955, seven separate deeds of trust settling specific properties for the benefit of his minor children. Under each deed Nagappa settled certain properties for the benefit of his named minor child and vested the properties in four trustees—Nagappa, his two wives and a married daughter. Under each deed of trust a portion of the income arising out of the trust property was to be utilised immediately for the benefit of the beneficiary and the balance was to be accumulated for his or her benefit and to be handed over to the beneficiary at a future date specified in the deed.

In the proceeding for assessment for the year 1962-63, the 5th Income-tax Officer, City Circle II, Bangalore, included in the total income of Nagappa the income arising from the trust properties and used for the immediate benefit of the beneficiaries, but not the income directed to be accumulated. The Commissioner in exercise of the power under s. 263 of the Income-tax Act, 1961 directed that the income for the deferred benefit of the minor beneficiaries be also included in the total income of Nagappa. In appeal against that order to the Income-tax Appellate Tribunal, Nagappa contended that the income from trust properties was liable to be assessed under s. 161(1) only in the hands of the trustees, and not in the hands of the settlor. The Tribunal rejected that contention. At the instance of Nagappa, the Tribunal referred two questions for the opinion of the High Court of Mysore :

A “(1) Whether having regard to the provisions of sub-s. (2) of s. 161, s. 64(v) of the Income-tax Act was applicable to the assessee’s case for computing the assessee’s income for the assessment year 1962-63 ?

B (2) Whether the assessments on the minor beneficiaries for the assessment year 1962-63 are a bar for assessing the income (assessed in the hands of the minor beneficiaries) in the hands of the assessee for the same assessment year 1962-63 ?”

The High Court of Mysore recorded answers to the questions as follows :

C “(1) Section 64(v) of the Income-tax Act, 1961, was rightly applied to the assessee’s case for computing his income for the assessment year 1962-63. Sub-section (2) of s. 161 of the Act does not make s. 64(v) inapplicable to the case of the assessee.

D (2) The assessments on the minor beneficiaries for the assessment year 1962-63, though in themselves illegal in view of the above answer do not in law operate as a bar for the application of s. 64(v) to the case of the assessee, the illegality of the assessments on the minors being open to correction otherwise.”

E Nagappa has appealed against the order passed by the High Court.

F Counsel for Nagappa contended that the Income-tax Officer was bound to assess the income under each deed of trust separately in the hands of the trustees as “representative assessee” and was incompetent in view of the express enactment of sub-s. (2) of s. 161 to assess the income in the hands of Nagappa or of the beneficiaries. Counsel argued that notwithstanding the express direction in s. 64(v) of the Act to include the income under the trust in the conditions specified therein in the total income of the settlor, the Income-tax Officer is powerless to resort to that provision and is obliged to assess the income used or accumulated for the benefit of minors in the hands of the trustees.

G Section 160 of the Income-tax Act defines “representative assessee”. Sub-section (1) of s. 160 insofar as the definition is relevant provides :

“For the purposes of this Act ‘representative assessee’ means—

H (iv) in respect of income which a trustee appointed under a trust declared by a duly executed instrument in writing whether testamentary or otherwise (includ-

ingany wakf deed which is valid under the Mussalman Wakf Validating Act, 1913 (6 of 1913) receives or is entitled to receive on behalf or for the benefit of any person, such trustee or trustees.”

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By sub-s. (2) of s. 160 it is provided that every representative assessee shall be deemed to be an assessee for the purposes of the Act. Section 161 deals with the liability of a representative assessee. It provides :

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“(1) Every representative assessee, as regards the income in respect of which he is a representative assessee, shall be subject to the same duties, responsibilities and liabilities as if the income were income received by or accruing to or in favour of him beneficially, and shall be liable to assessment in his own name in respect of that income; but any such assessment shall be deemed to be made upon him in his representative capacity only, and the tax shall, subject to the other provisions contained in this Chapter, be levied upon and recovered from him in like manner and to the same extent as it would be leviable upon and recoverable from the person represented by him.

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(2) Where any person is, in respect of any income, assessable under this Chapter in the capacity of a representative assessee, he shall not, in respect of that income, be assessed under any other provision of this Act.”

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It is implicit in the terms of sub-s. (1) that the Income-tax Officer may assess a representative assessee as regards income in respect of which he is a representative assessee, but he is not bound to do so. He may assess either the representative assessee or the person represented by him. That is expressly so enacted in s. 166 which states :

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“Nothing in the foregoing section in this Chapter shall prevent either the direct assessment of the person on whose behalf or for whose benefit income therein referred to is receivable, or the recovery from such person of the tax payable in respect of such income.”

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The Income-tax Officer may therefore assess the person represented in respect of the income of the trust property and the appropriate provisions of the Income-tax Act relating to the computation of the total income and the manner in which the income is to be computed will apply to that assessment. The Income-tax Officer may in appropriate cases assess the representative assessee in respect of that income and limited to that extent, and tax may be levied and recovered from him to the same extent as may be leviable and recoverable from the person represented by him.

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A The contention raised by counsel for Nagappa that since the trustees were assessable in respect of the income of the beneficiaries under s. 161(1), that income could not by virtue of sub-s. (2) of s. 161 be assessed in the hands of the beneficiary is contrary to the plain terms of s. 166. Sub-section (2) of s. 161 does not purport to deny the Income-tax Officer the option to

B assess the income in the hands of the person represented by the representative assessee : it merely enacts that when a representative assessee is assessed to tax in exercise of the option of the revenue, he shall be assessed under Ch. XV and shall not in respect of that income be assessed under any other provision of the Act. We will presently state the reasons why the rule was so

C enacted by the Parliament. But on the plain word used by the Parliament the plea raised by counsel that the representative assessee alone may be assessed as regards income in respect of which he is a representative assessee cannot be accepted.

We may now examine whether the income under the deeds of trust could not be included in the total income of Nagappa.

D By s. 4 of the Act the charge of income-tax is imposed in respect of the *total income* of the previous year of every person, and by s. 5 the scope of total income is determined. Chapter IV deals with computation of total income of an assessee under different heads and by Ch. V income of other persons in certain conditions is liable to be included in the assessee's total income. Section 64, which falls in Ch. V, provides :

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"In computing the total income of any individual, there shall be included all such income as arises directly or indirectly—

(i) to the spouse of such individual from the membership of the spouse in a firm carrying on a business in which such individual is a partner;

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(ii) to a minor child of such individual from the admission of the minor to the benefits of partnership in a firm in which such individual is a partner;

(iii) subject to the provisions of clause (i) of section 27 to the spouse of such individual from assets transferred directly or indirectly to the spouse by such individual otherwise than for adequate consideration or in connection with an agreement to live apart;

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(iv) subject to the provisions of clause (i) of section 27, to a minor child, not being a married daughter of such individual, from assets transferred directly or indirectly to the minor child by such individual otherwise than for adequate consideration; and

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(v) to any person or association of persons from assets transferred otherwise than for adequate consideration to the person or association of persons by such individual, to the extent to which the income from such assets is for the immediate or deferred benefit of his or her spouse or minor child (not being a married daughter) or both.

Explanation.—

It is clear that in each of the five cases income which in truth is not the income of the assessee is directed in the special conditions prescribed to be included in the total income of the assessee. Where an individual has transferred assets without adequate consideration to another person or association of persons, the income from the assets intended for the benefit immediate or deferred of the spouse or minor child of such individual is, by cl. (v), liable to be included the income of the individual. There is no doubt that the word "transferred" includes settled under a trust.

By the express injunction in s. 64(v) income which accrues from the assets settled by Nagappa upon the trustees for the benefit of his minor children was liable to be included in his total income. The income to the extent to which it is liable to be included in the total income of Nagappa could not again be brought for the purpose of assessment to tax in the total income of the minor children or of the trustees to whom it is transferred. Section 161(1) predicates the existence of income liable to tax: where income from a trust is made exigible to tax in the hands of the settlor, it cannot be brought to tax in the hands of the beneficiary or the trustee, for the income is already charged to tax in the hands of the settlor. If the income cannot be brought to tax under sub-s. (1) of s. 161, there is no scope for the application of sub-s. (2).

Sub-section (2) of s. 161 was presumably intended to remove the conflict of judicial opinion which arose in the interpretation of the analogous provisions of ss. 40 & 41 of the Indian Income-tax Act of 1922. In *Saifudin Alimohamed and Anr. v. Commissioner of Income-tax Bombay City*⁽¹⁾ the Bombay High Court expressed the opinion (which was not necessary for the ultimate decision of the reference) that s. 41 conferred an option upon the Income-tax Officer either to assess the income as the income of the beneficiary or as the income of the trustee. The Court observed at p. 247 in dealing with the case in which the trustees appointed by the Civil Court in a suit were carrying on the business on behalf of two minors:

"..... it was open to the department to have assessed the income of the guardians under Section 10 on

(1) 25 I.T.R. 237.

A the basis that the particular business was carried on
 by the guardians in their own right, and the taxing de-
 partment could have taken up the stand that they had
 no concern with what the guardians did with the pro-
 fits after they had paid the tax on the income from the
 business; or it was open to the department to proceed
 B against the guardians under Section 41 and to tax in
 their hands only that income which they had received
 on behalf of the minors."

It was apparently assumed that it was open to the Income-tax
 Officer either to assess and tax the guardians and if they were
 owners of the business and of the income accruing therefrom, or
 C to tax them as trustees under s. 41. In so assuming the Court
 exalted ss. 40 & 41 into quasi-charging sections. The observa-
 tion was plainly *obiter*, for the Income-tax Department had assess-
 ed the income in the hands of the guardians as trustees under
 s. 41.

D In a later judgment of the same High Court, the Court revers-
 ed the earlier opinion : *Commissioner of Income-tax Ahmedabad*
v. Balwantrai Jethalal Vaidya⁽¹⁾. The Court held in that case
 that the liability of trustees to income-tax is co-extensive with that
 of the beneficiaries and cannot in any case be a larger or wider
 liability. If the assessment is made upon a trustee, his liability
 to pay tax must be determined in accordance with s. 41 of the
 E Income-tax Act. It was observed in that case that s. 41 gives no
 option to the Taxing Department to treat the income received by
 the trustee on behalf of the beneficiary as his own income or to
 treat it as the income of the trustee on behalf of the beneficiary.
 It was further observed :

F "If the assessment is upon a trustee, the tax has to
 be levied and recovered in the manner provided in sec-
 tion 41. The only option that the Legislature gives is
 the option embodied in sub-section (2) of section 41,
 and that option is that the Department may assess the
 beneficiaries instead of the trustees, or having assessed
 the trustees it may proceed to recover the tax from the
 G beneficiaries. But on principle the contention of the
 Department cannot be accepted that, when a trustee is
 being assessed to tax, his burden which will ultimately
 fall upon the beneficiaries should be increased and whe-
 ther that burden should be increased or not should be
 left to the option of the Department. The basic idea
 underlying section 41, and which is in conformity with
 H principle, is that the liability of the trustees should be
 • co-extensive with that of the beneficiaries and in no

(1) 34 I.T.R. 187.

sense a wider or a larger liability. Therefore, it is clear that every case of an assessment against a trustee must fall under section 41, and it is equally clear that, even though a trustee is being assessed, the assessment must proceed in the manner laid down in Chapter III." A

The earlier judgment of the Bombay High Court was followed by the Madras High Court in *V. Ramaswamy Iyengar and Anr. v. Commissioner of Income-tax Madras*⁽¹⁾. The principle underlying the judgment in *Balwantrai Jethalal Vaidya's case*⁽²⁾ was approved in *Birendra Kumar Datta v. Commissioner of Income-tax, Calcutta*⁽³⁾; and *A. Razzak v. Commissioner of Income-tax, West Bengal*⁽⁴⁾. B

In our opinion the observations made in *Saifudin Alimohameds case*⁽⁵⁾ (set out earlier herein) were incorrect. The Legislature while enacting the new Act, to avoid doubts has given effect to the observations made by Chagla, C.J., in *Balwantrai Jethalal Vaidya's case*⁽²⁾ and has enacted that where the income is assessable under Ch. XV in the hands of a person in the capacity of a representative assessee it is not liable to be assessed under any other provision of the Act that is, the tax is not liable to be levied under any other provision of the Act. C

In our view Chagla, C.J., was right in observing in *Balwantrai Jethalal's Vaidya's case*⁽²⁾, in dealing with the scheme of s. 41 of the Income-tax Act, 1922, that— D

"..... it is clear that every case of an assessment against a trustee must fall under section 41, and it is equally clear that, even though a trustee is being assessed, the assessment must proceed in the manner laid down in Chapter III. . . . Section 41 only comes into play after the income has been computed in accordance with Chapter III. Then the question of payment of tax arises and it is at that stage that section 41 issues a mandate on the Taxing Department that, when they are dealing with the income of a trustee, they must levy the tax and recover it in the manner laid down in section 41." E

The same considerations must apply in the interpretation of s. 161 (2) of the Income-tax Act, 1961. F

Sub-section (2) of s. 161 merely enacts that when income is assessed in the hands of a representative assessee in his own name, the assessment shall be deemed to be made upon him in the G

(1) 40 I.T.R. 377.

(2) 34 I.T.R. 187.

(3) 42 I.T.R. 661.

(4) 48 I.T.R. 278.

(5) 25 I.T.R. 237.

- A representative capacity only and tax shall be levied and recovered in the manner provided in sub-s. (1).

It is true that in this case for the assessment year 1962-63 the minors were assessed to tax, but the assessment will not affect the validity of the inclusion of the trust income in the assessment made on Nagappa under s. 64(v). It was conceded before the High Court on behalf of the Revenue that the assessment of the minor beneficiaries in respect of the income could not stand, in view of the assessment of Nagappa under s. 64(v). In our view that concession was rightly made, and we have no doubt that all the assessments made against the minor beneficiaries will be annulled and the tax, if any, recovered will be refunded.

- C In the view we have taken, this appeal must fail and is dismissed with costs.

R.K.P.S.

Appeal dismissed.