Tax Treatment Of Private Trusts

K. Srinivasan

NATIONAL INSTITUTE OF PUBLIC FINANCE AND POLICY

Trusts are intermediaries between the taxpayers and the Revenue, like partnerships and companies. While India has had a long tradition in religious and charitable endowments, private trusts came to India at about the same time as the income tax. In their present form, both had their origin in Britain. In this book, the author examines the interaction of the private trust and taxation laws. He outlines the existing system of tax treatment of private trusts and brings out some of its deficiencies. He also shows how trusts tend to be used for tax avoidance purposes, particularly by taxpayers in the high income brackets, and suggests the lines on which the law can be amended to counteract such avoidance.

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OF PRIVATE TRUSTS

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Foreword

The National Institute of Public Finance and Policy is an autonomous, non-profit society engaged in research and training in the area of public finance and policy. The Institute also undertakes consultancy work on behalf of the Central and State governments as well as international agencies and other public bodies. In addition, it undertakes studies on its own, on subjects of importance from the national point of view, particularly in terms of policy formulation.

The use of private and public trusts for tax planning purposes and the proper tax treatment of these entities have evoked considerable interest and controversy in recent years.

The subject is a vast one, as it covers private trusts, public trusts of various kinds and employee welfare trusts. The scope of the present study is limited to the tax treatment of private trusts. Its author, Shri K. Srinivasan, who was formerly a Member of the Central Board of Direct Taxes, has outlined the history of the legislation on the subject, the existing law and some of the difficulties experienced in its working. He has also indicated the legislative action required to plug the still existing loopholes and to effect the necessary improvements in the administration of the law. The Institute decided to sponsor this study because of the intrinsic importance of the subject on which no standard book has been written to-date. It is hoped that the book will meet the felt need for an analysis of the law and the facts available on the subject.

The Governing Body of the Institute does not take responsibility for the views and analysis presented in the study. In respect of the reports and publications of the Institute, generally speaking, besides the author, the Director and the other staff associated with the concerned project also share the responsibility for the basic approach and views. However, in

the present case, Shri Srinivasan, who is an acknowledged expert in the field of direct taxation, was given the sole responsibility for conducting the study. And the views expressed and the conclusions arrived at are his own and do not necessarily reflect those of the Institute.

September 30, 1983
New Delhi

R. J. CHELLIAH
Director

Preface

ONE of the reasons why taxes tend to be complicated all over the world is that they are subject to various other laws which directly or indirectly affect the income and property rights of a person. Even the countries which do not have to cope with the intricacies of the Hindu law or the Mohammedan law have not succeeded in simplifying their tax statutes significantly. The problem is accentuated in India not merely by the influence which the personal laws exercise on various aspects of social life and economic activity but also by the import of the distinctively British concept of trusts. The direct taxes system in India has suffered a great deal from the piecemeal, patch-work, disharmonised legislation through which it is trying to adjust itself to this medley of laws.

The attempt in this book is confined to an appraisal of the position of private trusts in the levy of direct taxes in India. The general law governing trusts is summarised in the first Chapter; and the second Chapter indicates the role of trusts as one of the intermediaries in taxation. The current tax treatment of private trusts and how it has evolved over a period of years are explained in Chapter 3. Chapter 4 describes how trusts have fared in other countries. The inadequacy of the existing provisions in the tax statutes in India is brought out in Chapter 5, and their indifference to the principles of equity and neutrality in Chapter 6. Some of the common methods of tax avoidance through trusts are set out in Chapter 7, with suggestions on the action needed to neutralise them in Chapter 8. Chapter 9 points out how scanty are the data available to show the extent of the use of private trusts in the country, while the last chapter briefly indicates the view one can reasonably take on the treatment to be accorded to private trusts in the light of the picture that emerges from the earlier chapters.

The case law on the points made in the text and also clarifications on some of the issues with which it was not considered necessary to burden the text, are furnished in the notes at the end of each chapter. They are supplemented by the additional notes preceding the index, seeking to cover further facts and court decisions that could not be incorporated in the body of the text or the notes following the different chapters.

More data are available on public trusts than on private trusts, which are veiled in secrecy and which are of relatively limited interest to the public though they cause constant vexation to the Revenue. Apart from the availability of more information in some of the States which have statutory regulation and supervision of public trusts, charitable and religious trusts have a pervasive impact on the day-to-day life of the community. They raise issues of greater public interest than private trusts which primarily concern the affluent. India has had a long tradition in public endowments and the law on several aspects of this subject is settled by court rulings, despite the absence of a comprehensive central legislation. The implications of the tax privileges that public trusts enjoy require detailed consideration in a separate book. It is proposed to deal with the employee welfare and other allied trusts also along with religious and charitable trusts.

My debt of gratitude to Dr. R. J. Chelliah is very heavy. He has taken the trouble of going through the text completely and with great care and given invaluable suggestions. More than this help, I must confess that it would not have been possible for me to write this book but for my association with the Institute as a Consultant, for which Dr. Chelliah is responsible.

The first draft of this book was shown to Dr. I. S. Gulati whose comments and advice have been duly taken into account. I ventured on this study on the suggestion of Dr. Amaresh Bagchi and I have had the benefit of discussing the contents of the book with him at length from time to time. I owe a lot to both Dr. Gulati and Dr. Bagchi.

I must also acknowledge the considerable help I have received from Mr. Christopher Cecil in editing the book; his tireless energy and zeal have speeded up the printing and

publication of the book. I am thankful to the banks which have taken the trouble of supplying me the information that I needed, to the extent possible for them. Some of the banks could have been more helpful, but they apparently believe that they are rendering a service to their constituents by withholding general statistical data.

I have received the maximum practicable secretarial assistance from Mr. Suhas Kumar. I must place on record his outstanding ability as a stenographer and his excellent language sense, which have made my task lighter.

I may make it clear that this book is not a commentary as such on any provisions of the Income-tax and other Acts. It is more in the nature of a study of the background and the implications of the current tax treatment of trusts and the extent to which it is susceptible of improvement.

September 30, 1983
New Delhi

K. SRINIVASAN

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AC	Appeal Cases
ACED	Assistant Controller of Estate Duty
AG	Attorney General
AIR	All India Reporter
All	Allahabad
All ER	All England Law Reports
All ER Rep	All England Law Report Reprints
ALT	Andhra Law Times
AP	Andhra Pradesh
APLJ	Andhra Pradesh Law Journal
App Cas	Law Reports, Appeal Cases, House of Lords 15 Vols. 1875-1890
As	Assam
ATC	Annotated Tax Cases
Beav	Beavan's Reports, Rolls Court, 36 Vol. 1838-1866
BLJR	Bihar Law Journal Reports
Bom	Bombay
BTR	British Tax Review
CA	Court of Appeal
CAL	Calcutta
CBDT	Central Board of Direct Taxes
Commr	Commissioner
Commr Agl IT	Commissioner of Agricultural Income Tax
Ch	Reports in Chancery
Ch D	Chancery Division
CGT	Commissioner of Gift Tax
CIT	Commissioner of Income Tax
CWT	Commissioner of Wealth Tax
CED	Controller of Estate Duty

CLD	Calcutta Law Journal
CLR	Calcutta Law Report
CTR	Current Tax Report
CLP	Current Legal Problems
CWN	Calcutta Weekly Notes
De GF & J	De Gex, Fisher and Jones Chancery
Del	Delhi
DLT	Delhi Law Times
ED	Estate Duty
ER	English Reports
FA	Finance Act
FB	Full Bench
Gau	Gauhati
GLR	Gujarat Law Report
GT	Gift Tax
Guj	Gujarat
Hare	Hare's Reports, Vice-Chancellor's Court
HL	House of Lords
HP	Himachal Pradesh
IA	Indian Appeals
IC	Indian Cases
ILR	Indian Law Reports
In re	In regard to
IR	Inland Revenue Commissioners
IT	Income Tax
ITAT	Income Tax Appellate Tribunal
ITC	Income Tax Cases
ITO	Income Tax Officer
ITR	Income Tax Reports
JK	Jammu & Kashmir
Jur (OS)	Jurist Reports (Old Series)
Kar	Karnataka
KB	King's Bench
Ker	Kerala
Lah	Lahore
LJ	Law Journal (British)
LJKB	Law Journal King's Bench (British)

LR	Law Reports (British)
LT	Law Times Reports (British)
Mad	Madras
MLJ	Madras Law Journal
MLW	Madras Law Weekly
MP	Madhya Pradesh
MPLJ	Madhya Pradesh Law Journal
MWN	Madras Weekly Notes
Myl & K	Mylne and Keen's Reports, Chancery (British)
Mys	Mysore
Nag	Nagpur
NLJ	Nagpur Law Journal
OR	Orissa
OWN	Oudh Weekly Notes
Pat	Patna
PC	Privy Council
PH	Punjab and Haryana
PLR	Punjab Law Reporter
Punj & Har	Punjab and Haryana
QB	Queen's Bench
Raj	Rajasthan
Rang	Rangoon
Re	Regarding
RLW	Rajasthan Law Weekly
SC	Supreme Court
SJ	Solicitor's Journal
SCR	Supreme Court Reports
Sim	Simon's Reports, Vice-Chancellor's Court
SLP	Special Leave Petition
Taxman	Taxman (Monthly Magazine)
Tax LR	Taxation Law Reports
TC	Tax Cases
TLR	Times Law Reports (British)
TMA	Taxes Management Act, 1970
V	Versus
Ves Jun	Vessey Junior's Reports, Chancery

WLR	Weekly Law Reports (British)
Wilm	Wilmot's Notes of Opinions and Judgments (British)
WR	Weekly Reports (British)
WT	Wealth Tax

1

Introduction

Origin of Trusts

THOUGH the law of trusts has developed its own specialised vocabulary, there is no satisfactory definition of a trust. In essence, it is an arrangement by which property is transferred to one person for the benefit of another. The trust concept, which has been acclaimed as a valuable British contribution to jurisprudence, is not commercial in its origin like the company or partnership. It started as a device for getting round the restraints which the Crown placed on transfers of property to the Church and also as a method of effecting family settlements.

In the 16th century, the Church in England had acquired extensive properties, which it held in perpetuity, making it impossible for the feudal superior to get them back. The Statutes of Mortmain tried to curb further expansion by insisting that a licence in mortmain should be obtained whenever any land was proposed to be transferred to a religious body. There was a second problem. The law did not provide for a testamentary transfer of land. Only movable property could pass by will. When a vassal died, his lord was entitled to various benefits called "relief", "wardship", and so on, if the heir happened to be a minor. In the absence of an heir by blood, the property went to the lord by escheat. These difficulties were by-passed by transfer of land to a friend for the "use" or benefit of the Church or any one else in whom the donor was interested.

Since such "uses" were not enforceable under the common law, litigation arising from them was taken to the Court of

Chancery. It was in protecting the interest of the beneficiary (the *cestui que*) that the distinction between the equitable ownership and the legal ownership of property was drawn. The legal concept of trust evolved from this distinction.

An attempt was made to abolish "uses" through the Statute of Uses 1536, but it did not succeed because its operation was limited to the first "use" of a property. People got round the Act through the method of "use upon use", e.g., by conveying free-hold land to "A" to the use of "B" to the use of "C". The Property Act of 1925 repealed the Statute of Uses, enabling the conveyance of land to "A" in trust for "B".

Utility

Though the trust originated as a strategy for resisting autocratic attempts to prevent gift of land—for avoiding feudal dues and the restraints of the mortmain Statutes in settling land—it has served a variety of social and personal purposes. The following are among such uses of the trust in recent times :

i. It has emerged as a very convenient instrument for running religious and charitable organisations.

ii. Another welcome development is the evolution of trusts for the benefit of employees—provident funds, pension schemes, gratuity funds, benevolent funds, etc. The Unit Trust has also enlarged the sphere of trust services, by enabling a small investor to get the advantages of a varied portfolio.

iii. A trust is the best possible arrangement for managing funds for those who are incapable of doing so themselves—e.g., minors, lunatics and the mentally retarded.

iv. A trust provides the means to carve out separate benefits in the same property for different persons in whom one is interested. It ensures that the persons entitled to succeed to a property eventually do get the benefit, which may be difficult to secure through outright gifts, e.g., life-interest for the spouse with remainder to the children, facilitating comfort for the

spouse for her life-time, without detriment to the children's long-term interest.

v. A trust can prevent dissipation of a profligate's inheritance.

vi. The most attractive feature of a trust is that it helps to reduce the liability to the different direct taxes within the framework of the law.

The concept of dual ownership, i.e., equitable and legal ownership, was unknown to the Hindu and Muslim laws which had, however, recognised the practice of charging the ownership of property with specific obligations, e.g., provisions for the maintenance of a daughter or daughter-in law or minor children.[1] The position of the *karta* or manager of a Hindu undivided family and also the *benami*[2] system illustrate the variety of forms in which fiduciary relations have exhibited themselves in India from ancient times. Similarly, while trusts as such have not had any special part to play in the sphere of religion in India, endowments of the nature of trusts for religious and charitable purposes have been noticed from the beginning of the country's recorded history. In recent years, however, charities have preferred the form of trusts to endowments.

The Indian Trusts Act, 1882, does not affect the mutual relations of the members of a Hindu undivided family or the rules of the Muslim law as to *waqfs* or private and public religious endowments or public charitable endowments. Apart from Parsis, Christians and also Hindus and Muslims, who had no legal compulsion to conform to their personal law in this regard, there was a large body of Englishmen and Anglo-Indians who were taking advantage of the English trust law in India. The English law of trusts was being applied by the Indian courts, depending upon the necessities and circumstances of the cases coming up before them. The need for codification of the scattered provisions in the Indian Trustee Act, XXVII of 1866, the Statute of Frauds, the Specific Relief Act and other statutes having a bearing on trusts, resulted in the Act of 1882. It is noteworthy that though trusts have become increasingly popular, wealthy and sophisticated, the Act has undergone little change. The subject, "trust and

trustees", is in the concurrent list (item 10 in List III) of the Seventh Schedule to the Constitu tion of India but it has not evoked much interest at the Centre while the States have so far left it alone.

Law Governing Private Trusts

The Indian Trusts Act, 1882, deals with private trusts alone and many of its provisions are based on the law of trusts administered in the equity courts in England. Section 1 of the Act specifically excludes public and private religious trusts and charitable endowments from the purview of the Act. Section 3 defines a trust as "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." A trustee holds trust property not on behalf but for the benefit of the beneficiary.[3]

A trust may be created for any "lawful purpose". That is to say, it cannot be utilised to defeat the law, e.g., frustrate creditors,[4] or carry out any purpose which is repugnant to public policy, e.g., separating parents from children or restraining marriage.[5] It is distinguishable from bailment, contract, agency, or a fiduciary power.[6] A trust can be created *inter vivos* or through a will. When a trust is set up by a living person, the following are the requirements[7] :

i. The intention should be declared unambiguously. A mere expression of desire will not do[8] ;

ii. The trust property should be set apart and the settlor should divest himself of its ownership.[9] Effective conveyance is essential.[10] If the property is immovable, the trust instrument has to be in writing[11] and the registration of the property in the trustee's name is essential to complete the transfer of ownership.[12] If it is a movable, delivery of its possession to the trustee will suffice.[13] If the author of the trust has appointed himself as the trustee, registration becomes unnecessary ;[14]

iii. The objects of the trust should be clearly stated—the purposes to which the trust income and corpus should

be applied and the persons or classes of persons for whom the benefits are meant.[15] There can be no trust without one or more beneficiaries who can enforce it through courts : where a trust is for a public purpose and not for specific individuals, it can be enforced by the Advocate General of a state.

Conditions (i) and (iii) are equally applicable to a testamentary trust. Death, which brings the trust into existence, automatically strips the testator of the ownership of his property and, therefore, dispenses also with the need for registration of the property in the trustee's name as a condition precedent to the completion of the trust. When an *inter vivos* or testamentary trust is to take effect will depend on the terms of the instrument. It will be a "contingent trust" if its operation is subject to a future event.[16] A trust does not have to be couched in any technical words,[17] but a mere resolution by a trading association to hold any property in trust will not become an instrument of trust.[18] If the ownership of land or other immovable property is charged with any obligation, that should be made clear.[19] What is important is that the identity of the beneficiaries and the subject matter of the trust should not be uncertain. The intention of the author of a trust will prevail, as long as it does not involve any fraud or contravention of any law. For instance, a direction for accumulation of income is valid as long as it does not offend the rule of perpetuity.[20] There can also be no objection to additions to the corpus of a trust through gifts by the trustees or third parties, unless it is expressly prohibited in the trust instrument.[21] A trust may conduct a business either independently or in partnership with others through its trustees.[22]

Author and Beneficiaries[23]

A trust may be created by any person competent to contract. It may be brought into existence even by a minor, provided the permission of the court is obtained by his guardian for this purpose.[24] Two or more persons can also jointly set up a single trust. The subject matter of a trust must be transferable property : it precludes mere beneficial interest under a subsisting trust.[25] A single instrument can

create more than one trust.[26] Any person capable of holding property may be a beneficiary. There can be no trust without at least one existing beneficiary.[27] There can also be no trust only for the spouse of a person who is still unmarried, or unborn children, or persons who become ascertainable only on the happening of a contingency.[28] Any such trust would be *ab initio* void under Sections 3 and 6 of the Indian Trusts Act and Section 13 of the Transfer of Property Act. It would not, however, be void if an existing beneficiary is given an immediate limited interest, and an unborn person an absolute interest in the settled property at the end of the limited interest.[29] A beneficiary is not a party to a contract with the author of the trust and may, therefore, renounce his interest under the trust by a disclaimer addressed to the trustee, if he is so inclined. After a trust is set up its author cannot alter it or meddle with its working. It is possible, however, to augment the original trust funds ; and where two trusts are set up for the same beneficiaries on identical terms, with the same trustees, their coalescence is not barred.[30] Rescission of an *inter vivos* trust is feasible with a court's approval, only if there has been a genuine mistake in regard to its objects.[31] As for a testamentary trust, the grip of the "dead hand" and court supervision are even more rigid. The court's jurisdiction over it is a continuous one, from the time a will is "proved".

Trustee[32]

A trust will not fail if its author has not designated a trustee : it is an omission which can be made good by a court.[33] A person can be a trustee if he can hold property, is competent to contract and is not an insolvent : a bank or a company can also, therefore, be a trustee. The author of the trust may also be a beneficiary. A trustee may also be a beneficiary in the trust. No one is bound to accept a trust.[34] But, after having accepted it, he cannot relinquish it except with the prior permission of the court, or at the instance and with the unanimous concurrence of all the beneficiaries.[35] A trustee's responsibilities are onerous. He is bound to implement the purpose of the trust. He has to stick to the directions of its author given at the time of its creation,[36] except as modified

with the consent of all the beneficiaries. It is his duty to acquaint himself with the true state of the trust properties and take all the action necessary for the assertion or protection of the title of the properties and also their preservation.[37] He is required to deal with the trust properties as carefully as a man of ordinary prudence would deal with them if they were his own.[38] He must be impartial among the beneficiaries and refrain from exercising his discretion to the advantage of one of them at the expense of the others. He should keep clear and accurate accounts and invest the trust funds in the securities prescribed in section 20 of the Indian Trusts Act, subject to any direction contained in the instrument of trust. He cannot delegate his powers to anyone else or act singly when there are more trustees than one.[39] He is liable to compensate the loss which the trust property may suffer as a result of any negligence or breach of trust on his part.[40] He is not entitled to any remuneration for his services unless the trust deed provides for it or the court sanctions it.[41] The remuneration, if any, that he gets will not be treated as salary, since there is no employer-employee relationship, nor as professional fee, for trusteeship cannot be a profession.[42] Profits, if any, made by him by virtue of his trusteeship[43] and all improvements to the trust property effected by him, enure to the advantage of the beneficiaries. He cannot buy, lease or acquire any interest in the trust property : even a loan to him out of the trust funds may amount to a benefit.[44] He cannot put himself in a position where his interests may clash with his duties. He has a right to apply to the court for its opinion, advice or direction on questions of importance arising from the management of the trust property.[45] Any of the beneficiaries can prefer a compensation claim against him before a court for whatever is believed to have been done by him to the prejudice of the trust. Abuse of power or any other transgression by a trustee will not, however, render the trust invalid.[46] A trustee may be removed by a court under its inherent jurisdiction.[47]

The Official Trustee, who is required to have the prescribed minimum experience as an advocate or attorney of a High Court or a member of the judicial service of the State, may

be appointed as the sole trustee under the Official Trustee Act, 1915 either by a court or by the author of a private trust, with his prior concurrence. He is prohibited from accepting a trust for the benefit of the author's creditors or for a religious purpose. He cannot also accept any trust which involves the management or carrying on of any business. He may be appointed as a trustee by a will provided his prior consent has been obtained and his appointment is recited in the instrument.

The Public Trustee who is appointed by the Central Government under Section 153A of the Companies Act (I of 1956), discharges his functions and exercises the rights and powers conferred on him under that Act. Where any shares or debentures of a company exceeding Rs. 1 lakh in value or 25 per cent of the company's paid up share capital, are held in a public or private trust, the trustees of the trust are required to make a declaration of their holdings to the Public Trustee under Section 153B of the Companies Act. In such cases the Public Trustee may exercise the rights and powers of the trustees who are shareholders, including the right to vote by proxy at any meeting of the company and of any class of members of the company. The object of this provision is to ensure that the trusts are not used by any group of persons for augmenting their own voting rights in the company, and strengthening their control over the company for furthering their own business interest, to the detriment of the interests of the trust.

Classification of Trusts

A trust can be classified with reference to the manner in which it is created, or the nature of the duties it casts on the trustees, or its objects. It may be constituted through the express declaration of the settlor,[48] in which case it is known as an "express trust". It may follow the unexpressed but presumed intention of the settlor as an "implied trust". It may also be imposed by the operation of law as a "constructive trust" to cover, for example, fraudulently acquired property, or the advantage gained by a stranger to a trust receiving trust property, or even part payments made in a

purchase transaction.[49] There may be court intervention wherever unconscionable conduct is noticed in any *inter vivos* transaction. A trust is "executed" when it is complete and "executory" when it needs to be supplemented by a further instrument setting out the terms in detail. It fastens itself on the conscience of the legatee when a testator has communicated a secret obligation to him that has not been recorded in the will : such a "secret trust" is discovered from the facts and circumstances of the case.[50]

Considered from the point of view of the trustee's functions, where he has a merely passive role, the trust is a "simple" one and the trustee is a "bare trustee." If he is required to discharge any significant duties in accordance with the trust deed, he is an "active trustee" in a "special trust". A trust is "specific" when the beneficiaries and their respective shares are known, and "discretionary" when the settlor has vested the trustee with the discretion to determine how much benefit should be conferred on whom, among a group of beneficiaries indicated by him, during any particular year.[51] It is to the trust document that one must turn for finding out whether a settlor intended that a beneficiary should have an immediate vested interest or a contingent interest in the income or corpus of the trust or whether the extent of the interest had been left to the discretion of the trustees.[52]

A trust is private when its benefits are limited to one or more identifiable persons. In a public trust, the rights to the benefits are not confined to any specific individuals but are available to a fluctuating body of persons—the public at large or a cross-section of the public—answering a particular description.[53] A public trust may be charitable or religious while a private trust may be religious but cannot be charitable.[54] A private trust, which provides for charitable purposes may turn public when the private beneficiaries renounce their rights.[55] Though the terms "charity" and "religion" have a much wider connotation in India than in the UK, the USA and several other countries, there is no comprehensive statutory definition of a public trust or institution as distinct from a private one. Tests have, however, been deduced from court decisions, which make the distinction reasonably clear.[56]

The name borne by an institution cannot determine its character.[57] Easy accessibility to the public and equal treatment to all devotees are, for example, among the decisive criteria in the case of a temple or a mosque.[58] A trust for the family deity does not become "public" merely because arrangements have been made for feeding the poor or celebrating some festivals or maintaining a hospital.[59] An *akhara* (i.e., an establishment for training wrestlers) cannot claim to be a public religious trust only by reason of the installation of some idols.[60] Similarly, a trust for a pet dog or cat is not a trust for a charitable purpose but a *gaushala* or *pinjrapole* is.[61] There are, however, a few grey areas where controversies arise : for example, gifts to enable poor persons to get married[62] or financial assistance to give a person a good start in life.[63] The following are some of the purposes which have not been found charitable in the Indian courts :

(i) provision of employment ;[64]
(ii) trusts for the benefit of employees, including provident funds, gratuity funds and pension funds ;[65]
(iii) political education ;[66]
(iv) worship at tombs ;[67]
(v) advancement of cricket or other sports or gymnastics;[68] and
(vi) horse-racing.[69]

Where the application of the income of a trust depends on the trustee's discretion and some of the purposes of the trust are not charitable, the trust is not considered charitable ;[70] but a specified part of the income or corpus of a trust may be held for non-charitable purposes, without the charitable part of the trust being vitiated for tax purposes.[71]

A *debuttar*[72] estate or an endowment for the maintenance of worship of a family deity is of the nature of a private trust, though the Indian Trusts Act is not applicable to it. Dedication of property to a deity may be absolute or partial,[73] but it is not revocable.[74] It is only in a figurative sense that an idol is the owner of any property which it cannot enjoy, protect or dispose of. The purpose of an endowment to a deity is obviously not to confer any benefit on it. The beneficiaries are the members of the family privileged to offer worship at the

temple. The *shebait* of a *debuttar* estate is not a trustee because the trust property vests in the deity and not in him. He is not, however, a mere holder of an office because he may have a share in the usufruct, depending on the terms of the grant or custom or usage. His duties and his personal interests are blended.[75]

The position in the case of a *waqf-alal-aulad*[76] is analogous. The property is dedicated to and permanently detained in God, but the income is applied to the benefit of the members of the settlor's family : the usufruct is available for enjoyment by the descendants of the settlor, while the corpus is tied up in perpetuity.[77] Under the Musalman Waqf Validating Act of 1913, such a *waqf*[78] is valid, if there is an ultimate gift to charity. The *Hanafi* law, which the *Sunnis* follow, prevents the creation of a *waqf* for the benefit of the settlor and for the payment of the settlor's debts. Under the *Shia* law, a *waqf* will not be valid, unless the settlor divests himself of the ownership of the *waqf* property : he must not "eat out of the *waqf*".[79] There is no bar, however, to the aggrandisement of the settlor's family, as long as there is a provision for making the property available for pious or charitable purposes in the long run. An *imambara* (i.e., a place where Muharam ceremonies are performed) is a private *waqf* unless proved otherwise[80], while a *takia* or a *khanqa* (monastery) and a *dargah* or an *astana* or *ziayarat* (shrine) are public *waqf*s. A mosque may be either.[81] The *mutawalli*[82] who manages the *waqf's* property, is like the *shebait* of a *debuttar* estate, for all practical purposes. He is the *amin* (bailee) of God's property and is expected to conduct himself accordingly. The *waqf* may remunerate him and in the absence of a provision in the *waqf* deed the court may also allow him remuneration not exceeding one-tenth of the *waqf's* income.[83] He cannot transfer his office to anyone else.[84]

Failure of a trust—"Resulting Trust"

An imperfect or incomplete trust is not valid,[85] but a trust may be partly valid and partly void.[86] When an express public trust fails, it is saved in certain circumstances by the *cy pres*[88] doctrine. The courts permit the resources of the trust, which

has become impracticable, to be applied to some other charitable purpose which is allied to or which closely resembles the purpose of the frustrated trust. If an express private trust is invalidated either for failure of consideration, illegality, perpetuity,[88] uncertainty, lapse, disclaimer or any other reason, a trust in favour of the settlor ordinarily results.[89] If the trust has been created by a will, the trust property devolves upon the legal heirs and successors of the testator. It is a logical inference that the settled property should revert to the settlor or his legal heirs and successors if the settlement is vitiated or does not materialise for any reason. A private religious endowment governed by the Hindu law, may have a similar treatment, if voided on any ground. As for a *waqf-alal-aulad*, the property will revert to the *waqif* if the ultimate dedication for a religious, pious or charitable purpose is not *bona fide*. If, however, only one of the purposes of a *waqf* has been invalidated, the *waqf* will not be voided. There will only be acceleration of the application of the *waqf* income to other purposes.[90]

Termination of a Trust

The beneficiary of a trust is entitled to have the mistakes, if any, in a trust instrument rectified by the court and the intention of its author specifically executed to the extent of his (i.e., beneficiary's) interest, though the powers of a trustee cannot be curtailed by him.[91] Where there is only one beneficiary and he is competent to contract or where there are several beneficiaries and all of them are *sui juris*, absolutely entitled, and of one mind, he or they may bring the trust to an end, taking over the capital or dividing it among themselves, irrespective of the intention of the author of the trust. If any of the beneficiaries is not of full age or capacity and, therefore, not in a position to give a valid discharge, the court's concurrence may be required for ending the trust.[92]

It is debatable whether a private *debuttar* estate can be given a secular turn or terminated through a family consensus.[93] A *waqf-alal-aulad* may become ineffectual through a ceaseless increase in the number of its beneficiaries from generation to generation but they have no authority to put an end to it.

Tax Implications of a Trust

Since a trust holds property and derives income for the benefit of either the public at large or individuals, it is inevitable that it should have tax ramifications.

Almost every country with a system of direct taxation encourages religious and charitable institutions by offering tax immunity, if they use their income entirely for the purposes for which they have been set up and if they do not venture into any competitive trade. They are also permitted to accumulate a part of their annual income in the ordinary course. If a religious or charitable trust wants to accumulate more of its income than is normally allowed, it will have to intimate the purpose of the accumulation to the Income-tax Officer and invest the money in the specified modes. If any part of the money is used for any purpose other than the one intimated or if it ceases to remain invested in the prescribed form, it will be deemed to be the income of the trust in the year in which such deviation occurs.[94] A trust may also conduct a business subject to the condition that the business subserves its primary object,[95] and the work is mainly done by the beneficiaries.

Provident fund and other employees' welfare trusts are basically private trusts but they are given tax exemption where they are specifically approved or "recognised" by the revenue authorities and also strictly conform to the requirements of the rules framed in this regard.[96] Tax liability results only when a trust does not observe the conditions laid down by the Government for its recognition.[97] The tax liability of the trustees, the employer or the employees for the profits of any business in which the employees are offered some kind of a participatory interest will depend on the precise nature of the interest, i.e., whether it is immediately vested or deferred or contingent[98].

As for family trusts, they are as complex as the tax laws, necessitating special provisions for their treatment. The problems posed by religious and charitable trusts and trusts for employees are proposed to be considered separately. The following chapters are confined to a study of the taxation of private trusts other than trusts for employees, debenture holders and unit holders.[99]

NOTES

1. Smt. Krishna Ramani Dasi v Ananda Krishna Bose, 4 BLR 231 O.C. 278 ; Ganendra Mohan Tagore v Upendra Mohan Tagore, 4 BLR O.C. 134.

2. Literally, "without a name." In a *benami* transaction, a person acquires property with his own money, but in the name of another person. The transaction is also called *furzee*. Recourse to it may be due to various reasons, e.g,, anxiety to hide one's personal affairs from the public eye. Effect is not given to a *benami* deal if it is opposed to public policy or designed to defraud the real owner's creditors : Mulla, *Principles of Hindu Law*, 12th Ed., N.M. Tripathi (Pvt.) Ltd., Bombay, articles 604-611.

   Vide also, the observation of Sir George Farwell in the Judicial Committee's judgment in Bilas Kunwar v Desraj Ranjit Singh (1915) 42 IA 202 ; 37 All 557 ; 19 CWN 1207 : "It is quite unobjectionable and has a curious resemblance to the doctrine of English law, that the trust of the legal estate results to the man who pays the purchase-money, and again follows the analogy of our common law, that where feoffment is made without consideration, the use results to the feoffer."

   As for the practice among Muslims, see Uzhar Ali v Ultaf Fatima 13 MIA 346 ; Abid Ali v Asgar Ali 7 NLR 159. However, it has been held in Gosia Begum v Mohmd. Ghaziuddin, AIR 1956 Hyd 52 that the *benami* law is not a branch of Hindu or Muslim law but merely an application of the equitable general rule laid down in sections 81 and 82 of the Indian Trusts Act, 1882.

3. Suhasini Karuri v WTO (1962) 46 ITR 953 (Cal) ; Chintamani Ghosh Trust v CWT (1971) 80 ITR 331 (All) ; CWT v Phirozsha Pestanji (1974) 96 ITR 185 (Guj).

4. Illustration (c), section 4, Indian Trusts Act. Also, Elliot, Official Receiver, Cuddappah v Subbiah, 50 Mad 815. But a *waqf* to defraud the *waqif's* creditors cannot be revoked by the *waqif* or his heirs though the court may strike it down : Zafrul Hussan v Farid-ud-din AIR 1946 PC 177 ; Har Prasad v Mohammed Usman AIR 1943 All 2.

5. For trusts interfering with parental duties, Re. Sandbrook (1912) 2 Ch. 471 ; Re. Boulter (1922) 1 Ch. 75 ; Re. Piper, Dodd v Piper (1946) 2 All ER 503. For a trust voided on the ground of restraint of marriage, Lloyd v Lloyd (1852) 2 Sim. (N.S.) 255 ; White and Tudor, *Leading Cases in Equity*, 9th Ed, Vol. 1, p. 487. Curiously, requirement of consent to marriage will be

valid : Re. Whiting's Settlement, Whiting v De Rutzen (1905) 1 Ch. 96. So also, a limitation of property until marriage, Re. Lovell Sparks v Southall (1920) 1 Ch. 122.

6. McPhail v Doulton (1971) AC 424, (1970) 2 All ER 228 ; Re Gulbenkian's Settlement Trusts (1968) 3 All ER 785.

7. The three conditions commonly known as the "three certainties" required in a trust have been spelt out by Lord Langdale MR in Knight v Knight (1840) 3 Beav 148, 173. They are covered in section 6 of the Indian Trusts Act, 1882.

8. CIT v Manilal Dhanji (1962) 44 ITR 876, 885-6 (SC) ; CIT v Mrs. Jayalakshmi Duraiswamy (1964) 53 ITR 525 (Mad) ; CIT v Sardar Bahadur Sardar Inder Singh Trust (1956) 29 ITR 781 (Cal) ; Ram Ran Vijay Prasad Singh v Province of Bihar AIR 1942 Pat 435 (FB), (1942) 10 ITR 446 (Pat) ; Zafar Hussain v M. Ghiasuddin AIR 1937 Lah 552 (regarding a *waqf*) ; Chambers v Chambers AIR 1944 PC 78 ; Krishnamurthi v Anjayya AIR 1936 Mad 635 ; Chotabhai v Jnan Chandra, AIR 1935 PC 97 ; Re. Kayford Ltd. (1975) 1 All ER 604, (1975) 1 WLR 279 ; Re. Williams (1897) 2 Ch. 12 ; In re. Booth : Booth v Booth (1894) 2 Ch. 282 ; Jones v Lock (1865) 1 Ch. App. 25 ; Raikes v Ward (1842) 66 ER 1106 ; Woods v Woods (1836) 40 ER 429, 43 RR 214.

9. Retention of any powers over the trust property may be inconsistent with the divestiture that is required : The Allahabad Bank Ltd. v CIT (1953) 24 ITR 519 (SC). There is neither a trust nor a gift if the author of the trust merely executes an instrument, but does not transfer the purported trust property to the trustees : CGT v Maharaja Pateshwari Prasad Singh (1971) 82 ITR 654 (All).

10. Richards v Delbridge (1874) LR 18 Eq. 11.

11. Jang Bahadur v Rana Umanath Baksh Singh AIR 1937 Oudh 99 ; Anant Ram v Ishri Prasad AIR 1925 Oudh 201 ; Kesheo v Laxminarayan AIR 1926 Nag. 46 ; Kumuruddeen v Noor Mohammed 28 Mad LJ 251.

12. Smt. Pankumari Kochar v CED (1969) 73 ITR 373 (AP). If the value of an immovable property that is transferred to a trust exceeds Rs. 100, the law of registration cannot be avoided. Religious endowments are, however, outside its purview.

13. Pachaiyappa Chetty v Shivakami Ammal AIR 1926 Mad 109 ; Chambers v Chambers AIR 1940 PC 78. In order to render a settlement of shares valid and effective, the transfer of the shares will have to be executed in accordance with the articles of the company : Milroy v Lord (1862) 2 De GF & J. 264, (1861-73) All ER Rep 783 ; Re Rose (1952) 1 All ER 1217.

14. Richard v Delbridge LR 18 Eq. 11 ; Gharib Das v Munshi A Hamid AIR 1970 SC 1035 ; Tulsidas Kilachand v CIT (1961) 42 ITR 1,6 (SC) ; Smt. Pankumari Kochar v CED (1969) 73 ITR 373 (AP).
15. Mcphail v Doulton (1971) AC 424, (1970) 2 All ER 228 ; Gulbenkian's Settlements, Re (1970) AC 508 ; Baden's Deed Trusts (No. 2) (1972) 2 All ER 1034 ; Burrough v Philcox (1840) MYL & Cr 72.
16. Re. Turner's Will Trusts (1937) Ch. 15 ; Re. Watt's Will Trusts (1936) 2 All ER 1555 ; Re. Ransome (1957) 1 All ER 690 : Re. Holford (1894) 3 Ch. 30.
17. CIT v Tollyganj Club Ltd. (1977) 107 ITR 776 (SC) ; CIT v Thakurdas Bhargava (1960) 40 ITR 301 (SC) ; CIT v Lad Parishad Karyalaya (1974) 94 ITR 359, 360 (Bom) ; CIT v Cutchi Lohana Panchtade Mahajan Trust (1975) 98 ITR 448 (Bom) ; CIT v Pramod Jain Trust (1971) 81 ITR 604 (Del.) ; A.J. Patel v CIT (1974) 97 ITR 683 (Bom.) ; S. Devaraj v CWT (1973) 90 ITR 400 (Mad) ; Keshava Panickar v Damodara Panicker AIR 1970 Kerala 86, 88 (FB).
18. Joint Committee of B. Group Merchants, Bombay v CIT (1963) 48 ITR 427 (Bom.)
19. Maharaja Bahadur Ram Ran Vijay Prasad Singh v Province of Bihar (1942) 10 ITR 446, 451 (Pat).
20. Thellusson v Woodford (1798) 4 Ves Jun 227 ; on appeal, (1803-13) All ER Rep 30, which led to the Thellusson Act in 1800 ; Re. Jefferies (1936) 2 All ER 626 ; Re Maber (1928) Ch. 88. The following is section 114 of the Indian Succession Act, 1925, which lays down the rule against perpetuity :

    "114 No bequest is valid whereby the vesting of the thing bequeathed may be delayed beyond the life-time of one or more persons living at the testator's death and the minority of some person who shall be in existence at the expiration of that period, and to whom if he attains full age, the thing bequeathed is to belong.

    Illustrations

    (i) A fund is bequeathed to A for his life and after his death to B for his life : and after B's death to such of the sons of B as shall first attain the age of 25. A and B survive the testator. Here the son of B who shall first attain the age of 25 may be a son born after the death of the testator ; such son may not attain 25 until more than 18 years have elapsed from the death of the longer liver of A and B ; and the vesting of the fund may thus be delayed beyond the life-time of A and B and the minority of the sons of B. The bequest after B's death is void."

For the principle on which this provision is founded, see Stanley v Leigh (1732) All ER 917, 918 :

"For the law does abhor what is called perpetuity . . . the reason of which is the mischief that would arise to the public from estates remaining for ever inalienable or untransferable from one hand to another, being a damp to industry and a prejudice to trade, to which may be added the inconvenience and distress that would be brought on families whose estates are so fettered."

21. Sardar Bahadur Indra Singh Trust v CIT (1971) 82 ITR 561 (SC).

22. K.T. Doctor v CIT (1980) 124 ITR 501 (Guj) ; CIT v Juggilal Kamlapat (1967) 63 ITR 292 (SC) ; Addl. CIT v Ram Krishna Gupta (1979) 117 ITR 218 (All).

23. Sections 7 and 9 of the Indian Trusts Act.

24. Sub-clause (b) of section 7 of the Indian Trusts Act. While a minor cannot create a testamentary trust, since he is incompetent to leave a will under section 59 of the Indian Succession Act, 1925, he can set up a trust *inter vivos*.

    In the UK a minor cannot hold land but can have an equitable interest in land. If a trust is created by him, it is voidable by him shortly after he attains majority ; Edwards v Carter (1893) AC 360, (1891-94) All ER Rep 1259. The guardian of a minor cannot create a *waqf* on his behalf : Commissioner of Waqfs, West Bengal v Mohsin in 48 WBN 252.

25. Section 8 of the Indian Trusts Act. Salary and pension are inalienable and cannot be the subjects of a trust. There can also be no transfer of the right of the beneficiary to proceed against a trustee.

26. CIT v Manilal Dhanji (1962) 44 ITR 876 (SC) ; CIT v HEH the Nizam's Supplemental and Religious Endowment Trust (1973) 89 ITR 80, 84, 85, (AP) ; Dr. A.J. Kohiyar, v CIT (1964) 51 ITR 221 (Bom).

27. Vide sections 5 and 13 of the Transfer of Property Act, 1882. Sopher v Administrator-General of Bengal 71 IA 93 : 46 Bom LR 86 (PC).

28. T.C. Hornby v E.T. Farmer AIR 1960 Cal 36 ; Sopher v Administrator-General of Bengal 71 IA 93 : 46 Bom LR 86 (PC).

29. That an unborn child can be one of the beneficiaries is assumed in several cases : Addl. CIT v Ram Krishna Gupta (1979) 117 ITR 218 (All) ; CWT v Trustees of HEH the Nizam's Family (Remainder) Wealth Trust (1977) 108 ITR 155 (SC); Trustees of Putlibai R.F. Mulla Trust v CWT (1967) 66 ITR 653. For a different view, vide Nirmala Bala Sirkar v CIT (1969) 74 ITR 268 (Cal). The ITAT, Calcutta (Special Bench) has expressed the view that where a trust provided for payment of 5 per cent of the income to a lady and for the accumulation of the balance for her unborn son for 21 years, the

trust was a valid one, not liable to tax at the maximum rate : ITO v C.L. Sadani Family Trust, ITA 2573 (Cal) of 1979, reported in *Selected Orders of ITAT* (Vol I), 1982, New Delhi : Taxman, pp. 484-93.

30. Re. Rydon (1955) Ch. 1 ; Re. Curteis (1872) LR 14. Eq. 217.

    The settlor's intention has to be established. Merger may be open to question where the settlors or/and trustees are different, or there is any variation in the terms of the trusts : Re. Campbell (1922) 1 Ch. 551 ; Re. Eykyn (1877) 6 Ch. D 115 ; Re. Marke Wood (1913) 2 Ch. 574 ; Re. Beaumont (1913) 1 Ch. 325 ; Hart (Inspector of Taxes) v Briscoe (1978) 2 WLR 832, (1978) 1 All ER 791. Where there is a disposition of a limited interest in a settlement, two settlements may result : Midland Bank Executor and Trustee Co. Ltd. v IR (1959) Ch. 277. For the effects of variation of trust arrangements with the court's approval : Re. Ball's Settlement Trusts (1968) 1 WLR 899, (1968) 2 All ER 438 ; Re. Holt's Settlement (1969) 1 Ch. 100 ; (1968) 1 All ER 470.

31. For the grounds of rescission, vide Pettit, *Equity and the Law of Trusts*, Second Ed. (1970), Butterworths, pp. 445-50 ; G.W. Keeton and L.A. Sheridan,, *The Law of Trusts*, 20th Ed. 1974, Professional Books Ltd., pp. 117-24. Also section 89 of the Indian Trusts Act.

32. Sections 11 to 30 of the Indian Trusts Act set out the duties and liabilities of trustees, sections 31 to 45 their rights and powers and sections 46 to 54 their disabilities.

33. Re. Gibbon's Trusts Ch. (1882) 30 WR 287 ; Re. Tempest (1886) 1 Ch. App 485 ; A.G. v Lady Downing (1767) Wilm. 1 ; Re. Wrightson (1908) 1 Ch. 789.

34. A disclaimer cannot be partial. The trustees must either accept the trust as a whole or decline the trusteeship : Re. Lord and Fullerton's Contract 1896 1 Ch. 228.

    The disclaimer may be oral or made evident by conduct. It may also be intimated to the court through counsel : Bingham v Clanmorris 1828 2 Moll, 253 ; Stacey v Elph 1833 1 Myl & K 195, (1824-34) All ER Rep 97 , Re. Birchall 1889 40 Ch. D 436 ; Re. Clout and Frewer's Contract 1924 2 Ch. 230, (1924) All ER Rep 798 ; Landbroke v Bleaden (1852) 16 Jur (0.S) 630 ; Foster v Dawber 1860 8 WR 646.

35. Section 46 of the Indian Trusts Act : Raja of Kovilagon v Kottayath, 7 MH CR 210 ; Vrandavan v Parshottam AIR 1927 Bom 75 ; 28 Bom LR 1481 ; Mst. Krishan Bai v Dhondo Ramchandra AIR 1924 Nag 129 ; Krishandas v Ratanbai AIR 1941 Bom 41.

36. For the consequence of failure to follow the directions of the settlor : Kerner v George 321 Ill. App. 150, 52 NE (2d) 3001 (1943). Brief details of the case are furnished by Eleanor K. Taylor, *Public Account-*

ability of Foundations and Charitable Trusts, 1953, New York : Russel Sage Foundation, p. 42.

37. Harvey v Olliver (1887) 57 LT 239 ; Bennet v Burgis (1846) 5 Hare 295 ; Re. Strahan (1856) 4 WR 536, 44 ER 402 ; Hallows v Lloyd (1888) 59 LT 603 ; 37 WR 12.

38. Learoyd v Whitely (1887) 12 App case 727, 733 ; Lucking's Will Trusts v Lucking (1967) 3 All ER 726.

39. Sections 47 and 48 of the Indian Trusts Act. On the question of delegation, Atmaram Ranchhod v Ghulam Hussain Ghulam (1972), 13 GLR 828 ; Abdul Kayum v Alibhai AIR 1963 SC 309 ; Mahadev Jew v Balkrishna Vyas AIR 1952 Cal 763 ; Marimuthu Pillai v Narayanavadian Bhagavathy 1949 TCLR 70 ; Sir Dinshah v Sir Jamshedji 2 IC 701 ; Sankaran Nambi v Devki Antherjenam AIR 1922 Mad 269 ; Parasurama Udayar v Vedaji Bhaskar Thirumal Rao Sahib AIR 1921 Mad 623 ; Gopal Sridhar Mahadev v Sahai Bhushan Sarkar AIR 1933 Cal 109 ; Sridhar v Dharamdas 3 IC 549 ; Gopalaswami v Subramania AIR 1942 Mad 397.

    On the requirement of joint action of trustees, vide Shyam Rangini Ray Chaudhurani v Ajindranath Tagore (1949) 1 ILR 165 ; Jankirama Ayyar v Nilakanta Ayyar (1954), Mad LJ 486 ; Commissioner for Hindu Religious and Charitable Endowments, Madras v A.P.S. Sethurama Pillai (1960) Mad LJ 157 ; Manmohandas v Janki Prasad AIR 1945 PC 23 ; Narendra Kumar v Atul Chandra Bandopadhyaya AIR 1918 Cal 810 ; Vedakannu v Annadana Chetram AIR 1938 Mad 982 ; Vavuttu Naicken v Venkata Sesha Aiyar AIR 1914 Mad 119 (1) ; S.V. Daniels v G.W. Friendly Trust AIR 1959 All 579 ; Board of Trustees, Shri Hindu Kanya Pathasala v Nandoo Lal 1958 Pat LR 383.

40. Bartlett v Barclay's Bank (1979) 1 All ER 139.

41. Re. Duke of Norfolk's Settlement (1978) 3 WLR 655 ; Protheroe v Protheroe (1968) 1 All ER 1111 ; Bannister v Bannister (1948) 2 All ER 133 ; Re. Macadam (1945) 2 All ER 664 ; Dale v IR (1953) 2 All ER 671.

42. Baxendale v Murphy 9 TC 76 ; Dale v IR 34 TC 468 (HL).

43. For a situation in which the profit assumes the form of a bribe, see suggestion in Lister and Co. v Stubbs (1886-90) All ER Rep 797.

44. Sections 51 and 54 of the Indian Trusts Act : Nagappa v Official Assignee AIR 1931 Mad 251 (2) ; Krishnajee v Sadasiva AIR 1927 Mad 249 ; Krishnamurthy v Chetty Punyam Devanadhaswamy Devasthanam (1957) 2 Mad LJ 411 ; Manickavasagam Chettiar v CIT (1964) 53 ITR 292 (Mad) ; CIT v Jayantilal Amratlal (1968) 67 ITR 1 (SC) ; Re. Lacey Exp. (1802) 6 Ves 625.

45. Section 34 of the Indian Trusts Act : Avoch Thevar v Chammar AIR 1956 Ker 381 ; In re. Mohamed Hashim Gazdar AIR 1945 Sind 81

(FB) ; Amina Bee v Mariam Bee AIR 1939 Rang 347 ; In re. Madras Devotom Trust Fund ILR 18 Mad 443 ; Talbot v Talbot (1967) 1 All ER 604.

46. Sections 23 and 59 of the Indian Trusts Act : Thanthi Trust v ITO (1973) 91 ITR 261, 285 (Mad) ; CIT v Gopal Krishna Kone (1965) 57 ITR 569 (Mad); Attorney General v Lady Downing (1767) Wilm 1, 97 ERI. See also Krishnaswami Pillai Kothandarama Naicker (1914) 27 MLJ 582 ; Gokuldass Jamnadass and Co. v Lakshminarasimhulu Chetty AIR 1940 Mad 920 ; Sunder Singh Malla Singh Sanatan Dharam High School Trust Indaura v Managing Committee, Sunder Singh Malla Singh Rajput High School Indaura AIR 1938 PC 73 ; Managing Shebaits of Bhukailash Debuttar Estate v WTO (1977) 106 ITR 904 (Cal) ; Rash Mohan Chatterjee and others v CED (1964) 52 ITR EDI (Cal) ; Lang v Webb (1912) 13 CLR 503 ; Clifford John Check v Commissioner of Stamp Duties of New South Wales 37 ITR ED 89.

47. Letterstedt v Broers (1894) 9 App. Cas. 371 ; (1881-5) All ER Rep 822 ; Millard v Eyre (1793) 2 Ves 94.

48. While every trust is a settlement, the term "settlement" is wider in its scope. It includes any disposition, covenant, arrangement or transfer of assets which may or may not involve a trust.

49. Cooke v Head (1972) 2 All ER 38 ; Hussey v Palmer (1972) 2 All ER 744 ; Heseltine v Heseltine (1971) 1 All ER 952 ; Bannister v Bannister (1948) 2 All ER 133 ; Boardman v Phipps (1965) 3 All ER 721 ; Industrial Development Consultants Ltd. v Cooley (1972) 2 All ER 86 ; Keech v Sandford (1558-1774) All ER Rep 230 ; Re. Diplock (1948) Ch. 465, (1948) 2 All ER 318 ; (1950) 2 All ER 1137 ; Nelson v Larholt (1947) 2 All ER 751 ; Williams-Ashman v Price and Williams (1942) 1 All ER 310 ; Belmont Finance Corporation Ltd. v Williams Furniture Ltd. (1979) 1 All ER 118.

50. Blackwell v Blackwell (1929) All ER Rep 71 ; Re. Keen's Estates (1937) 1 All ER 452 ; Re. Bateman's Will Trusts (1970) 3 All ER 817 ; Re. Stead (1900) 1 Ch. 237 ; Re. Tyler's Fund Trusts (1967) 3 All ER 389 ; Wallgrave v Tebbs (1855) 4 WR 194 ; Moss v Cooper (1861) 4 LT 790.

51. CIT v Manilal Dhanji (1962) 44 ITR 876 (SC) ; CIT v Puthiya Ponmanichintakam *Waqf* (1962) 44 ITR 172 (SC) ; CIT v Lady Ratanbai Mathuradas (1968) 67 ITR 504 (Bom) ; D.V. Arur v CIT (1945) 13 ITR 465, 480 (Bom) ; CIT v Arvind Narottam (1972) 102 ITR 232 (Guj) ; CIT v Arvind Narottam (1969) 73 ITR 490 (Guj) ; Lokmanya Tilak Jubilee National Trust Fund, In re. (1942) 10 ITR 26 (Bom) ; ITAT v Managing Trustee, Sree Radha Madho Trust (1946) 14 ITR 470 (Nag) ; Trustees of Sahebzadas of Sarf-e-khas Trust v CIT (1962) 44 ITR 332 (AP) ; V.E.A. Vairavan Chettiar v CIT (1973) 92 ITR 474 (Mad) ; Bankim Chandra Dutta v CIT (1966) 62 ITR

239 (Cal); Nirmala Bala Sarkar v CIT (1969) 74 ITR 268 (Cal); CIT v Trust Estate of Tarun Kumar Roy (1974) 94 ITR 361 (Cal).

52. CWT v Bhogilal Maganlal Shah (1968) 68 ITR 288 (Guj); CWT v Kum. Manna G. Sarabhai (1972) 86 ITR 153 (Guj); CWT v N.D. Petit (1981) 128 ITR 650 (Bom); CWT v Anarkali Sarabhai (1971) 81 ITR 375 (Guj); CWT v Ashok Kumar Ratanlal (1967) 63 ITR 133 (Guj); CWT v Master Jehangir H.C. Jehangir (1982) 137 ITR 48 (Bom).

53. Deokinandan v Murlidhar AIR 1957 SC 133; Ram Saroop Dasji v S.P. Sahi AIR 1959 SC 951; Chintamani Ghosh Trust v CWT (1971) 80 ITR 331 (All); Farman Ali Khan v Md. Raza Khan AIR 1950 All 62, 66; Trustees of Gordhandas Govindram Family Charity Trust v CWT (1968) 70 ITR 600, affirmed in 88 ITR 47 (SC); Trustees of KBMH Bhiwaniwala v CWT 1977 106 ITR 709 (Bom); CWT v J.P. Pardiwala Charity Trust (1965) 56 ITR 46 (Bom); S.K. David Sassoon v CIT (1959) 36 ITR 512 (SC); CWT v Trustees of HEH the Nizam's Supplemental and Religious Endowments Trusts (1973) 89 ITR 80 (AP); Bai Hirbai and Kesarbai Charitable and Religious Trust v CIT (1968) 68 ITR 821 (Bom); CIT v Dwarka Dheesh Temple (1951) 19 ITR 440 (All); CWT v Hyderabad Race Club (1978) 115 ITR 453 (AP); Kedia Jatiya Sahayak Sabha and Fund v CIT (1963) 49 ITR 74 (Cal); The Guru Estate v CIT (1958) 34 ITR 656, 662, 663 (Orissa), affirmed in (1963) 48 ITR 53 (SC); CIT v ASHM Sait Dharma Stapanam v Commr. of Agl. IT (1973) 91 ITR 5 (SC); In re. Smt. Charusila Dassi (1946) 14 ITR 362 (Cal); Official Trustee of West Bengal v CIT (1968) 67 ITR 218 (Cal); Sri Jyotishwari Kalimata v CIT (1946) 14 ITR 703 (Pat); Biswaranjan Bysack v CIT (1967) 66 ITR 452 (SC); Smt. Ganeshi Devi Rami Devi Charity Trust v CIT (1969) 71 ITR 696 (Cal).

A trust for religious purposes has been held to be exempt from the gift tax notwithstanding the fact that the wife of its author was given the right to reside for life in a portion of the settled property : CGT v Sri Sahaji the Chatrapati Maharajasaheb of Kolhapur (1965) 58 ITR 140 (Bom).

54. CIT v Jamal Mohammad Sahib (1941) 9 ITR 375 (Mad).

55. CIT v Smt. Kasturbai Walchand Trust (1 67) 63 ITR 656 (SC); CIT v Trustees of Sri Kikabai Premchand Trust (1967) 65 ITR 213 (Bom).

56. See 53 supra.

57. CWT v HEH The Nizam's Supplemental and Religious Endowment Trust (1973) 89 ITR 80, 83 (AP). The name may, however, be a pointer : Trustees of Gordhandas Govindram Family Charity Trust v CIT (1973) 88 ITR 47, 52 (SC).

58. Radhakanta Deb v Commissioner of Hindu Religious Endowments, Orissa AIR 1981 SC 798; T.D. Gopalan v Commissioner of Hindu

Religious Endowments, Madras AIR 1972 SC 1716 ; Goswami Shri Mahalaxmi Vahuji v Shah Ranchhoddas Kalidas AIR 1970 SC 2025 ; Amardas Mangaldas v Harmanbhai Jethabhai AIR 1942 Bom 291 ; Ramsarandas v Jairam AIR 1943 Pat 135 ; Parmanand v Nihalchand AIR 1938 PC 195 ; Laxmanrao Umajirao v Govind Rao Madho Rao AIR 1950 Nag 215 ; Prakash Chandra v Subodh Chandra AIR 1937 Cal 67 ; Bhagwandin v. Gir Harswaroop AIR 1940 PC 7 ; State of Bihar v Smt. Charusila Devi AIR 1959 SC 1002 ; Bihar Board of Religious Trust v Palat Lal AIR 1972 SC 57 ; Shri Govindlalji v State of Rajasthan AIR 1963 SC 1638 ; State of Bihar v Biseshwar Das AIR 1971 SC 2057 ; Bhagwan Sitaram Khasale v Namdeo Narayan Gore AIR 1957 Bom 168 ; Martand Pandharinath Harkare v Charity Commissioner, Bombay, 63 Bom IR 274 ; Rudrappa v Kandappa AIR 1967 Mysore 239 ; Gurcharan Prasad v Krishnanand AIR 1968 SC 1032 ; Smt. Ganeshi Devi Rami Devi Charity Trust v CIT (1969) 71 ITR 696, 706 (Cal) ; CIT v Shri Dwarka Dheesh Temple (1946) 14 ITR 440 (All) ; CIT v Shri Thakurji Lakshminathji (1947) 15 ITR 215 (All).

59. CIT v Administrator-General of Bengal (1952) 21 ITR 241 (Cal) ; Estate of Harendra Kumar Roy v CIT (1944) 12 ITR 68 (Cal) ; The Guru Estate v CIT (1958) 34 ITR 656 (Orissa), affirmed in (1963) 48 ITR 53 (SC) ; Smt. Charusila Dassi, in re. (1946) 14 ITR 362 (Cal)

60. Ramchandra Shukla v Shree Mahadeoji AIR 1970 SC 458.

61. Trust for the testator's mare : Pettingall v Pettingall (1842) 11 LJ Ch. 176.

    Trust for the testator's hounds, ponies and horses : Re. Dean (1889) 41 Ch. 652 ; 60 LT 813.

    Welfare of animals : Trustees of the Charity Fund v CIT (1959) 36 ITR 513 (SC) ; CIT v Sri Jagannath Jew (1977) 107 ITR 9 (SC) ; CIT v. Swastik Textile Trading Co. Pvt. Ltd. (1978) 113 ITR 852 (Guj) ; Satya Vijay Patel Hindu Dharmshala Trust v CIT (1972) 86 ITR 683 (Guj) ; Vallabhdas Karsondas Naha v CIT (1947) 15 ITR 32 (Bom) ; Pradhan v Bombay State Federation of Gaushalas and Pinjrapoles (1957) 59 Bom LR 890 ; Lalita Prasad v Brahmanand AIR 1953 All 449.

62. The object was held to be charitable in the following cases :

    Dwarka Nath Bysack v Burroda Prasad Bysack (1878) ILR 4 Cal 443 ; Advocate General of Bombay v Yusuf Ali Ebrahim AIR 1921, Bom 338 ; CIT v Trustees of Abdul Kadar Ebrahim (1975) 100 ITR 85 (Bom) ; Addl. CIT v A.A. Bibijiwala Trust (1975) 100 ITR 516 (Guj).

    The contrary view is expressed in the following :

    Trustees of Gordhandas Govindram Family Charity Trust v CIT (1952) 21 ITR 231 (Bom) ; Kedia Jatiya Sahayak Sabha and Fund v

CIT (1963) 49 ITR 74 (Cal) ; CIT v Karim Bros. Charity Fund (1943) 11 ITR 603 (Bom).

63. D.V. Arur v CIT Bombay (1949) 13 ITR 465 ; Taw Chew v Taw Kock AIR 1939 Rang 203 ; Trustees of Gordhandas Govindram Family Charity Trust v CIT (1952) 21 ITR 231 (Bom). The contrary view is found in Ramaswami v Aiyasami AIR 1960 Mad 467.

64. Yogiraj Charity Trust v CIT (1976) 103 ITR 777 (SC) ; CIT v Karim Bros. Charity Fund (1943) 11 ITR 603 (Bom).

65. Special provisions are made for tax exemption for approved/ recognised gratuity, provident and superannuation funds in sub-section (25) of section 10 of the Income-tax Act while proviso (iv) to section 164 (1) of the Act indicates the tax treatment of unrecognised funds. For employee welfare trusts in general, vide Baker v National Trust Co. Ltd. 2 All ER 550.

66. Re. Lokmanya Tilak Jubilee National Trust Fund (1942) 10 ITR 26 (Bom) ; Subhash Chandra Bose v Gordhandas J. Patel AIR 1940 Bom 76 ; Laxman Balwant Bhopatkar v Charity Commissioner, Bombay AIR 1962 SC 1589 ; Bonar Law Memorial Trust v IR (1933) 17 TC 508.

67. Saraswathi Ammal v Rajagopal Ammal AIR 1953 SC 491. A trust for the performance of ceremonies for the peace of the departed soul is charitable : CWT v Trustees of J.P. Pardiwala Charity Trust (1965) 58 ITR 46 (Bom).

68. Cricket Association of Bengal v CIT (1959) 37 ITR 277 (Cal). The Madras High Court has taken a different view : CIT v Ootacamund Gymkhana Club (1977) 110 ITR 392 (Mad) ; South Indian Athletic Association Ltd. v CIT (1977) 107 ITR 108 (Mad). The insertion of a specific provision for exemption of the income tax in section 10 (23) of the Income-tax Act has raised doubts on the question whether a sports association can claim to be a charitable trust under sections 11 to 13 and donations to it will qualify for deduction from the taxable income under section 80 G.

69. Bangalore Race Club Ltd. v CIT (1970) 77 ITR 435 (Mys).

70. Mohammed Ibrahim Riza v CIT AIR 1930 PC 226 ; East India Industries (Madras) Pvt. Ltd. v CIT (1967) 65 ITR 611 (SC) ; Sri Agastyar Trust v CIT (1963) 48 ITR 673 (Mad) ; In re. Probynabad Stud Farm (1936) 4 ITR 114 (Lah) ; G.K. Hosiery Factory v CIT (1971) 81 ITR 557 (All) ; CIT v Jaipur Charitable Trust (1971) 81 ITR 1 (Del) ; Dharmadeepti v CIT (1978) 114 ITR 454, 463, (SC), reversing CIT v Dharmadeepti (1975) 100 ITR 375 (FB) (Ker) ; Dharmaposhanam Co. v CIT (1978) 114 ITR 463, 471 (SC), affirming (1975) 100 ITR 351 (FB) (Ker) ; Moulana Malak v CIT, AIR 1930 PC 226, affirming AIR 1928 Nag 10 ; CIT v Ahmadabad Mill Owners' Association (1977) 106 ITR 725 (Guj). Also see CIT v Andhra Chamber of Commerce (1965) 53 ITR 722 (SC).

71. CIT v Jamal Mohammad (1941) 9 ITR 375 (FB) (Mad).

72. "Debuttar" means "belonging to the deity." A dedication of immovable property to a deity is an endowment which assumes the character of a private trust and not a "settlement" : Bhupatinath v Basanta Kumar AIR 1936 Cal 556.

73. CIT v Sri Jagannath Jew (1977) 107 ITR 9 (SC) ; Sree Sree Ishwar Sridhar Jew v Mst. Sushila Bala Dasi AIR 1954 SC 69 ; Sri Sridhar Jiu v Manindra Kumar Mitra AIR 1941 Cal 272 ; CIT v P. Krishna Warrier (1964) 53 ITR 176 (SC) ; Sappani Mohamed Mohideen v R.V. Sethu Subramania Pillai AIR 1974 SC 740. Partial dedication is not *debuttar* : there is partial dedication when the entire beneficial interest is not conveyed to the deity.

74. Kunwar Doorganath Roy v Ramchandra Sen (1876-77) 4 IA 52 (PC). For scope of revocation of a charitable trust, see CED v Bhagwandas Velji Joshi (1981) 6 Taxman 202 (Bom) ; (1983) 131 ITR 326 (Bom).

75. Commissioner, Hindu Religious Endowment v Swamiyar AIR 954 SC 282 ; Moti Das v S.P. Sahi AIR (1959) SC 942 ; Smt. Angurbala Mullick v Debabrata Mullick AIR 1951 SC 293 ; CIT v Pulin Chandra Daw (1967) 63 ITR 179 (Cal) ; Sri Sri Sridhar Jiu v ITO (1967) 63 ITR 192, 223 (Cal) ; Nirmala Bala Ghosh v Balai Chand Ghosh AIR 1965 SC 1874 ; a *shebait* is entitled to minister to the idol (deity) owning the endowed estate. Power to remove *shebaits* has been held to make a *debuttar* settlement revocable : Panchanan Dey (decd.) v CIT (1983) 142 ITR 762 (Cal).

76. In essence, a private trust, as distinct from *waqf-fisabilillah*, a public trust. A *waqf-alal-aulad* ordinarily turns into a public *waqf* when the family benefiting from it becomes extinct. Family *waqfs* have been abolished in Egypt and some other Muslim countries, vide Tahir Mahmood, *Progressive Codification of Muslim Personal Law*, p. 87, *Islamic Law in Modern India*, (1972) Delhi : The Indian Law Institute.

77. Bibi Siddique Fatima v Saiyed Mohammed Mahmood Hasan AIR 1978 SC 1362.

78. A family settlement. See S. Khalid Rashid, *Administration of Waqfs in India : Some suggestions*, pp. 237-38, *Islamic Law in Modern India* (1972), Delhi : The Indian Law Institute.

The Mussalman Waqf Validating Act of 1913 was necessitated by the decision of the Privy Council in Abdul Fata Mahomed Ishak v Rassamay Dhur Chowdhury (1894) ILR 22 Cal 619 (PC). Family settlements in which the benefits to charity or religion were either illusory or postponed idefinitely while the property so dedicated could be enjoyed from generation to genera tion by the family of the *waqif* were regarded as opposed to the rule against perpetuity in the Indian Succession Act and the Transfer of Property Act : Fazlul Rabbi

Pradhan v State of West Bengal AIR 1965 SC 1722 ; Mahant Sri Srinivas Ramanuj Das v Agl. ITO (1978) 115 ITR 153 (SC). Section 3 of the Mussalman Waqf Validating Act 1913, validates such private *waqfs* which, expressly or by implication, reserve the ultimate benefit for charitable or religious purposes. But *waqfs* in which the ultimate benefaction is uncertain will be void : Abdul Karim Adenwala v Rahimbai AIR 1946 Bom 342 ; Faqir Mohd. v Abda Khatoon AIR 1952 All 127.

79. Abadi Begum v Kaniz Zainab (1927) 54 IA 33 ; see also Mulla, *Principles of Mahomedan Law,* 18th Ed. p. 210, notes under sec. 192.
80. Mundaria v Shyam AIR 1963 Pat 93 ; Mohammad Yusuf v Shafi AIR 1934 All 1013.
81. Imdad Ali Khan v Sardar Khan AIR 1954 Orissa 15 ; Shri Ghasi v *Waqf-alal-aulad* (1969) All LJ 923.
82. A *mutawalli* is not a trustee in the technical sense. He is a procurator, superintendent or manager : CWT v Puthiya Ponmani Chintakam Waqf (1967) 63 ITR 787 (Ker) ; Vidya Varuthi Thirtha v Balusami Ayyar AIR 1922 PC 123, 128 ; Alla Rakhi v Mohammad Abdul Rahim (1933) LR 61 IA 50 ; CIT v Puthiya Ponmani Chintakam Waqf (1962) 44 ITR 172 (SC) ; CIT v Managing Trustees Nagore Durgah (1965) 57 ITR 321, 325 (SC), regarding *nattanmaigars* who manage the Durgah and *kasupangudars* who have beneficial interests ; vide Tahir Mahmood (1980) : *The Muslim Law of India,* Law Book Company, pp. 288-291 ; also, Hafiz Mohammed Zafar Ahmad v U.P. Sunni Central Board of Waqf AIR 1965 All 333 ; CED v K.A. Kader (1974) 96 ITR 289 (Mad) ; CED v Kamaluddin Fakri (1980) 124 ITR 98 (Mad).
83. Mumtaz Qadar v A.G. AIR 1946 Oudh 244.
84. Khalil Ahmed Khan v Siddiq Ahmed Khan AIR 1974 All 382.
85. Milroy v Lord (1862) 4 De G.F. & J 264 ; Ida Chambers v K.H. Chambers (1940) 2 MLJ 963.
86. CIT v Hamdard Dawakhana (1960) 39 ITR 144 (Pun) ; Amiya Krishna Khan v Debendra Lal Khan 46 CWN 865 ; Kayastha Pathasala v Mst Bhagwati AIR 1937 PC 4 ; Re. Porter 1925 All ER Rep. 179.
87. The law of charities does not allow property gifted for charitable purposes to revert to the donor or his legal heirs and successors if there is difficulty in implementing the exact purpose he had in view. The *cy pres* doctrine enables the Court to direct the application of the gift to an object as close as possible to that indicated by the donor. Sec 92(3) of the Code of Civil Procedure, 1908 incorporates the doctrine with effect from February 1, 1977 : Thanthi Trust v CIT (1981) 23 CTR (Mad) 155 ; State of U.P. v Bansidhar AIR 1974 SC 1084, 1090-1 ; Ratilal Panachand Gandhi v State of Bombay, AIR

1954 SC 388 ; Commissioner, Lucknow Division v Dy Commissioner, Pratapgarh AIR 1937 PC 240 ; In re. Ulverston & District New Hospital Building Trust (1956) 3 All ER 164.

88. The principle is that the right of sale or alienation should not be suspended for an unreasonable period. The terms of a private trust must specify its life.

89. Section 83 of the Indian Trusts Act : Sir Fazalbhoy Currimbhoy v Official Trustee AIR 1979 SC 687, 691 ; Re Vandervel's Trusts (No. 2) (1974) 1 All ER 47 ; Vandervel v IR (1967) 1 All ER 1 ; Re. Vinogradoff (1935) W.N. 68 ; Essery v Cowland (1884) 26 Ch. D. 191 ; Shephard v Cartwright (1954) 3 All ER 649 ; Gissing v Gissing (1970) 2 All ER 780 ; Pettit v Pettit (1969) 2 All ER 385 ; Smith v Cooke (1891) 40 WR 67, (1891) A.C. 317.

90. Abdul Karim v Rahimbhai AIR 1948 Bom 342, (1946) 48 Bom LR 67 ; Sattar Ismael v Hamid Sait AIR 1944 Mad 504 ; Mt. Ruqia Begum v Surajmal AIR 1936 All 404.

91. Dagdu v Bhara ILR 28 Bom 20 ; Thanthi Trust v CIT (1981) 23 CTR (Mad) 155 ; Jagadamba Charity Trust v CIT (1981) 128 ITR 377 (Del) ; Kamla Town Trust v CIT (1975) Tax LR 829 (All). *Halsbury's Laws of England*, Third ed. Vol. 26. para 1709, 920. The author cannot alter the objects of the trust : CIT v S. Ramaswami Iyer (1977) 110 ITR 364 (Mad). He cannot also change the trustees unless this power has been retained by him in the original instrument : CED v K.A. Kadar (1974) 96 ITR 289, 294 (Mad). Where a trust deed has been rectified, a decision on the revocability of the trust will depend on the rectified deed. Where, however, a tax assessment has been completed before rectification of the deed, there is no scope for amending the assessment : Smt. Durga Sundari Dey v CIT (1979) Tax LR 223 (Cal).

92. Sec. 56 of the Indian Trusts Act, 1882. Saunders v Vautier (1835-42) All ER 58. Also, Wharton v Masterman (1895-99) All ER Rep. 687 ; Dawson v Hern IR & M 606 ; Magrath v Morehead (1871) LR 12 Eq. 491; Josselyn v Josselyn (1837) 9 Sim 63; Gosling v Gosling (1859) 123 RR 107 ; Re. Lord Nunburholme (1911) 2 Ch. 510 ; Berry v Geen (1938) 2 All ER 362 ; Re. Marshal (1911-13) All ER Rep 671 ; Re. Sandeman's Will Trusts (1937) 1 All ER 368 ; Tomlinson v Glyns Executor and Trustee Co. (1970) 1 All ER 381 ; Re. Brockbank Ward (1948) 1 All ER 287; Stephenson v Barclays Bank Trust Co. Ltd. (1975) 1 All ER 625. For the Court's inherent powers to make good any want of capacity on the part of the beneficiary, vide IR v Holmden (1968) 1 All ER 148. In the UK, any variation of a trust can be effected only with the approval of the Court, under the Variation of Trusts Act, 1958, where the beneficiaries are unascertained or they include an infant or the unborn. One of the odd features of the trust law in India, as in the UK, is that the beneficiaries cannot

control the trustees, though they can end the trust or call for the conveyance of any of the trust assets to them.

93. An *obiter dictum* of Sir Montague Smith in a judgment of the Judicial committee in Kunwar Doorga Nath v Ram Chandra (1877) 2 Cal 341 ; (1876-77) 4 IA 52 that a family consensus may give a different direction to the estate of the family idol has been followed by the Calcutta High Court in Gobinda Kumar v Debendra Kumar (1907) 12 CWN 98, but this view has not been accepted by the same High Court in Chandi Charan v Dulal ILR 54 Cal 30, CWN 930; Surendra Krishna v Sri Bhuwaneswari, ILR 60 Cal 54 ; and Sukumar Bose v Abani Kumar AIR 1956 Cal 308. See paras 4.52, 4.53 and 4.54, pp. 196-198, B.K. Mukherjee on *The Hindu Law of Religious and Charitable Trusts*, Fourth ed., edited by P.B. Gajendragadkar and P.M. Bakshi, Eastern Law House, Calcutta, 1979.

94. Subsecs. (2) and (3) of sec. 11 of the Income-tax Act, 1961.

95. Subsec. (1) (bb) of sec 13, *Ibid.*

96. *Ibid.*, secs. 2 (38) and 10 (25) and Sch IV Part A for provident funds, and secs. 2 (5), 2 (6), 10 (25) (iv) and 10 (25) (iii) and Sch IV Parts C and B for gratuity and superannuation funds.

97. *Ibid.*, proviso (iv) to sec. 164 (1)

98. Walker v Reith 1906-8 F 381 ; 43 SC LR 245 ; Edwards v Roberts 19 TC 618 (CA) ; Smyth v Stretton 5 TC 36 ; IR v Parsons 13 TC 700 (CA).

99. Trust accounts under the Married Women's Property Act 1874 are also proposed to be considered separately along with employee welfare trusts, etc.

2

Private Trusts as Intermediaries in Taxation

FROM the point of view of taxation, a private trust is an intermediary between the taxpayer and the Revenue, like a company or a firm. It is like a firm, and unlike a company, in not having a juridical personality, capable of suing or being sued.[1] But, while a firm is treated as a legal entity for the limited purpose of taxation of income,[2] a trust is not. Just as the term "partnership" describes the relationship between the persons who have agreed to share the profits of a business conducted by them, a "private trust" is a convenient expression for describing a commitment for the benefit of one or more persons, and the financial arrangements made to that end. Each of the three genres appears to be specially adapted for particular purposes. Firms are in vogue in trading activities which are not widespread ; and corporations are in demand for large-scale trading and for industrial undertakings. In the past, trusts were used mostly for long-term investments in arrangements for ensuring financial security for a settlor's family, but of late, they have also become agencies for running a business, without some of the inhibitions from which partnership concerns and companies suffer.

Trusts have played a predominant part wherever tax has been levied on transfers of properties on death or *inter vivos* gifts. They have also assumed an increasingly important role in the taxation of individual income and wealth. In an ideal operation of the law, taxes are expected to be neutral as between assets held in trust and those which are held absolutely ;

and no tax advantage should be gained by anyone through recourse to an intermediary. But no country has been able to achieve this ideal. This is because the tax treatment of a trust is overlaid with practical as well as legal difficulties and it offers boundless scope for the exercise of ingenuity in securing tax reduction.

As pointed out in Chapter 1, there may be circumstances in which trusts are constituted without any intention to avoid tax. For instance, a trust is probably the safest method for ensuring that heirs who are mentally unsound or retarded, or suffering from serious physical disabilities, are properly looked after during their lifetime. It may also satisfactorily serve minor children, or a spouse who does not have adequate experience in the management of financial affairs. It may be better than an outright gift in the case of a dependant in whose judgment one has no confidence but about whose welfare one is anxious[3]. Experience has shown that barring such special cases, a private trust is resorted to primarily for artificial fragmentation of income and wealth. It is human nature to make all possible efforts to preserve one's fortune intact for successive generations. The paramount consideration in setting up a private trust is to provide for people in whom one is intimately interested, as long as possible, at the least cost in terms of tax liability.

A trust does not come into existence spontaneously, by the adoption of a standard form of instrument. It is designed to suit the requirements of the individual cases and, in the process, provides ample opportunity for tax manoeuvres. For this reason, it is sustained less by statute than by case law. Since a family settlement affects comparatively few people, it enjoys a sheltered privacy without any legal compulsion, as in the case of a company, to file or register any document with any prescribed authority[4].

NOTES

1. ". . . although, for purposes of the Income-tax Act, a firm has certain attributes simulative of personality, we have to take it that a partnership is *not a person* but a plurality of persons." CIT v C.M. Chidambaram Pillai (1977) 106 ITR 292 at p. 300 (SC).

2. A "person" has been defined in Section 2 (31) of the Income-tax Act to include (i) an individual, (ii) a Hindu undivided family, (iii) a company, (iv) a firm, (v) an association of persons or a body of individuals, whether incorporated or not, (vi) a local authority and (vii) every artificial juridical person, not falling within any of the preceding categories. Sub-section (7) of section 2 states that an "assessee" means "a person by whom any tax or any other sum of money is payable under this Act". Section 4 provides for levy of tax "in respect of the total income of the previous year or previous years, as the case may be, of every person." Section 6 (2) lays down that "a Hindu undivided family, firm or other association of persons is said to be resident in India in any previous year except where during that year the control and management of its affairs is situated wholly outside India."
3. Income from property settled on trust was not includible in the total income of the settlor under the Indian Income-tax Act, 1922, even if the settlor appointed himself as the trustee with full powers to lease out, mortgage or encumber the properties and he was not accountable to the other trustees for his dealings : CIT v Brojendranath Kundu (1977) 110 ITR 336 (Cal) ; CIT v Jayantilal Amritlal (1968) 67 ITR 1 (SC).
4. All charitable and religious trusts and institutions seeking tax exemption under sections 11 and 12 of the Income-tax Act should register themselves with the concerned Commissioners of Income-tax under section 12A of the Act. Private trusts are not required to do so. Similarly, some of the States have legislation for registering religious and charitable trusts or only Hindu religious trusts and also for supervision of their working : The Bombay Public Trusts Act 1950 (applied to Gujarat also), the Rajasthan Public Trusts Act 1959, the Madhya Pradesh Public Trusts Act 1951, the Madras Hindu Religious and Charitable Endowments Act 1959, the Bihar Hindu Religious Trusts Act 1950, the Orissa Hindu Religious Endowments Act 1969, and the Travancore-Cochin Hindu Religious Institutions Act, 1950. The Waqf Act 1954 provides for the registration and survey of public *waqfs* in the entire country (except Jammu & Kashmir). The Indian Trusts Act, which covers different aspects of the creation and operation of private trusts, does not, however, have any similar provision.

3

Legislative History

Transfers of Income and Revocable Transfers of Assets

IT is not uncommon for a person to transfer the income from a property to a dependant for the beneficiary's or his own lifetime, without divesting himself of the ownership of the property. Where the property is also transferred, the duration of the transfer and the rights, if any, in the property that the transferor has reserved for himself assume importance. For this purpose, a transfer includes a trust, settlement,[1] covenant, agreement or arrangement.

Legislative efforts were directed in the first instance only against (a) transfers of income without transfer of assets and (b) revocable transfers of assets. Mere transfer of income without transfer of the asset from which the income arose would not free one from the liability to pay the income tax. The income continued to be included in the transferor's total income[2]. A revocable transfer of property did not also relieve the transferor of tax liability in respect of it.[3] Even a trust which was charitable could not escape the tax, if it was revocable.[4] A transfer is not taken to be revocable if it is operative during the lifetime of the beneficiary or transferee, without any scope for the exercise of any powers over it by the transferor[5]. It is deemed to be revocable only if—

i. it contains any provision for the retransfer directly or indirectly of the whole or any part of the income or assets to the transferor,[6] or
ii. it gives the tranferor a right to reassume power directly or indirectly over the whole or any part of the income or assets.[7]

These provisions led to considerable litigation. Their ambit has been examined in great detail in several court judgments[8]. It has been clarified, for instance , that assignment of shares in partnership concerns, followed by the declaration of the trustees that they are partners in the firms in question in a representative capacity may constitute an effective transfer of not merely income but the source of the income[9]. A transfer is not considered revocable merely because the trustees have acted in derogation or breach of the deed of transfer or even if the trust deed empowers the trustees to invest the trust property as they, in their discretion, think fit, despite the restrictions imposed by the Indian Trusts Act[10]. Provisions in the trust deed forfeiting the beneficiaries' interests in the event of their insolvency[11] or limiting the rights of the beneficiaries to question certain acts of the trustees and preventing frivolous litigation will not have the effect of giving the settlor a right to reassume power directly or indirectly over the income or assets[12]. Even if the author of a trust enjoys any benefit in the trust, the trust will not be deemed to be revocable unless the benefit has been reserved for him or he is permitted to enjoy it by the trust deed[13]. Where income from property settled on trust is included in the income of another person but the tax attributable to the income is proposed to be recovered from the trustees or the beneficiary, due notice will have to be given to them and appropriate action taken only after ascertaining their points of view[14]. A trust that is revocable or deemed to be revocable is not non-existent : a legal fiction may cause its income or wealth to be tagged to its author's, but not void it.[15]

Equivalence in Tax Liability Between Trustees and Beneficiaries—Irrevocable Trusts

If there was a transfer of assets which was not revocable, then the transferor himself was not embarrassed with the liability to pay the tax on the income from the assets, except in certain circumstances. The intention in India, as in England, has been that beneficiaries should be directly assessed to tax where they are *sui juris*, and in possession and control of the trust income. However, income is generally taxed where it is

found, as a matter of expediency[16]. The Revenue has gone to the trustee where there is a trust for accumulation of income against a contingency or for capital expenditure and no one has been specifically designated to receive the income in a particular year. The trustee has also been taxed where he is running a business in the interest of the beneficiaries : it is easier to arrive at the income of the trust on the basis of the books maintained for it than determine it in the hands of the beneficiaries who may be able to throw little light on the details needed for computation of their income. The liability of a trustee does not, however, preclude direct access to the beneficiary.[17]

Till the forties, a trustee was taxed as a representative assessee, on the income which he received on behalf of the beneficiaries. The Income-tax Amendment Act, 1939, altered the basis and made him liable for tax on the income that he was entitled to receive for their benefit.

There were two simple provisions for dealing with private trusts in the Income-tax Act, to start with. One related to a trustee appointed under a duly executed trust instrument. The other pertained to the Court of Wards, the Administrator General, the Official Trustee, or any person appointed by or under any order of a court. All of them were liable to tax on the income received by them on behalf of the beneficiaries concerned. The tax was to be raised on a trustee in the same manner and to the same extent as it would have been, had the assessment been made directly on the beneficiary.[18] The trust was not liable to pay tax on the entire income passing through it, as a unit.[19] If a beneficiary had an additional source of income apart from the trust, it was open to the Revenue to proceed against him and assess his entire income including the income from the trust directly in his hands, instead of assessing the income from the trust in the trustee's hands. Discretion to withhold distribution of income in a particular year would not affect the beneficiary's right to be assessed on the basis of his individual share, if it had been specified in the trust instrument.[20] Where only a part of the income was taxable, the beneficiary's share was chargeable *pro tanto*. These special provisions were taken to constitute an

enabling machinery which imposed no statutory obligation on the Revenue to proceed only against the trustee or only against the beneficiary : the Revenue could proceed against either of them.[21]

At the same time, it was conceded by the revenue authorities, that the option did not imply that the same income could be assessed twice, in the hands of both the trustee and the beneficiary.[22] By some process of ratiocination, it was concluded that once the trustee was taxed on the beneficiary's income, it would not be proper for the Revenue to reconsider whether it would not be better for it to subject the beneficiary to tax directly on his total income, including the income derived by him from the specific trust. The view was also taken that it would not be correct even to apply the average rate of tax on such total income to the beneficiary's other income, where the trustee had already been assessed to tax on the trust income.[23]

Income Tax on Discretionary Trusts

Discretionary trusts, i.e., trusts in which the beneficiaries were uncertain or their shares were not defined, were treated on a different footing : they were subjected to the income tax but not super-tax at the maximum rate.[24] The income of a discretionary trust bore tax as if it was the income of an association of persons, if none of its beneficiaries had any other income chargeable to tax or was an artificial juridical person like a Hindu idol ; and any amount paid out of it to a beneficiary was not assessable in his hands.[25] A trust was held to be specific and not discretionary if a beneficiary was entitled to recover a lump sum payment from it ; the share was taken to be indeterminate, and the trust discretionary, if there were any fluctuating additions to the amount.[26] A mere right to be maintained or educated could not be construed as a definite share in determining whether a trust was discretionary.[27]

When the Income-tax Act was overhauled in 1961, the opportunity to rationalise the trust provisions in keeping with the trust practices and development was missed. The only modification made in the Income-tax Act in 1961 related to the

provision for the charge of tax at the maximum rate from the trustees if the beneficiaries were unknown or their respective shares were not fixed.[28] This was substituted by a milder provision in section 164 allowing the assessment of trustees as a single unit consisting of an "association of persons," or when payments had actually been received by any of the beneficiaries, the levy of tax applicable to such individual beneficiaries, whichever course was more advantageous to the Revenue.[29] Where a beneficiary was directly assessed on a part of the income, the trustees could be assessed on the balance at the rate appropriate to that balance.[30] If the beneficiaries were not known or their shares were indeterminate in only a part of the trust, it was only that part that called for the differential treatment.[31] Variations in the class of beneficiaries in different years would not subject a trust to the provisions of section 164, if the beneficiaries and their shares were ascertainable in the particular year under consideration[32]. Income, which was notional or which was receivable but not received could not be taken to be income in which the shares of the beneficiaries were indeterminate or unknown.[33]

It is common knowledge that there was an upsurge of discretionary *inter vivos* trusts in the early sixties and that the incidence of tax on the income from the settled property was maintained at a low level by

a. splitting the income among multiple trusts and,

b. merely giving a class or list of eligible beneficiaries without quantifying the income apportionable among them.

Since some of the persons qualifying for benefits from the trusts were in the high income brackets and would have to pay heavy taxes if their shares had been specific, schemes were usually designed to regulate the distribution of trust income with an eye on the tax dues of the beneficiaries. With a view to discouraging this technique, the Finance Act, 1970, revised the charge to a flat rate of 65 per cent or the rate which would be appropriate to an "association of persons" with the same income, whichever might fetch more revenue. Legacies in

wills and trusts in which all the beneficiaries were persons with small income were, however, protected.

The amendment to the Income-tax Act in 1970 might have circumscribed the scope for discretionary trusts in the cases of taxpayers in the middle income groups, but the rage was unabated in the bigger cases. The maximum rate of tax was 72 per cent in 1980 and one could get away with a lower rate, *viz.*, 65 per cent or the marginal rate of an association of persons by setting up a trust.

The special dispensation that the rate of 65 per cent would not apply where none of the beneficiaries of a trust had other income chargeable to the income tax was also misused in some cases by spawning a large number of discretionary trusts, the beneficiaries of which did not have any other income chargeable to the income tax. Similarly, the exclusion of a discretionary trust created under a will from the purview of the provision regarding the flat rate of 65 per cent was made with a view to relieving hardship in genuine cases where testamentary benefits were sought to be conferred on near relations. Experience showed, however, that this legislative intention was also defeated by a testator's creating many discretionary trusts by will.

It was noticed further that in some cases discretion was given to the trustees to decide the allocation of income every year. This enabled the trustees to convert a discretionary trust into a specific trust whenever it suited the beneficiaries tax-wise.

Since the amendment in 1970 did not, therefore, prove to be a disincentive to the incessant resort to discretionary trusts, the following amendments were made in 1980 :

i. A discretionary trust would be liable to tax at the maximum marginal rate of income tax on its entire income. The maximum rate, including surcharge, was 72 per cent in 1980-81 and 66 per cent thereafter.

ii. The maximum marginal rate would be invoked if any beneficiaries had any income chargeable to tax or if any of them was also a beneficiary under any other private trust. In this context, "income chargeable to tax" would mean total income above the exemption limit for the relevant year.

iii. The concession for testamentary trusts would be restricted to cases where a person had made only one trust by will.

iv. Income of a trust set up before March 1, 1970 could be assessed as if it were the income of an association of persons, if it had been created *bona fide* exclusively for the benefit of the relatives of the settlor, or where the settlor was a Hindu undivided family, exclusively for the benefit of the members of such family, in circumstances where such relatives or members were mainly dependent on the settlor for their support and maintenance.[34]

v. The annual conversion of a discretionary trust into a specific trust has been prevented by an amendment confining the relief available to specific trusts to cases in which the individual shares of the persons on whose behalf or for whose benefit any income is receivable are stated in the instrument of trust or the *waqf*-deed or the order of the court as the case may be, and are ascertainable as such on the date of such instrument, deed or order. As a result of this amendment, a trust under which the trustee can decide the allocation of the income every year will be regarded as no more than a revised version of the discretionary trust and taxed accordingly. Since there is no provision of law under which the trustees can vary the terms of the original trust-deed,[35] old trusts will be badly hit by this requirement.

Income Tax on Oral Trusts

The Revenue had all the time thought only in terms of discretionary trusts based on elaborately drawn instruments. The constraints to which the periodical amendments subjected such discretionary trusts did curb their growth, but the Revenue had not bargained for oral discretionary trusts. The Government observed that certain taxpayers managed to reduce their income tax and wealth tax liability, by creating a number of oral trusts, each having a small corpus.[36] The law was, therefore, amended again in 1981 to subject oral trusts to the

maximum marginal rate of income tax.[37] Opportunity has, however, been given to the trustee of an oral trust to file a statement in writing before the revenue authorities, setting out the purpose of the trust and particulars as to the trustees, the beneficiaries, and the trust property. The trustee of any parol trust that may be set up in future will have to file such a statement within three months of its coming into existence. If the trust is a specific one, it will receive the same treatment after filing such a statement as any specific trust declared by a duly executed instrument in writing. If it is discretionary, the maximum marginal rate of tax will be charged though under a different provision of the law.[38]

The Wealth Tax and Trusts

The Wealth- and Gift-tax Acts were enacted not as sources of revenue but rather as components of an integrated system of taxation, including taxation of income, wealth, gifts and expenditure, to countervail tax evasion.[39] The base for the wealth tax is narrow. It excludes, among other things, agricultural land and buildings in the vicinity of the land, used or occupied by the cultivators. It excludes also rights to annuities which are not commutable. Only annuities that have been purchased by the taxpayer or purchased by any one else in pursuance of a contract with him are to be included in his net wealth. Similarly, interest in property where such interest is available for less than six years from the date on which it vests in the taxpayer is not to be taken as a part of his net wealth. As regards trusts, the procedural and also some of the substantive provisions of the Wealth-tax Act correspond broadly to those of the Income-tax Act. The trustees of a trust constitute an assessable unit under the Wealth-tax Act : the word "individual" in section 3 of that Act includes individuals or more than one beneficiary.[40] The right of a settlor to have the net income of a trust applied for his support and maintenance is an interest in the trust property that has to be valued and included in the settlor's wealth.[41] Assets transferred to trusts or *waqf* for the benefit of the spouse or a minor child are to be included in the transferor's wealth.[42] Under the provision as originally enacted, only assets transferred for the immediate

benefit of the spouse or minor child could be added to the transferor's wealth, but section 4(i)(a)(iii) was amended by the Wealth-tax (Amendment) Act, 1964, to reach also assets offering deferred benefits.[43] Trust property utilised for residential purposes by a beneficiary will qualify for exemption upto the prescribed limit.[44] Where several beneficiaries occupy the same residential house held under trust, each will be eligible for a separate deduction upto the ceiling.[45] The value of the interest of a beneficiary in a trust is includible in his wealth.[46] Life-tenancy is taken to represent the right to the income as well as the underlying property for the beneficiary's life-time and subjected accordingly to both the income and wealth taxes. It is a wasting asset : while its value for the life-tenant diminishes from year to year, the value of the remainderman's interest goes up proportionately. A deferred benefit has to be discounted to arrive at the present market value of the beneficiary's interest. The beneficiary can be taxed directly ; and he will be entitled to all the exemptions conferred to a taxpayer by Section 5.[47] Alternatively, the trustees can be taxed as representative assessees, but their liability will be worked out on the same line as the beneficiary's, and cannot be wider than that liability.[48] The option to make the assessment in the hands of the beneficiaries or the trustees is not, however, available, to the revenue authorities when the shares of the beneficiaries are indeterminate or unknown.[49] Where the beneficiaries are not identifiable or their shares are unascertainable on the valuation date, there is a special provision in sub-section (4) of section 21 of the Wealth-tax Act for levying tax at a higher rate on the wealth about which there is such uncertainty.[50] Subsequent developments, like the death of one of the beneficiaries or increase in the number of beneficiaries by a birth, cannot affect the position as on the valuation date for any particular assessment[51]. The possibility that the shares of the remaindermen may be altered by later events is immaterial.[52]

When the Income-tax Act was amended from time to time to discourage discretionary trusts meant to avoid the income tax, there were parallel changes in the Wealth-tax Act also. Adverse court judgements led to the following amendments to make the

legislative intention clear :

i. In a case where the aggregate value of the interests of the beneficiaries falls short of the value of the assets held in trust, the trustees shall, in addition to the wealth tax payable on the basis of the value of the benefits derived by the beneficiaries, be chargeable to the wealth tax in respect of the difference between the value of the corpus of the property as a whole and the aggregate of the values of the interests of the beneficiaries. This has been necessitated by the failure of the wealth tax to reach the trust property in full, when it is proportioned to the individual beneficiary's quantum of ownership.[53] The tax will be levied at the flat rate of three per cent or at the appropriate rate of wealth tax which will be applicable if such excess value were the net wealth of an ordinarily resident Indian citizen, whichever course is beneficial to the revenue. There will be no tax-exempt threshold in either case.

ii. The flat rate of three per cent or the appropriate rate of wealth tax applicable to an individual, whichever results in larger revenue, has also to be invoked in cases where the beneficiaries are not identifiable or their entitlements are not ascertainable with reference to the trust instrument or the court order creating the trusts.[54] Creation of more than one discretionary trust by testament will also bring the trust in question within the mischief of the amended provision.

iii. Where a trust provided that the trust property could be sold (a) only to the beneficiaries and (b) at a price fixed in the trust-deed, the market value of the property, for wealth tax purposes, was being pegged to the amount specified in the trust-deed, however arbitrary, unrealistic, low or out-of-date it might be. Such a stipulation enabled avoidance of wealth tax on the true market value of the trust property. This has been countered by a new provision to the effect that such restrictive covenants, which create any kind of artificial disability, will be ignored for purposes of determining the value chargeable to tax.

Oral trusts came for a drubbing in the Wealth-tax Act also when a special provision regarding them was made in the Income-tax Act. With effect from April 1, 1981, they are liable to the wealth tax at the rate of three per cent or the rate applicable to an ordinarily resident Indian citizen, whichever course is more beneficial to the Revenue.[55]

Gift Tax and Trusts

As for the gift tax, it is confined to *inter vivos* gifts,[56] since the estate duty regime covers gifts *mortis causa* and also all properties gifted by will. A gift has been defined to mean a transfer of movable or immovable property without consideration and includes the creation of a trust in property. When property is transferred to a trustee and the beneficiaries of the trust have no legal right to the trust fund, it does not mean that no interest has been created in favour of the beneficiaries : the trust is a gift to the extent of the benefits it provides to one or more persons.[57] The execution of a settlement reserving for the settlor the limited right to enjoy the profits of a business for his lifetime and transferring his proprietary interests in the business to his grandchildren subject to this reservation would be a gift *inter vivos*.[58] A gift of a movable property, including a beneficial interest in a trust situated outside India will not be chargeable to the gift tax unless the donor is an Indian citizen and has also been ordinarily resident in India.[59] Gift tax rates are more steeply graduated than the estate duty upto a value of Rs. 350,000, the rates being identical above that value upto Rs. 15 lakh. The maximum rate of gift tax is 75 per cent, and of the estate duty 85 per cent, above Rs. 20 lakh. The gift tax paid on assets included in the computation of the estate of the deceased is deducted from the estate duty, to avoid double taxation of the value of the same asset.[60]

There is no "gift" when a settlor reserves to himself the power of revocation of a trust without any limit as to the time of its exercise.[61] No gift tax is exigible on the natural extinguishment of a beneficiary's interest, but there is no reason why deliberate acceleration of a successor's or remainderman's interest by its premature termination should escape

tax.[62] It was pointed out by one of the courts that no gift tax would be attracted under the existing provisions of the Gift-tax Act, where a beneficiary of a trust exercised the power of appointment conferred on him under a trust-deed and released his life-interest in the trust in favour of other persons.[63] The definition of the expression "transfer of property" in the Act has been amended to make it clear that the exercise of a power of appointment will amount to a transfer, irrespective of whether such power is general or special or subject to any restriction as to the persons in whose favour the appointment may be made. It has also been clarified that where a person who has an interest in property as a tenant for a term or for life, or a remainderman, surrenders his interest in the property or otherwise allows his interest to be terminated without consideration, or for a consideration which is not adequate, the value in excess of the consideration received shall be deemed to be a gift made by such person.[64]

Present Position in Regard to the Three Taxes

On a review of the development of the provisions dealing with trusts in the Income-tax, the Wealth-tax and Gift-tax Acts, the following is found to be the prevalent regime :

i. The direct taxes Acts in India do not have any provisions for taxing a trust as such. They do not even attempt to define a trust or distinguish between a private trust and a public trust, though they have their own definitions of a partnership, a company, a company in which the public are substantially interested, etc. The term "trustee" is used not in the strict sense which it carries in the English law but in a wider sense.

ii. Though a trust may be constituted even without an instrument in writing, the Income-tax and Wealth-tax Acts accord a preferential treatment to trusts supported by such instruments.[65] While the opening of an account in one's books and his disclaiming benefit from that account may serve as evidence of his intention to set up a trust, a trust will not be perfected till the trust fund or property is handed over to the trustees.[66]

iii. "Property" is a term of the widest import and it signifies every possible interest which a person can acquire, hold and enjoy.[67] A settlor can carve out of a property as many time-enjoyment interests and distribute the slices to as many persons as he desires. It is possible to transfer a property to a trust *minus* a particular right or subject to an existing liability.[68] There is no bar to beneficiaries being companies or persons who are not competent in law to enter into a contract, e.g., minors or individuals who are insane. The taxation laws do not seek to supersede or nullify any of the provisions of the trust law and practices.[69] They try merely to ensure that tax is not avoided through the provisions[70].

iv. The income of trusts can be taxed to one of three possible taxpayers : (a) the founder of the trust, (b) the trustee and (c) one or more beneficiaries. Ordinarily, the author of a trust cannot be assessed on the trust income if the trust is valid and effective in law, unless there is a statutory provision requiring its aggregation with his income or deeming it to be his.[71] Where a founder retains substantial dominion and control over any part of the income and property of the trust even during the life-time of the beneficiary, he is deemed for tax purposes, to continue to be its owner. In such cases, the grantor is liable to tax on the income of the trust that is at his command, whether he actually enjoys it or not.[72] The settlor will be chargeable to tax in respect of the entire income and wealth of the trust created by him even if he can assume indirect power over a portion of the income or wealth.[73] Similarly, when a trust fails, the income belongs to the settlor or his legal heirs and representatives in the resulting trust ; and they will be taxable accordingly.[74] In all the other cases the income derived through the trust is assessed to tax in the hands of either the fiduciaries or the beneficiaries.[75] Collecting the tax from a fiduciary is easier than proceeding against a beneficiary, for it is only when the latter can enforce

payment of an amount that it can be treated as his income.

v. Once a valid trust has been created and the founder has divested himself of the trust properties, his subsequent conduct cannot result in the defeasance of the trust.[76] While reservation of any power to dispose of trust property is equivalent to retention of ownership and the disponer will not therefore be relieved of his tax liability for the settled income and wealth, the mere fact that the guiding mind and will behind the trust is his and that the trustees are susceptible to his influence cannot provoke any action against him by the Revenue.[77] If he is not legally competent to redesignate the beneficiaries or redirect the flow of income or revoke the trust, any intermeddling by him may make him liable for action for breach of trust but will not vacate the trust or warrant the inclusion of the value of the trust assets in the estate of the settlor on his death.[78] Where the founder of a trust disposes of a settled property while he is not competent to do so or his legal heirs avoid giving effect to the direction in his will for utilising the income from a specified property for charitable purposes or his heirs dispose of the property or the trustees have not applied the trust funds to the object specified in the trust-deed, there is nothing that the revenue authorities can do in the matter. It will be a case of violation of the trust law for which remedial action lies elsewhere.[79] Similarly, if the trustees were to advance money to themselves, despite the clear prohibition under section 54 of the Trusts Act, they would be committing a breach of the law.[80] A trust is not voided if a trustee exceeds his powers under the deed and diverts the trust income to purposes other than those laid down in the deed. However, the revenue authorities may take due notice of such deviations in the relevant tax assessments of the trustees or the beneficiaries.

vi. The income and wealth of an individual will include, for tax purposes, the income and the value of

properties settled in trust without "adequate consideration" for the benefit of the spouse[81] or a minor child (not being a married daughter or an illegitimate child or a foster child).[82] The income may not be received in species : its notional value will be aggregated with the income of the transferor even if it is no more than the advantage of occupation of a house.[83]

It is doubtful, however, whether the unilateral release or renunciation of life-interest by a beneficiary will amount to transfer of an asset and whether the accelerated income of the remaindermen who happen to be minors can be included in the income of the person entitled to the life-interest, if he is a parent of the remaindermen,[84] despite the definition of a "transfer" in section 2(47) of the Income-tax Act to include relinquishment of an asset or extinguishment of a right therein. But assignment of life-interest will fall within the sweep of the definition.[85]

Assessment of the income in the hands of the spouse or minor children will not affect the validity of the inclusion of the trust income in the hands of the settlor,[86] unless the asset from which the income has been derived was transferred to the trust for adequate consideration. However, if the income is taxed to the settlor, it cannot again be considered in the assessment of the spouse or minor children or the trustees.[87] Natural love and affection would not be "adequate consideration"[88] for a spouse trust or for a settlement in trust for minor children. It is also open to question whether every individual has a legal obligation to maintain and educate his or her minor children and whether a court decree requiring payment to them of a part of his or her income or approving a settlement for this purpose will result in the exclusion of that part of the income and the value of the settled assets from the computation of the individual's income and wealth.[89]

Aggregation of income or wealth cannot be averted merely by deferment of enjoyment of the benefit if the beneficiary is entitled to claim it immediately

and it has already accrued or become available.[90] When only a part of the income of a trust is earmarked for the benefit of the spouse or minor child, the part so reserved will alone be added to the income of the transferor.[91] But if no income accrues in favour of either of them and no other benefit is derived by them, the aggregation provisions are not obviously attracted.[92]

vii. When the minor child of a taxpayer is a beneficiary under a trust and the trustee is a partner in a firm on behalf of the trust, the income derived by the trust from the partnership business will be includible in the hands of the taxpayer whether it is accumulated or paid to the child and whether the taxpayer is also a partner in that firm or not.[93] If the spouse of the taxpayer is a beneficiary, the income of the trust from the firm will be clubbed with the taxpayer's income irrespective of whether the spouse is entitled to the income immediately or it is accumulated in terms of the trust-deed, only if the taxpayer is also a partner in the same firm.[94]

viii. The tax liability of a trustee is a vicarious one[95] where a link between the beneficiaries and the income of the trust is established. It is co-extensive with the tax liability of the beneficiaries.[96] But where a trust has income that is not distributed to the beneficiaries, the trustee has additional tax liability independent of what the beneficiaries may receive.[97] As many assessments may be made on him as there are beneficiaries. His "status", i.e., whether it is that of an individual or a Hindu undivided family or a limited company, is taken as that of the beneficiary for the purpose of working out the latter's tax liability for which he is accountable in his representative capacity. That will be the position even if the trustee happens to be a bank or a company providing trusteeship services.[98] A single order may be passed by the assessing officer, as a matter of administrative convenience, but the order will have to compute the income of each beneficiary

and determine the tax payable for him or on his behalf, separately.

Where the beneficiaries are unknown or their shares are indeterminate, the entire trust income is assessable in the hands of the trustee in the status of an association of persons or a body of individuals.[99]

The taxes cover the chain of interests held in trust, as long as they last. When eventually the remainderman or reversioner gets the absolute interest in the property, the taxes turn to him and stop chasing the trustee.

ix. The nature of a beneficiary's interest, i.e., whether it is the bare chance of a relation in a legacy or a vested interest, can be ascertained only with reference to the terms of the instrument. A person with a contingent interest in a trust does not become a beneficiary till the contingency occurs ; there is only a chance of his being able to enjoy the benefit. Even when the interests of the beneficiaries are vested, their respective shares may be indeterminate.[100] The intentions of the founder of a trust must be manifest from the words used in the instrument.[101] The interest granted to a beneficiary under a settlement or will should be held to be vested unless a condition precedent to the vesting is expressed clearly. Where a settlement provides that the corpus should be given absolutely to the beneficiary if alive on a particular date and that the intermediate income should be applied for his benefit and the beneficiary has also been given the power of appointment to dispose of the corpus, the beneficiary's interest is not contingent but vested.[102]

x. Where the income of a beneficiary has been charged to tax in the hands of the trustees, the alternative course of directly taxing the beneficiary will not be available,[103] even if two different officers deal with the cases of the trust and the beneficiary. The choice between the two methods is not required to be made only at the time of the assessment of the trustees or only by the officer assessing the trustees ;[104] it may also be made

by the officer dealing with the case of the beneficiary while making the beneficiary's assessment. While assessment of the same income in the hands of the trustees and the beneficiary is not possible, there is no bar to charging the trustees to tax on income other than that which has borne tax in the hands of the beneficiary. The liability of the beneficiary is confined to what he receives while that of the trustees is independent of it.[105]

xi. A discretionary trust is one in which the trustees can apply its income and capital as they will and the beneficiary in the field of choice has no more than a hope that he may attract their favourable notice.[106] A trust will not cease to be discretionary if the trustees distribute specific amounts in the exercise of their discretion.[107] A beneficiary is entitled to demand that money may be paid over to him only when the trustees have exercised their discretion in his favour.[108]

But if the beneficiaries and their shares are specified, the possibility of a change in the beneficiaries in the event of any development in future will not make any difference : the trust is "specific" for the present.[109]

Discretionary trusts, whether oral or supported by an instrument are, with certain exceptions,[110] being subjected to the income tax at the maximum rate applicable to an individual and the wealth tax at a relatively high rate; discretionary disbursements cannot be treated as gifts to the beneficiaries merely because they are not obligatory. In computing the income, no allowance will be made for a tax-free slice of investment income, as in the case of an individual or a Hindu undivided family (section 80L of the Income-tax Act) ; there will not even be a tax-exempt threshold. Similarly, amounts which are excluded in arriving at the net wealth of an individual or a Hindu undivided family under sub-section (1) of section 5 of the Wealth-tax Act will not be so excluded in the assessment of the trustees of a discretionary trust in terms of explanation 2 to sub-section 4 of section 21

of the Wealth-tax Act.

In the case of a discretionary trust the revenue authorities do not have the option of going to the beneficiary under section 21(2). They have to assess the trustees to tax.[111]

xii. The surrender of interest by a prior beneficiary accelerates the interest of the subsequent beneficiary. A settlement does not become "discretionary" if the beneficiaries and their respective shares are specifically determinable at any point of time, after taking such relinquishment of interest into account.[112] But no one can have any interest or estate at law or in equity, contingent or other, in the property of a living person to which he hopes to succeed as heir at law or next of kin of such living person.[113] A married woman cannot also deprive herself, during the subsistence of her marriage, of her beneficial interest in property which is transferred or bequeathed for her benefit [114]

xiii. The character of the income in a beneficiary's hands will not be altered by its being derived through a trust. The income of each beneficiary in a trust will partake of the nature of the income of the trust itself, unless the trust-deed has allocated to him income from particular assets or sources. For example, if the trust has income from property, interest on securities, business or income from other sources, including dividends, the beneficiary's share will be composed of proportionate income falling under the same heads.[115] Likewise, if a house belonging to a trust is used by a beneficiary as his residence the property will be eligible for exemption from the wealth tax in terms of section 5(1) (iv) of the Wealth-tax Act.[116]

xiv. A trust is entitled to maintain its books either on the cash or the mercantile basis and establish an accounting year of its choice, which it cannot subsequently alter except on such conditions as the revenue authorities may lay down. The beneficiary will have to declare his income from a trust in the same manner as he returns his income from other sources, say, a

partnership concern, for which he does not have to keep day-to-day records. There is, however, a difference between a share in a firm and interest in a trust in the matter of accounting year. The accounting year of a firm is also the partner's accounting year, but there is no similar provision for a trust. All the income due to or actually received by a beneficiary in the financial year immediately preceding the assessment year is liable to be included in his total income. The income of a trust will have to be computed for tax purposes as if it were the income of a taxpayer who is an individual or an association of persons.[117] The entire trust income will be liable to tax without any deduction for the administration charges incurred by the trust.[118] All expenses not incurred for earning the trust income, e.g., interest on money borrowed for the beneficiary's personal purposes, will also be inadmissible.[119]

If the trust is a specific one, with several beneficiaries with distinct shares in the income and if the trustees are assessed to tax in their representative capacity, the tax liability will be the aggregate of (a) the liability of the beneficiaries on the income to which they are entitled and (b) the trustees' direct liability on the undistributed income, including the amount of income spent on the administrative expenses, etc., which are not deductible from the trust income.

xv. Where the income from a property is alone held for charitable or religious purposes and not the property itself, exemption from the income tax is not available. If the property consists of a business run by a firm, the income will be assessable to tax in the hands of the firm.[120]

xvi. Sums spent on religious or charitable purposes will not be exempt from tax if the trust income does not enure for the benefit of the public.[121] When the claim of a trust to be a public charitable trust is found untenable, the outcome may be a "resulting trust" in favour of the settlor.[122] There may be a private trust for religious purposes but no private charitable trust.[123]

Trusts for a *sadavart* or for the political advancement of the country are liable to be treated as trusts in which the income is not receivable on behalf of any one known person.[124]

Income derived from property held under trust in part for charitable or religious purposes, is exempt from the income tax to the extent of the actual expenditure on such purposes. Even if the income spent for such purposes exceeds the proportion for which the trust-deed provides, tax exemption will be available in respect of the amount applied to such purposes.[125]

xvii. A Hindu deity, personified by an idol, is a juristic entity, capable of holding property, and also liable to tax where the endowment is private.[126] Dedication to a deity is distinguishable from a trust in which a family deity is made a beneficiary. An endowment does not technically create a trust as understood in the English law, but in a larger sense, but evidence is required to decide whether an endowment is real or illusory.[127] The income of the deity includes the amounts spent on daily worship and religious ceremonies connected with the deity. The surplus income of an estate resting in a deity under a will, after meeting its expenses, cannot be taken to be held in trust for charitable purposes and is not, therefore, entitled to tax exemption.[128] Where, instead of dedication of assets to a deity, a trust is formed for daily worship and performance of ceremonies "for the benefit of the author and members of his family" the trust properties are not includible in the settlor's hands.[129] The trust income can not also be aggregated with the author's.

xviii. Where any properties are consecrated to a deity and the *shebaits* are required to give effect to the pious purposes symbolised in it, e.g., to arrange for the daily worship and other services and hold and manage the properties for and on behalf of the deity, it will be a case of a specific trust for a single person.[130] If there

are two deities, separate assessments may be necessary.[131]

xix. Even the deities for whom an endowment is made are not excepted by the provision regarding discretionary trusts. Where the *shebait* of a private religious trust is empowered to vary the amounts to be spent for two deities, the shares of the deities in the income of the trust are considered indeterminate.[132] Where, however, a bequest does not specify the shares of the different deities, the income will have to be apportioned equally among them and they will also be taxed accordingly.[133]

xx. Proceedings for the recovery of the tax due from the deity will be against the trustees where a trust as such is constituted and the trust properties are transferred to the trustees.[134]

xxi. There is no element of gift in a *waqf* which is a settlement.[135] A *waqf* which is revocable or contingent is not valid.[136] A *waqf* is treated like an irrevocable trust for tax purposes, and the liability to tax of the *waqif* or the founder, the *mutawalli* or the manager,[137] and the beneficiaries will depend on the terms of the *waqf*-deed.[138] Where the surplus income of a religious trust is distributed among certain specified class of beneficiaries under a court scheme, their shares cannot be considered to be indeterminate.[139] A private *waqf* is not entitled to tax exemption.[140] A *waqf-alal-aulad* in which no one is entitled to a specific share, may be treated like a discretionary trust. But, where the income of the *waqf* is required to be distributed among the beneficiaries in accordance with the Mohammedan law it has to be dealt with as a trust in which the shares of the beneficiaries are fixed, unless the terms of the *waqf*-instrument point to the contrary.[141] The *mutawalli* is treated as a trustee though he is not one, in the technical sense, under the Mohammedan law.[142] He can represent the *waqf* in a partnership like the trustee of a trust.[143]

xxii. A trust which is not exempted as a public trust is

liable to tax through the trustees, like an "association of persons"[144] or a "body of individuals",[145] depending on whether it is carrying on a business or is merely deriving income from investments.

xxiii. The interest of the settlor or a beneficiary in a trust or a *waqf* must be valued for levying the wealth tax even though it may be a personal estate, incapable of being sold in the open market. For this purpose, a hypothetical sale must be assumed in a fictional market.[146]

xxiv. Joint trustees of a trust will be taken to be a single unit and not as an "association of persons" for wealth tax purposes. The unit will be assessable to the wealth tax as an individual under section 21(1) or (4) of the Wealth-tax Act.[147] The liability will, however, be determined "in the like manner and to the extent" it will be leviable upon and recoverable from the individual beneficiaries.[148] Where the value of the trust estate exceeds the sum of the values of the individual beneficiaries' interests the trustees will bear tax on the difference at not less than three per cent.[149]

xxv. Sub-section (1) of section 21 of the Weath-tax Act will be applicable with the option to the Revenue to tax either the beneficiaries or the trustees where the beneficiaries have a life interest in the trust or get specified sums of money periodically or are entitled to a fixed share in the assets or specified assets. But if there is any indefiniteness in regard to the shares of the beneficiaries in the trust properties or the beneficiaries are not known e.g., the number and identity of the remaindermen, the value of the relevant "interest" about which there is uncertainty will be assessable to tax under section 21(4) at the rates specified in Part I of Schedule I of the Wealth-tax Act or at the rate of three per cent, whichever may be more beneficial to the revenue.[150] The exemption under section 5(1)(xvi) in respect of notified securities will be available only to the person in whose name they stand and not to the beneficial owners.[151]

Estate Duty

Estate duty, introduced in 1953, before the wealth tax (1957) and the gift tax (1958), was modelled on the English law. It had, therefore, the advantage of the experience in the administration of the law in the UK. Many of the intricacies caused by the use of trusts in that country repeated themselves in India too. The following are some of the noteworthy features of the treatment of settlements in trust in the levy of estate duty in India :

i. Beneficial interest in a settlement is movable property. There will be liability to the estate duty, irrespective of domicile, in respect of all properties, movable or immovable in India, "passing" or changing hands on a death. When an individual domiciled in India expires, his movable property outside India is also exigible to duty.[152] On the death of a person not domiciled in India, there will be liability for duty on movable property outside India, only if it is settled property, and the settlor had been domiciled in India when the settlement was effected.[153]

ii. Beneficial interest in a settlement may be absolute or limited. It will attract liability to the duty, only if its disposal had been within the competence of the deceased.[154] For example, when L is given a life-estate in certain property and R, the remainderman, is to get the absolute estate after L's death, the duty is chargeable on L's death.[155]

iii. However, an interest in expectancy that does not ripen into an interest in possession before the death, will not suffer duty. To illustrate, if R the remainderman predeceases L who has been holding the life-estate, there will be no duty. Interest in possession implies that the intended benefit has materialised.[156]

iv. Life interest reserved by a settlor is includible in the dutiable estate even if the immediately succeeding beneficiaries are also given only a life-interest[157].

v. A limited right to withdraw income from a trust and the right to receive share of trust property on the revocation of the trust would be interests that pass on

the death of the beneficiary.[158] There is no cesser of interest on the death of the beneficiary when a trust is terminated under an enactment and the beneficiary receives the same income as before by way of bounty and not as a right till his or her death. But a life interest that ceases by the operation of a statute is also includible in the estate of the deceased beneficiary as a limited interest disposed of less than two years before the death.[159]

vi. Property does not pass where there is mere enlargement of an existing beneficial interest.[160] It does, however, pass when ownership right is acquired over the residuary estate by some persons who, along with others, had beneficial interest in it earlier.[161]

vii. Ordinarily, executors assume the duties of trustees as soon as debts are paid and an asset has been given to the legacies.[162] But, the interest of a benificiary in an estate can be an interest in possession, even before the completion of the administration of the estate of the deceased settlor.[163] The beneficiary's interest in the property will bear duty in the event of his demise during the pendency of the administration.[164] Where the Official Trustee is appointed as the sole executor as well as trustee in terms of sections 7(6) and 9 of the Official Trustees Act, he ceases to be the executor as soon as he obtains the probate and he is accountable for the properties, which vest in him from that moment, as a trustee.[165]

viii. The value of property settled for non-charitable purposes less than two years before death will be includible in the estate. of the deceased settlor. The date of the settlement is the relevant one for this purpose. Accretions to the settled property between the date of the settlement and the death of the settlor will be ignored.[166]

ix. The transfer of legal ownership to the beneficial owner is not required for the levy of the duty[167] but a trust will be imperfect unless the legal ownership of the trust property vests in the trustee. Immovable

property of which the owner had not divested himself through a proper transfer document registered according to the law of registration, will be considered to be a part of the estate of the owner at its market value as on the date of his death.[168] The expression of a desire to transfer the property to a trust is alone not sufficient to bring about a trust.[169]

x. Employment of the income of a trust property by way of loans from the trust or reservation of any interest in a settled property for the settlor and his relatives will result in duty being charged on the entire property.[170] A gift conditional on the maintenance of the donor and some of his relatives is a settlement with reservation[171]. A gift from which the donor is not excluded entirely, e.g., money transfered to a trust account but not withdrawn from the settlor's firm will be treated as a part of the estate of the donor on his death[172]. When a part of the premises transferred to a trust for the benefit of the settlor's son was leased to the settlor after the creation of the trust, it was held that there would be estate duty liability despite the lease consideration being adequate. But a mere expression of hope that the beneficiaries in a settlement will look after the settlor during his life-time without creation of any charge on the settled properties cannot be taken to be reservation of an interest in the properties[173]. No damage is also caused where the life with reference to which any interest is reserved in a settled property is not the settlor's life.[174]

vir Property which is to revert to the disponer will not be deemed to pass on the temporary beneficiary's death. If S settles some property on L for either a stipulated period or L's life-time, and then for himself, no duty is payable on L's death. The reason is that L is not competent to dispose of the property. If the property does not go back to the settlor himself but his legal heirs and successors, duty is exigible.[175]

xii. An endowment providing for the worship of family deities, in which the public do not have the right to

participate, is a private trust but it will not offend the rule of perpetuity. There will be no estate duty on the death of the settlor if the endowment was made at least two years earlier; and the "beneficiary" is immortal. There may, however, be some liability to duty on the death of the *shebait*, who manages the estate, since he is not the mere holder of an office or a trustee. A *shebait* has interest in the property, which passes on his death to his successor, who is usually his legal heir[176].

xiii. The *mahanth* of a *math* is in charge of a religious institution. Where one is the elected head of an institution and celibacy is a prerequisite for the election, there can be no liability to the estate duty on his demise. Nobody can have a vested right to the dead man's shoes. The *mahanth* is merely a trustee for a trust without any heritable beneficial interest in it[177].

xxiv A *waqf* is a permanent dedication of property for any purpose recognised by the Mohammaden law as religious, pious or charitable[178]. But *waqf* property is settled property. If the *waqif* or settlor is entitled to a share of the income from the property, or the *mutawalli* has the power to nominate additional beneficiaries which may enable him to include himself as one of them, duty will be imposed on the property as a whole[179]. Reservation of the right of residence in a property under a *waqf* will result in the value of the residential property becoming liable to duty on the death of the *waqif*[180]. But the right to reside in a settled property as a *mutawalli* or trustee and not as the settlor will not amount to reservation of any interest by the settlor.[181]

xv. Property held by anyone in a fiduciary capacity as a trustee for any other person, or the *mutawalli* of a *waqf* is not liable to duty on his death[182], unless he had himself settled the property in trust, in which case also it will be excluded from his estate if the beneficiary had assumed possesssion and was in enjoyment of the property at least two years before his death[183]. Settled

property cannot be taken to be within the disposing capacity of the settlor, merely because he is the managing trustee and the other trustees are obliged to act on his directions[184]. Provisions in the trust deed empowering the settlor-trustee to rectify the deed to make it more effective will not make the trust revocable[185]. But if the deed confers on the settlor the authority to vary or cancel the trust and this authority has not been surrendered at least two years before the settlor's death, the trust property will not be excludible from the settlor's estate when he expires[186]. The offending clauses may, however, be nullified when the trust is blended with other trusts which do not provide any scope for revocation of the trust[187].

xvi. Where trust funds are kept by the trustees in deposit with the founder of the trust at any time during the two years preceding his death, the amount so held will be liable to the estate duty on his death on the ground that he had not been excluded from its possession and enjoyment[188].

xvii. If a part of a trust contravenes the rule against perpetuity and is voided, the relevant properties would continue to be the properties of the author and pass to his legal heirs and successors on his death[189].

The estate duty attaches itself only to property which "passes" on an individual's death, i.e., property which he has left or which changes hands or in which rights have been modified by reason of his death. Since no such consequence can follow when any property is held in a discretionary trust, particularly one from which the deceased has not derived any tangible benefit, it is unharmed by the estate duty, unless it has been set up by the deceased and he is one of its beneficiaries[190].

NOTES

1. "Settlement" means settling a property, right or claim, coveyance or disposition of a property for the benefit of another : CGT v N.S Getti Chettiar (1971) 182 IRT 599 (SC). The implications of a settlement have been examined at length in English cases : Chamber. lain v IR (1943) 2 All ER 200, 25 TC 317 (HL) ; Hood-Barrs v IR-

(1946) 2 All ER 768, 27 TC 385 (CA); IR v Leiner (1964)41 TC 589; IR v Plummer (1979) 3 All ER 755. See also para 1 (2) of Schedule 5 to the UK Finance Act 1975.

2. S. 60, Income-tax Act, which neutralises the Bombay High Court ruling in D.R. Shahapure v CIT (1946) 14 ITR 781 (Bom). Transfer by over-riding title does not protect the transferor: Ganpatari Sagarmal (Trustees) For Charity Fund v CIT (1963) 47 ITR 625 (Cal); Provat Kumar Mitter v CIT (1961) 41 ITR 624 (SC); S. Kartar Singh v CIT (1969) 73 ITR 438 (Del). Sections 60 and 61 will be inapplicable to the case of a bare trustee who continues to hold the trust property for the beneficiaries even after the trust has come to an end: Behramji Sorabji Lalkaka v CIT (1948) 16 ITR 301 (Bom). The right to income may itself be an asset, and it may not be easy to decide in some cases whether an asset or income is being transferred: Smt. M.S. Subbulakshmi v CIT (1955) 28 IRT 561 (Mad). Assignment of share of profits in a partnership concern is application of income: K. A. Ramachar v CIT Madras (1961) 42 IRT 25 (SC), affirming Rangachari, A.R., v CIT Madras (1955) 28 IRT 528 (Mad).
3. S.61 Ibid. A trust will be considered revocable even if the settlor needs the concurrence of others for its revocation: Wiggins v Watson's Trustees 1934 AC264; Ramji Keshavji v CIT (1945) 13 ITR 105 (Bom); Behramji Sorabji Lalkaka v CIT (1948) 16 IRT 301 (Bom). The authority to appoint additional beneficiaries will make a trust revocable: Keshavlal Punjaram v CIT (1944) 12 ITR 185 (Bom); K. Subramania Pillai v Agl ITO (1964) 53 ITR 764 (Mad). A trust will not be the less revocable because the power of revocation can be exercised only by the trustees and not by the settlor: IR v Warden 22 TC 416; IR v Countess of Kenmare 34 ITR 811 (HL). Cancellation of a provision in the trust deed forfeiting the interest of a beneficiary in certain circumstances will not, however, imply revocation of the deed: Tayabali Abdul Hussain Mandiwala v CIT (1949) 17 ITR 187 (Sind).
4. CIT v Radhaswami Satsang (1981) 132 ITR 647 (All).
5. S.62 Income-tax Act. CIT v Bhuwaneswari Kuer (1964) 53 ITR 195 (SC); Hrishikesh Ganguly v CIT (1971) 82 ITR 160 (SC); CIT v Kikabhai Premchand (1948) 16 ITR 207 (Bom); Ramji Keshavji v CIT (1945) 13 ITR 105 (Bom); CIT v Jitendra Nath Mullick (1963) 50 ITR 313, 320-2 (Cal); Dr. A.J. Kohiyar v CIT (1964) 51 ITR 221 (Bom); CIT v Raghbir Singh (1965) 57 ITR 408 (SC); Manikkavasagam Chettiar v CIT (1964) 53 ITR 292 (Mad). The exclusion of the income is conditional on the transferor's not deriving any direct or indirect benefit from the income. Further, the income will be chargeable to income tax as the income of the transferor as and when the power to revoke the transfer arises. In the UK, the income arising under a settlement in includible in the top slice of the income of the settlor if a settlement can be revoked. The tax paid can,

however, be realised from the trustees by the settlor : section 446 and section 449(3) and (5) ICTA 1970.

6. Chunilal Mulji Motani v CIT Tax LR 283, 290-1 (Cal), (1981) Taxman 400 (Cal) ; (1913) 139 ITR 166 (Cal). Unlike sec. 63 (a) of the Income-tax Act, 1961, sec. 16 (1) (c) of the Income-tax Act 1922 did not make a trust revocable, if only a part of the income or benefit of the trust was reserved for its author ; the benefit which was or could be enjoyed by the author of the trust was includible in his income : Hrishikesh Ganguly v CIT (1971) 82 ITR 160 (SC) ; CIT v Rani Bhuwaneswari Kuer (1964) 53 ITR 195 (SC) ; CIT v Jitendra Nath Mullick (1963) 50 ITR 313 (Cal). Power to remove trustee and alter terms of trust deed will make a trust revocable : Panchanan Dey (decd) v CIT (1983) 142 ITR 762 (Cal).

7. S.63 Income-tax Act. C.T. Senthilnathan Chettiar v State of Madras (1968) 67 ITR 102 (SC) ; CIT v Kikabhai Premchand (1948) 16 ITR 207 (Bom) ; Ramji Keshavji v CIT (1945) 13 ITR 105 (Bom).

8. Re. Jayantilal Amritlal (1965) 55 ITR 214 (Guj), affirmed in (1958) 67 ITR 1 (SC) ; Also see CIT v Raghbir Singh (1965) 57 ITR 498 (SC) affirming Raghbir Singh v CIT (1961) 42 ITR 410 (Punj) Nathalal Ratilal v CIT (1954) 25 ITR 426 (SC) ; CIT v Nawab Sir Mir Osman Ali Bahadur (1974) Tax LR 86 (AP) ; CIT v Shyamlal Bhuwalka (1978) 113 ITR 127 (Cal) ; CIT v Brojendranath Kundu (1977) 110 ITR 336 (Cal) ; CIT v Smt. Nathi Bai Binani, IT Ref. 423 of 1975 decided by the Calcutta High Court on 12.5.1975 ; Tulsidas Kilachand v CIT (1961) 42 ITR (SC) ; Manikavasagam Chettiar v CIT (1964) 53 ITR 292 (Mad) ; CIT v Gopal Krishna Kone (1965) 57 ITR 569 (Mad) ; Keshavlal Punjaram v CIT (1944) 12 ITR 185 (Bom) ; R.B. Shan v CIT (1976) CTR 493 (Bom) ; Ramji Keshavji v CIT (1945) 13 ITR 105 (Bom) ; CIT v Sir S.M. Bose (1952) 21 ITR 135 (Cal) ; Chunilal Mulji Motani v CIT (1913) 139 ITR 166 (Cal) ; CIT v Rani Bhuwaneswari Kuer (1964) 53 ITR 195 (SC) ; CIT v Trustees of Sreeram Surajmall Charity Trust (1971) 79 ITR 649 (Cal) ; CIT v Kikabhai Premchand (1948) 16 ITR 207 (Bom) ; CIT v Jagdish Pratap Soha (1971) 79 ITR 235 (All) ; CIT v Jitendra Nath Mullick (1963) 50 ITR 310 (Cal) ; Hrishikesh Ganguly v CIT (1971) 82 ITR 160 (SC) ; Subramania Pillai v Agl ITO (1964) 53 ITR 764 (Mad)

9. CIT v Juggilal Kamalapat (1967) 63 ITR 292 (SC), affirming Juggilal Kamalapat v CIT (1964) 53 ITR 351 (Cal) ; CIT v Smt. Nandiniben Narottamdas (1981) 7 Taxman 389 (Guj).

10. Mrs. Leela Nath v CIT (1982) 134 ITR 507 (Cal). Also, S. Raghbir Singh v CIT (1961) 42 ITR 410 (Punjab) affirmed in CIT v S. Raghbir Singh (1965) 57 ITR 408 (SC), where the settlor's debts were repaid out of the income of a trust, but the view was expressed that the discharge of a settlor's liability through a trust would not bring the trust within the purview of s. 16 (1) (C) of the Income-tax Act, 1922,

corresponding to s.63 of the Income-tax Act, 1961. In the UK, reservation of power by the settlor to use the settled funds is treated as power to revoke the settlement : s. 446 (2) ICTA 1970 ; Also IR v Kenmare (1958) 34 ITR 811 (HL) ; 37 TC 383 ; (1957) 3 All ER 33. The equivalent of any loan advanced by the trustees to the settlor or his spouse is deemed to be his income. Even where a settlor lent money to a settlement made by him, repayment of the loan has been held to be retention of an interest in the funds of the settlement; IR v De Vigier 42 TC 25 (HL) ; (1964) 2 All ER 907.

11. Tayab Ali Abdul Hussain Mandiwala v CIT (1949) 17 ITR 187 (Sind).
12. CIT v Sir S.M. Bose (1952) 21 ITR 135 (Cal).
13. Mrs. Leela Nath v CIT (1982) 134 ITR 507, 517 (Cal).
14. Nawal Kishore Choudhury v ITO (1980) 122 ITR 576 (Cal).
15. Nawal Kishore Choudhury v ITO (1980) 122 ITR 576 (Cal).
16. Williams v Singer (1920) 7 TC 387, 411. The trustees can be assessed even if there is only one beneficiary : Hamilton-Russel's Executors v IR (1943) 25 TC 200. As for Indian authority, see Aggarwal Chamber of Commerce Ltd. v Ganpatrai Hiralal (1958) 33 ITR 245, 251, 252 (SC) ; Executors of the Estate of J.K. Dubash v CIT (1951) 19 ITR 182, 189, (SC) ; Official Trustees of West Bengal v CIT (1968) 67 ITR 218 (Cal).
17. M/s Haji Abdul Hamid v CIT (1967) Tax LR 165 167 (All).
18. C.R. Nagappa v CIT (1969) 73 ITR 626 (SC) ; CIT v Mir Osman Ali (1966) 59 ITR 758 (SC) ; CIT v Balwantrai Vaidya (1958) 34 ITR 187 (Bom) ; Birendra Kumar Dutta v CIT (1961) 42 ITR 661 (Cal) ; A. Razzak v CIT (1963) 48 ITR 276 (Cal) ; J.N.A. Hobbs v Dy. Commissioner of Agricultural Income Tax (1963) 49 ITR 811 (Mys) ; Haji Abdul Hamid v CIT (1967) Tax LR 165, 167 (All); Aggarwal Chamber of Commerce Ltd. v Ganpatra Hiralal (1958) 33 ITR 245, 251 (SC).
19. CIT v Balwantrai Jethalal Vaidya (1958) 34 ITR 187 (Bom) ; Khan Bahadur M. Habibur Rahman v CIT (1945) 13 ITR 189 (Pat).
20. Khimji Keshavji Trust Estate v CIT (1978) 113 ITR 751, 758 (Cal).
21. C.R. Nagappa v CIT (1969) 73 ITR 626, 629 (SC) ; CIT v Manilal Dhanji (1962) 44 ITR 876, 886 (SC) ; CIT v Arvind Narottam (1969) 73 ITR 490, 496 (Guj) ; Mahanth Ramswaroop Das v State of Bihar (1961) 42 ITR 770, 773 (SC) ; Shrimant Govinda Rao Narayan Rao Ghorpade v CIT (1973) 48 ITR 54, 73, 64 (Bom) ; Arundhati Balkrishna v CIT (1976) 102 ITR 356 (Guj)
22. Mrs. Saldana v CIT 6 ITC 114 (Mad-FB) ; AIR 1932 M 378 ; Hotz Trust, Simla v CIT Punjab AIR 1930 LAH 929 ; (1930) 5 ITC 8 ; Sir Sorabji Mehta v CIT Bombay (1933) 6 ITC 386. Panna Sanjay Trust v CIT (1969) 74 ITR 396 (Guj) ; Trustees of Chaturbhuji Raghavji Trust v CIT (1963) 50 ITR 693 (Bom) ; C.R. Nagappa v CIT (1969) 73 ITR 626 (SC) ; CWT v Kum. Manna G. Sarabhai (1972) 86 ITR 153) Guj).

23. CBDT instruction no. 45/78/66-ITJ (5) Dated Feb. 22, 1967 and Circular 157 Fro. 228/8/73 IT (AII) Dated Dec. 26, 1974.
24. In re. Lokmanya Tilak Jubilee Fund (1942) 10 ITR 26; Estate of Harendra Kumar Roy v CIT Bengal (1944) 12 ITR 68 (Cal); D.V. Arur v CIT (1945) 13 ITR 465; Income-tax Appellate Tribunal Bombay Lalji Radha Madho Trust (1946) 14 ITR 460 (Nag); Yakub Versey Shri v CIT (1946) 14 ITR 548 (Bom); CIT v Indubala Sen Trust (1975) 101 ITR 561 (Pat); CIT v Puthiya Ponmani Chintakam Waqf (1962) 44 ITR 172 (SC); CIT v Manilal Dhanji (1962) 44 ITR 876 (SC); Bankim Chandra Dutta v CIT (1966) 62 ITR 239 (Cal); Nirmala Bala Sarkar v CIT (1969) 74 ITR 268 (Cal); CIT v Trust Estate of Tarun Kumar Roy ((1974) 94 ITR 361 (Cal); CWT v Arvind Narottam (1976) 102 ITR 232 (Guj); CIT v Arvind Narottam (1969) 73 ITR 490 (Guj); V.E.A. Vairavan Chettiar v CIT (1973) 92 ITR 474 (Mad); Smt. Santimoyee Bose v CIT (1969) 74 ITR 133 (Cal); CIT v Lady Ratanbai Mathuradas (1968) 67 ITR 504 (Bom); D.M. Vakil v CIT (1946) 14 ITR 298 (Bom).
25. CIT v Hemant Bhagubai Mafatlal (1982) 135 ITR 768 (Bom).
26. Bankim Chandra Dutta v CIT (1966) 62 ITR 239 (Cal).
27. CIT v Indu Bala Sen Trust (1975) 101 ITR 561, 567 (Pat).
28. Sahebzadas of Sarf-e-khas Trust, Trustees of, v CIT (1962) 44 ITR 332 (AP); CIT v Arvind Narottam (1969) 73 ITR 490 (Guj); CIT v Puthiya Ponmani Chintakam Waqf (1962) 44 ITR 172 (SC); Shamsuddin Khan v CIT (1958) 33 ITR 733 (Orissa); B.P. Mahalaxmiwala, v CIT (1954) 26 ITR 177 (Bom) dissenting from Yakub Versey Lalji v CIT (1946) 14 ITR 548 (Bom); Official Trustee of West Bengal v CIT (1954) 26 ITR 410 (Cal). Lady Ratanbai Mathuradas (1968) 67 ITR 504 (Bom); CIT v Indu Bala Sen Trust (1975) 101 ITR 561 (Pat); G.T. Rajamannar v CIT (1964) 51 ITR 339 (Mys); Nirmala Bala Sarkar v CIT (1969) 74 ITR 268 (Cal); Santimoyee Bose v CIT (1969) 74 ITR 133 (Cal).
29. This was done in implementation of a recommendation of the Law Commission, *12th Report* : List 1, p. 66.
30. Panna Sanjay Trust v CIT (1969) 74 ITR 396 (Guj). The 1st proviso to Sec. 41 of the Act of 1922 provided for the maximum rate of income tax and also for super-tax at the appropriate rate in such cases : Official Trustee of West Bengal v CIT (1954) 26 ITR 410 (Cal).
31. Official Trustee of West Bengal v CIT (1954) 26 ITR 410 (Cal); Sahebzadas of Sarf-e-khas Trust v CIT (1962) 44 ITR 332 (AP); CIT v Trustees of the Estate of Tarun Kumar Roy (1974) 94 ITR 361 (Cal).
32. R.H. Pandit v CIT (1972) 83 ITR 136 (Bom); Suhasini Karuri v WTO (1962) 46 ITR 953 (Cal); Padmavati Jaykrishna Trust v CWT (1966) 61 ITR 66 (Guj); Trustees of Putlibai R.F. Mulla Trust v CWT (1967) 66 ITR 653 (Bom); CWT v Trustees of Hansabai Tribhuwandas Trust (1968) 69 ITR 527 (Bom); Habibur Rahman v

CIT (1945) 13 ITR 189 (Pat); CIT v Puthiya Ponmani Chintakam Waqf (1962) 44 ITR 172 (SC).

33. Birendra Kumar Dutta v CIT (1961) 42 ITR 661, 670 (Cal).
34. Proviso (iii) to s. 164 (1). It has been held that a trust for beneficiaries who are not mainly dependent on the settlor at the time of the creation of the trust will not get the advantage of this treatment: CIT v Gunvantlal Family Trust (1982) 133 ITR 162 (Guj). The term "relative" has been construed to be wide enough to include "ladies of position" who were not legally wedded to the settlor and also mistresses of the settlor whom he chose to regard as his relatives and for whom he provided in a trust: CWT v Trustees of HEH the Nizam's Family Pocket Money Trust (1982) 134 ITR 444 (AP) dealing with the second proviso to s. 21 (4) of the Wealth-tax Act which is worded like proviso (iii) to s. 164 (1) of the Income-tax Act. If a trust has been created *bona fide* for the benefit of the relatives of the settlor, mere non-application of the funds for its objects in the subsequent years will not disentitle the trust to treatment like an association of persons for tax purposes: Seth Keshrichand Khaitan Education and Welfare Trust v CIT West Bengal, (1982) 138 ITR 351 (Cal).
35. Piarelal Sakseria Family Trust v CIT (1982) 136 ITR 583 (MP).
36. In India as in the UK, oral trusts could be proved by evidence: In re. Allen (H/L 1925) 9 TC 234; Brenan v Scanlon (K/B 1925) 9 TC 427.
37. Subsec. (1) (v) and explanations 1 and 2 to s. 160 and s.164 A of the Income-tax Act. Till this amendment, oral trusts were chargeable to tax under s.4 and not under the provisions relating to representative assessees, vide the Law Commission, *12th Report*, p. 424.
38. S. 164 (1) of the Income-tax Act covering discretionary trusts.
39. Nicholas Kaldor (1956): *Indian Tax Reform—Report of a survey*.
40. Trustees of Gordhandas Govindram Family Charity Trust v CIT Bombay (1973) 88 ITR 47 (SC).
41. Purshottam N. Amarsey and Another v CWT (1973) 88 ITR 417 (SC), affirming CWT v Purshottam N. Amarsey (1969) 71 ITR 180 (Bom).
42. CIT v P.P. Hassan Koya (1967) 63 ITR 791 (Ker); Nelliyil Ummer Kutty v State of Kerala (1970) 77 ITR 489 (Ker); Tulsidas Kilachand v CIT (1961) 42 ITR 1 (SC); Harinder Singh v CIT (1969) 73 ITR 236 (Punj).
43. His Highness Yeshwant Rao Ghorpade v CWT (1966) 61 IRT 444 (SC).
44. Bai Hansabai Mehta v CIT 16 ITR 115 (Bom); CIT v Phirozsha Pestonji 96 ITR 185 (Guj); CWT v Official Trustee of West Bengal for Trust Murshidabed Estate (1982) 136 ITR 162 (Cal).
45. Chintamani Ghosh Trust v CWT (1971) 80 ITR 331 (All).
46. The Court directed the actuarial valuation of the life-interest of a beneficiary entitled to the income from certain shares and the use of jewellery of large value, some for daily purposes and others on

ceremonial occasions : CWT v Trustees of HEH the Nizam's Sahebzadi Anwar Begum Trust (1981) 129 ITR 796 (AP).

47. CWT v V. Thiruvenkata Reddiar (1981) 128 ITR 689 (Ker).
48. A beneficiary of a specific trust is eligible like any other taxpayer for the exemptions available under section 5 of the Wealth-tax Act : CWT v Thiruvenkata Reddiar (1981) 128 ITR 689 (Ker).
49. CWT v Purshottam N. Amarsey (1969) 71 ITR 180 (Bom), affirmed in 88 ITR 417 (SC).
50. CWT v Trustees of HEH Nizam's Family (Remainder Wealth) Trust (1977) 108 ITR 555 (SC); CWT v Trustees of HEH the Nizam's Miscellaneous Trust (1980) 126 ITR 233 (AP).
51. CWT v Trustees of HEH Nizam's Family (Remainder Wealth) Trust (1977) 108 ITR 555 (SC); Suhasini Karuri v WTO (1962) 46 ITR 953 (Cal); Trustees of Putlibai R.F. Mulla Trust v CWT (1967) 66 ITR 653 (Bom); CWT v Trustees of Mrs. Hansabai Tribhuwandas Trust (1968) 69 ITR5 27 (Bom) ; Padmavati Jaykrishna Trust v CWT (1966) 61 ITR 66 (Guj); CWT v Arundhati Balkrishna Trust (1975) 101 ITR 626 (Guj) ; CWT v Waqf K.B. Syed Ahmed Hussain Rizvi (1979) 116 ITR 344 (All); Trustees of HEH the Nizam's Supplemental Jewellery Trust v CWT 1975 Tax LR 1085 (AP) ; CWT v Trustees of HEH the Nizam's Sahebzadi Anwar Begum Trust (1981) 129 ITR 796 (AP).
52. CWT v K.J. Somaiya Trust (1977) 109 ITR 798 (Bom); CWT v Trustees of the Estate of V.R. Chetty and Brothers (1979) 120 ITR 329 (Mad).
53. CWT v Trustees of HEH Nizam's Family (Remainder Wealth) Trust (1977) 108 ITR 555 (SC).
54. The status of the beneficiaries has no relevance in the case of a discretionary trust : Maulik Trust v WTO, WT Appl. No. 235 (Ahmd) of 1981 (Assessment year 1980-81), Order dated April 3, 1982, of the ITAT Ahmedabad Bench "B" reproduced at pp. 721-4, *Selected Orders of ITAT*, vol. 2, Taxmann, Delhi, 1983.
55. Subsec. (4A) and the explanation to subsec. (1) of s. 21 of the Wealth-tax Act 1957.
56. The expression implies a transaction between two or more living persons, i.e. bilateral or multi-lateral transactions and not a unilateral transaction : CED v Smt. Laxmi Bai (1980) 126 ITR 73 (All) ; CGT v Maharaja Pateshwari Prasad Singh (1971) 82 ITR 654 (All).
57. CGT v Maharaja Pateshwari Prasad Singh (1975) 98 ITR 480 (All).
58. Pyndah Satti Raju v CGT (1977) 108 ITR 240 (AP); Vadulla Venkata Rao v CGT (1972) 85 ITR 240 (AP).
59. S. 5 (1) (ii) of the Gift-tax Act, 1958.
60. S. 50 A of the Estate Duty Act, 1953.
61. CGT v Dr. R.B. Kamdin (1974) 95 ITR 476 (Bom).
62. Levy of the tax was upheld in Mrs. Kunjharam Joseph v CGT (1973) 88 ITR 207 (Ker) ; V.S. Mani v CGT (1980) 123 ITR 414 (Mad). It

was upset in CGT v Smt. Anasuya Sarabhai (1982) 133 ITR 108 (Guj). For further illustrations of acceleration of interest : CIT v Bhagwandas S. Malvi & others (1977) 107 ITR 426 (Bom) ; CIT v Smt. Kasturbai Walchand Trust (1964) 51 ITR 255 (Bom) affirmed in (1967) 63 ITR 656 (SC).

63. CGT v Mrs. Jer Mavis Lubimoff (1978) 114 ITR 90 (Bom) ; CGT v Smt. Anasuya Sarabhai (1982) 133 ITR 108 (Guj).
64. S. 2 (xxiv) and s. 4 (1) (e) of the Gift-tax Act. Compare s. 23 (2) of the 1975 Act in the UK where a general power of appointment is equivalent to ownership : Re. Triffitt (1958) 2 All ER 299 ; Pilkington v IR (1962) 3 All ER 622.
65. See pages 38 and 41 supra.
66. CIT v Kalechand Motiram (1949) 17 ITR 304, 306, 307 (Sind) ; Hanmantram Ramnath v CIT (1946) 14 ITR 716 (Bom) ; Chambers v Chambers AIR (1944) PC 78 ; CIT v Trustees of Sreeram Surajmal Charity Trust (1971) 79 ITR 649, 657, 660 (Cal).
67. J.K. Trust v CIT (1957) 32 ITR 535, 541 (SC) ; Juggilal Kamlapat Bankers v WTO (1979) 116 ITR 646 (All) ; CIT v Nandiniben Narottamdas (1981) 26 CTR (Guj) 200 ; Pandit Lakshmikant Jha v CWT (1973) 90 ITR 97 (SC) ; Ahmed G.H. Ariff v CWT (1970) 76 ITR 471 (SC) ; CWT v H.H. Smt. Rajkuvarba (1972) 86 ITR 783 (Mys) ; CWT v Smt. Rani Kaniz Abid (1974) 93 ITR 332 (FB All) ; Dharma Vijaya Agency v CIT (1960) 38 ITR 392, 399 (Bom) ; A.J. Patel (by his legal representative) v CIT (1974) 97 ITR 683 (Bom). Even trusteeship can be property if emoluments are attached to the office : Angurbala Mullick v Debabrata Mullick AIR 1951 SC 293. Also see 182 below.
68. CIT v Jitendranath Mullick (1963) 50 ITR 313, 325 (Cal) ; H.R. Munro v Commissioner of Stamp Duties (1934) AC 61 ; 2 EDC 462.
69. Smt. M.S. Subbulakshmi v CIT (1955) 28 ITR 561 (Mad).
70. V.M. Raghavulu Naidu & Sons v CIT (1933) ITR 135 (Mad), where the claim of executors and trustees of a will for deduction of maintenance allowance to the mother and widow of the testator, was disallowed. Also, CIT v Dadabhoy G. Broacha (1968) 68 ITR 614 (Bom), where assignment of life interest to wife and minor children was held to be a transfer of an asset to them and the income from the relevant trust properties was aggregated accordingly with the other income of the assignor ; and Sunil Ramdas v CWT (1981) 132 ITR 92 (Bom), where contigent interest in trust property was held to be includible in taxable wealth.
71. CIT v Trustees of Sreeram Surajmal Charity Trust (1971) 79 ITR 649 (Cal) ; Dalooram Jainarayan v CIT (1962) 44 ITR 379 (Mad).
72. Where Trust funds were invested by the trustees with a proprietory concern of the settlor, it was taken to be a case of gift where the donor was not entirely excluded ; CED v Mrs. Sushila Umedlal Zaveri (1982) 135 ITR 727 (Bom).

73. Chunilal Mulji Motani v CIT (1983) 139 ITR 166 (Cal) ; CIT v Bai Navajbai N. Gamadia (1959) 35 ITR 793 (Bom). (This was an oral trust for a Parsi *Hunevsala*, followed later by a trust deed which vested the settlor with powers to revoke the trust wholly or in part). See Panchanan Dey (decd) v CIT (1983) 142 ITR 762 where a settlor retained the right to remove the *shebaits* and alter the terms of the settlement in a *debuttar* estate and the settlement was held to be revocable. See also Corliss v Bowers 281 US 376 (1930).
   Expenditure incurred in setting up a trust for providing an annuity to an employee is not deductible from the employer's income, if the employer has any dominion over the sums paid through the trustees or if there is a possibility of a resulting trust emerging in favour of the employer in any contingency : Indian Molasses Co. v CIT (1959) 37 ITR 66 (SC).
74. Dwarkadas Bhimji v CIT (1948) 16 ITR 160 (Bom); CGT v Maharaja Pateshwari Prasad Singh (1971) 82 ITR 654 (All); Aked v Shaw 28 TC 286 ; IR v Allan 9 TC 234 (HL) ; IR v Parsons 13 TC 700 (CA).
75. The fiduciary is only the medium for the assessment of the income or wealth of the beneficiary. Though he may be the legal owner of the property, his ownership is subject to his obligation to hold and use the corpus as well as the income for the benefit of the concerned beneficiary : National and Grindlay's Bank Ltd. v CWT (1978) 115 ITR 211 (Bom). The income of a trust for the liquidation of creditors' dues is liable to be assessed in the hands of the trustees on behalf of the general body of creditors and not in the hands of the persons who made the settlement or whose liabilities were arranged to be cleared through the settlement : CIT v Dutt's Trust (1942) 10 ITR 477 (Mad).
76. Thanthi Trust v ITO (1973) 91 ITR 261, 284-85 (Mad) ; Mrs. Leela Nath v CIT (1981) 6 Taxman 357 (Cal)/(1981) 22 CTR (Cal) 303 ; (1982) 134 ITR 507 (Cal).
77. CIT v Trustees of Sreeram Surajmall Charity Trust (1971) 79 ITR 649 (Cal) ; CIT v Sri Brojendranath Kundu (1977) 110 ITR 326 (Cal).
78. CIT v Jeyantilal Amritlal (1968) 67 ITR 1,9 (SC) ; CED v Bhagwandas Velji Joshi (1981) 6 Taxman 202 (Bom) : (1981) 22 CTR (Bom) 29, (1983) 139 ITR 316 (Bom).
79. Thanthi Trust v ITO (1973) 91 ITR 261 (Mad) ; Jang v Webb (1912) 13 CLR 503 ; Clifford John Chick v Commissioner of Stamp Duties of New South Wales (1959) 37 ITR (ED) 89. See also Chapter 1, n. 46.
80. CIT v Mathuradas Mangaldas Parekh IT Ref 4 of 1954, unreported judgment dated August 26, 1954 of the Bombay HC quoted by the SC in CIT v Jayantilal Amritlal (1968) 67 ITR 1 (SC) ; Ramchandra v Ranjit ILR 27 Cal 242 ; Madhav Chandra v Rani Sarat Kumari (1911) 15 CWN 126 ; Girijanand v Sailajanand (1896) ILR 23

Cal. 645 ; Ramaswami v Madras Hindu Religious Endowments Board AIR 1954 Mad 1110.

81. S. 64 (1) (vii) of the Income-tax Act and s. 4 (1) (a) of the Wealth-tax Act : D.M. Netarwala v CIT (1979) 120 ITR 848 (Bom) ; K.M. Sheth v CIT/CWT (1977) 107 ITR 45 (Bom) ; Shardaben Jayantilal Mulji v CWT (1977) 106 ITR 667 (Bom) ; Col. H H Sir Harinder Singh v CIT (1972) 83 ITR 416 (SC) ; Dr. T.M.A. Pai, In re. (1954) 25 ITR 75 (Mad); CIT v Mohd. Yusuf Ismail (1944) 12 ITR 8 (Bom); Chandulal Shivlal v CWT (1965) 55 ITR 441 (Guj); K.A. Ramachar and another v CIT (1961) 42 ITR 25 (SC) ; Baidyanath De v CIT (1960) 40 ITR 175 (Cal). The expression "spouse" takes in only the person who is lawfully wedded : CWT v Khan Sahib Dost Mohd. Alladin (1973) 91 ITR 179 (AP). Description of a lady as "wife" or reference to her children as the settlor's children in a trust deed would not make the income from the trust assets includible in the settlor's if the lady had not gone through the formalities of a valid marriage under the relevant personal law : ITO v Nawab Mir Barkat Ali Khan Bahadur (1974) 97 ITR 239 (SC) affirming Nawab Sir Mir Osman Ali Khan Bahadur v ITO (1970) 75 ITR 133 (AP). "Ladies of position", who are not legally wedded, and mistresses who have been regarded and provided for as relatives by the settlor would, however, qualify as "relatives" within the meaning of the term in the second proviso to s. 21(4) of the Wealth-tax Act and presumably also the proviso to s. 164 (1) of the Income-tax Act. That is to say, the trusts in question will be liable to the income tax on their income as if the income belonged to an association of persons and to the wealth tax at the rates applicable to an individual : CWT v Trustees of HEH the Nizam's Family Pocket Money Trust (1982) 134 ITR 444 (AP). See n. 34 above.

82. A "child" does not include a foster-child or an illegimate child for income tax purposes : s. 2 (15A) : Krishna Iyer's Executors v CIT (1960) 38 ITR 144 (Ker) ; But cl (ii) of sec. 27 (7) of the Estate Duty Act specifically provides for inclusion of illegitimate children in the term "relative" in considering dispositions in favour of relatives.

83. G.B. Banerjee v CIT (1979) 117 ITR 446, 452 (Cal) ; R. Ganesan v CIT (1965) 58 ITR 411 (Mad).

84. Dady R.D. Wadia v CIT (1971) 81 ITR 289, 292, 293 (Bom) ; CIT v Neville N. Wadia (1973) 90 ITR 155, 161, 162 (Bom).

85. CIT v Dadabhoy G Broacha (1968) 68 ITR 614 (Bom).

86. C.R. Nagappa v CIT (1969) 73 ITR 626 (SC) affirming C.R. Nagappa v CIT (1968) 67 ITR 740 (Mys) ; V.D. M.R.M. Muthiah Chettiar v CIT (1969) 74 ITR 183 (SC).

87. Arun Kumar Sarraf v CIT (1976) 104 ITR 90 (All).

88. Tulsidas Kilachand v CIT (1961) 42 ITR 1 (SC), affirming (1958) 33 ITR 383 (Bom.).

89. CIT v J.P.M. Pailly Pillai (1972) 86 ITR 516 (Ker FB) overruling

S. Viswasom v CIT (1963) 50 ITR 503 (Ker) on the question of the legal obligation of a Christian father to support his minor son. A court decree requiring maintenance of minor children by the mother out of the alimony she is to get from her husband results in the diversion of the decreed amount before it reaches the lady and, therefore, in its exclusion from her income : CIT v Smt. Shanti Meattle (1973) 90 ITR 385 (All). In such a case the father is not however relieved of the requirements to pay the income tax on the income he is compelled to apply for the children's maintenance through his wife. The payment to the wife is not liable to be aggregated with his income when it is made "in connection with an agreement to live apart" in terms of Sec. 64 (1) (iv), but not a payment made directly or indirectly for the maintenance of the children. Income spent by a widow on the maintenance and education of her children in accordance with a provision in her husband's bequest cannot be claimed to be a diversion of the income before it goes to her : CIT v Mrs. Jayalakshmi Duraiswamy (1964) 53 ITR 525 (Mad).

90. Section 64 (1) (vii) of the Income-tax Act which seeks to reach deferred benefits, superseding CIT v Manilal Dhanji (1962) 44 ITR 876 (SC).
91. Baidyanath De v CIT (1960) 40 ITR 175 (Cal).
92. CIT v Dr. B.B.A. Dalal (1974) 96 ITR 408 (Pat).
93. Explanation 2A to section 64 (1) of the Income-tax Act.
94. Explanation 1A to section 64 (1) of the Income-tax Act.
95. Clubbing the value of lands held by a taxpayer as trustee with the value of land owned by her absolutely is not permissible : K. Andalammal v Commr. of Agl. Income-tax, Madras (1981) 132 IIR 349 (Mad) ; Birendra Kumar Dutta v CIT (1961) 42 ITR 661 (Cal) ; Managing Trustees of Nagore Durgah v CIT (1962) 44 ITR 341 (Mad) affirmed in (1965) 57 ITR 321 (SC) ; Abdul Jalil Khan v Agl. IT Board, Lucknow (1958) 34 ITR 421 (All).
96. CIT v Balwantrai Jethalal Vaidya (1958) 34 ITR 187 (Bom); Birendra Kumar Dutta v CIT (1961) 42 ITR 661 (Cal) ; Mohammad Nurula v CIT (1961) 42 ITR 115 (SC); A. Razzak v CIT (1963) 48 ITR 276 (Cal) ; Harendra Kumar Roy's Estate v CIT (1944) 12 ITR 68 (Cal) ; Habibur Rahman v CIT (1945) 13 ITR 189 (Pat) ; ITAT v Radha Madho Trust (1946) 14 ITR 470 (MP) ; N.V. Shanmugam and Co. v CIT (1971) 81 ITR 310 (SC) ; N. Annamalai v CIT (1969) 73 ITR 809 (Mad) ; CIT v Pulinchandra Daw (1967) 63 ITR 179 (Cal) ; Sri Sri Sridhar Jiew v ITO (1967) 63 ITR 192 (Cal) ; CIT v Mir Osman Ali (1966) 59 ITR 666 (SC) ; CIT v Nandlal Agarwal (1966) 59 ITR 758 (SC) ; C.R. Nagappa v CIT (1969) 73 ITR 626 (SC) ; J.N.A. Hobbs v Dy. Commr. of Agl. Income-tax (1963) 49 ITR 811 (Mys) ; Currimbhoy Elbrahim Baronetcy Trust v CIT (1934) 2 ITR 148 (PC).

97. Where a trust has capital gains or any income not derived for the benefit of any particular beneficiary or it accumulates income till its beneficiaries, who are minors, attain majority or its wealth exceeds the aggregate value of the interests specifically assigned to the different beneficiaries, the trustee is subjected to the income tax or the wealth tax, as the case may be, regardless of the separate liabilities of the beneficiaries. See n. 105.
98. N.V. Shanmugam & Co. v CIT 81 ITR (1971) 310 (SC); CWT v Trustees of HEH Nizam's Family (Remainder Wealth) Trust (1977) 108 ITR 555 (SC). If there are several trustees engaged in a business they may have to be assessed as an association of persons, representing the individuals, Hindu undivided families or companies, as the case may be. under section 161 : CIT v Gangadhar Sikaria Family Trust (1983) 142 ITR 677 (Gauhati).
99. Trustees of Gordhandas Family Charity Trust v CIT (1968) 70 ITR 600 (Bom), affirmed in (1973) 88 ITR 47 (SC); G.T. Rajamannar v CIT (1964) 51 ITR 339 (Mys); J.N.A. Hobbs v Commr of Agl. IT (1963) 49 ITR 811 (Mys).
100. Nirmala Bala Sarkar v CIT (1969) 74 ITR 268, 275 (Cal); CIT v Trustees of the Trust Estate of Tarun Kumar Roy (1974) 94 ITR 361, 369 (Cal); Trustees of Putlibai R.F. Mulla Trust v CWT (1967) 66 ITR 653, 662 (Bom) : R.H. Pandit v CIT (1972) 83 ITR 136 (Bom).
101. CWT v Km. Manna G. Sarabhai (1972) 86 ITR 153 (Guj); CIT v Lady Ratanbai Mathuradas (1968) 67 ITR 504, 515 (Bom).
102. K.M. Sheth v CWT (1977) 107 ITR 45 (Bom); CWT v Ashok Kumar Ramanlal (1967) 63 ITR 133 (Guj); Rajesh Kanta Roy v Smt. Shanti Debi AIR 957 SC 255; Harrison v Grimwood (1849) 12 Beavan 192; Fox v Fox 23 W.R. 314.
103. Saldhana v CIT 6 ITC 114, 117 (FB-Mad.); Sahibuddin Ali Mohamed v CIT (1954) 25 ITR 237, 247 (Bom); CIT v Balwantrai Jethalal Vaidya (1958) 34 ITR 187 (Bom); CIT v Arvind Narottam (1969) 73 ITR 490, 497. This option is not available in respect of guardians or trustees of minors, lunatics or idiots who come under sec. 21 (3) of the Wealth-tax Act, though the reason for such differential treatment is not evident, vide Law Commission, *Twelfth Report*, p. 428.
104. Trustees of Chaturbhuj Raghavji Trust v CIT (1963) 50 ITR 693 (Bom).
105. CIT v Smt. Kasturba Walchand Trust (1967) 63 ITR 656 (SC), affirming (1964) 51 ITR 255 (Bom); Williams v Singer (1920) 7 TC 387; Reid's Trustees V IR 14 TC 512; Fry v Shiel's Trustees (1915) 6TC 583; Hamilton Russel's Executors v IR (1943) 25TC 200.
106. Mozley and Whiteley's Law Dictionary, 8th ed. p. 114; Snell's Principles of Equity, 25th ed., p. 129 (1965); Gartside v IR (1968) 70 ITR 663, 710, 719 and 720 (HL); IR v Holmden (1968) 1 All ER 148; Sainsbury v IR (1969) 3 All ER 919; Re. Weir's Settlement

Trust (1970) 1 All ER 297. It has been pointed out that *spes successionis* or the expectancy to succeed to the property of a living person, confers neither an actual nor even a contingent interest, liable to the estate duty. If the trust is "exhaustive", i.e., if the trustees are required to distribute the entire income to the beneficiaries, the beneficiaries can demand the payment of the fund to them, provided all of them are *sui juris* and the class of beneficiaries is also "closed" and cannot be modified by the trustees. Such demand has to be made collectively and not individually : Re. Smith (1928) All ER Rep 520. A *spes successionis* is distinguishable from a contingent interest : CWT v Ashok Kumar Ramanlal (1967) 63 ITR 133 (Guj) ; CWT v Anarkali Sarabhai (1971) 81 ITR 375 (Guj); CWT v N.D. Petit (1981) 128 ITR 650 (Bom) ; CWT v Kum. Manna Sarabhai (1972) 86 ITR 153 (Guj) ; CWT v Bhogilal Maganlal Shah (1968) 69 ITR 288 (Guj). It is pertinent to note that if the settlor is a potential beneficiary in a discretionary trust, the undistributed income of the trust can be deemed to be that of the settlor, in the UK : Sec 441 of the Income and Corporation Taxes Act, 1970.

107. Trustees of Chaturbhuj Raghavji Trust v CIT (1963) 50 ITR 693 (Bom).
108. Drummond v Collins (1915) 6TC 525 (HL) ; Lindus and Hortin v IR 17TC 442 ; Johnstone v Chamberlain 17 TC 706.
109. CWT v Trustees of HEH Nizam's Family (Remainder Wealth) Trust (1977) 108 ITR 555 (SC) ; CWT v Trustees of Mrs Hansabai Tribhuwandas Trust (1968) 69 ITR 527 (Bom) ; Padmavati Jaykrishna Trust v CWT (1966) 61 ITR 66, 81 (Guj) ; Court Receiver v CIT (1964) 54 ISR 189 (Bom) ; CWT v Trustee of HEH Nizam's Supplemental Family Trust (1968) 68 ITR 508 (AP) ; CWT v Administrator General of West Bengal (1971) 79 ITR 154 (Cal) ; Trustees of Putli Bai R.F. Mulla Trust v CWT (1967) 66 ITR 653 (Bom) ; Suhasini Karuri v WTO (1962) 46 ITR 953 (Cal) ; CWT v K.J. Somaiya Trust (1977) 109 ITR 798 (Bom) ; CWT v Waqf Syed Ahmed Hussain Rizvi (1979) 116 ITR 344 (All) : CIT v Puthiya Ponmani Chintakam Waqf (1962) 44 ITR 172 (SC) ; Habibur Rahman v CIT (1945) 13 ITR 189 (Pat). Where the beneficiaries are specified, but not their *inter se* shares, all of them may be taken to have equal shares, in which case their shares cannot be held to be indeterminate : Jogeshwar Narain Dev v Ramchand Dutt 23IA 37, (1896) ILR 23 Cal 670 (PC) ; CIT v Bhim Chandra Ghosh (1956) 30 ITR 46 (Cal) ; Visheshwar Singh v CIT (1951) 19 ITR 522 (Pat) ; Jyotishwari Kalimata v CIT (1946) 14 ITR 703 (Pat) ; CIT v Pulin Behari Dey (1951) 20 ITR 314 (Cal). The importance of the trust deed is brought out in the following cases : Arur v CIT (1945) 13 ITR 465 (Bom) ; B.P. Mahalaxmiwala v CIT (1954) 26 ITR 177 (Bom) ; Panchanan Das v CIT (1951) 20 ITR 75 (Cal) ; CIT v Arvind Narottam (1969) 73 ITR 490 (Guj).
110. GT Rajamannar v CIT (1964) 51 ITR 339 (Mys).

111. CWT v Purshottam Amarsay (1969) 71 ITR 108 (Bom) ; CWT v Kripashankar Dayashankar Worah (1971) 81 ITR 763 (SC) ; Suhasini Karuri v WTO (1962) 46 ITR 953 (Cal) ; Chintamani Ghosh Trust v CWT (1971) 80 ITR 331 (All). Also see n. 99 above.
112. CIT v Bhagwandas S Malvi (1977) 107 ITR 426 (Bom) ; CIT v Smt Kasturbai Walchand Trust (1964) 51 ITR 255 (Bom) affirmed in (1967) 63 ITR 656. Shares of beneficiaries were held to be indefinite and the trustees accordingly assessable at the maximum rate of income tax where the trustees were given the absolute discretion to accumulate income or use it for the benefit of any one or more of the beneficiaries to the exclusion of others in CIT v Lady Ratanbai Mathuradas and others (1968) 67 ITR 504 (Bom).
113. Parsons Stockley v Parsons (1890) 45 Ch. D 51 ; CWT v N.D. Petit (1981) 128 ITR 650 (Bom); CIT v Lady Ratanbai Mathuradas and others (1968) 67 ITR 504 (Bom).
114. Proviso to sec. 58 of the Indian Trusts Act : CIT v Nawab Mir Sarket Ali Khan Bahadur (1974) 97 ITR 246, 266 (SC).
115. N.V. Shanmugam & Co. v CIT (1971) 81 ITR 310 (SC) ; CWT v Trustees of Nizam's Family Remainder Wealth Trust (1977) 108 ITR 555 (SC) ; A.K. Gopalan Pillai v Agricultural ITO (1970) 75 ITR 120 (Mad) ; CIT v P. Krishna Warrier (1970) 75 ITR 154 (SC) ; K.K. Hamique v Member, Board of Agl. Income-tax (1966) 60 ITR 216 (SC); CIT v HEH Sir Osman Ali Bahadur (1966) 59 ITR 666, 682 (SC). The principle has also been applied to the case of a trustee who is remunerated by allotment of the agricultural income from a portion of the agricultural estate belonging to a trust : Mohammad Isa (Syed) v CIT (1942) 10 ITR 267 (All). Where, however, a *mutawalli* is appointed on a fixed salary, he is assessable to tax under the head "salary" despite the fact that the trust income is agricultural : Nawab Habibulla v CIT (1943) 11 ITR 295 (PC). The remuneration of a trustee fixed at 15 per cent of the estimated net income from agricultural properties held in trust for certain temples was also held to be liable to the income tax not being derived as rent or revenue of land : Maharajadhiraja Sir Kameshwar Singh v CIT Bihar and Orissa (1961) 41 ITR 169 (SC).
116. CWT v Official Trustee of West Bengal for Trust Murshidabad Estate (1982) 136 ITR 162 (Cal).
117. Harendra Kumar Roy's Estate v CIT (1944) 12 ITR 68 (Cal).
118. Hotz Trust v CIT (1930) 5 ITC 8 ; AIR 1930 Lah 929 ; Aikin v Macdonald's Trustees (1894) 3 TC 306 ; Reid's Trustees v IR (1929) 14 TC 512, 523 ; IR v Dewar 16 TC 84, 94, (HL) ; IR v Mc Intosh (1955) 36 TC 335.
119. Arundhati Balkrishna v CIT (1976) 102 ITR 356 (Guj).
120. Ganpatrai Sagarmal (Trustees) for Charity Fund v CIT (1963) 47 ITR 625 (Cal) ; Ganpatrai Sagarmal v CIT (1982) 138 ITR 294 (Cal).
121. Shri Jyotishwari Kali Mata v CIT (1946) 14 ITR 703 (Pat.) ; Neliyil Ummer Kutty v State of Kerala (1970) 77 ITR 489 (Ker).

122. Dwarkadas Bhimji v CIT (1948) 16 ITR 160 (Bom).
123. CIT v M. Jamal Mohammad Sahib (1941) 9 ITR 375 (Mad FB); Ramibai Agarwal v Baldeoraj 1977 (1) MPWN 123- See also p. 13.
124. ITAT v Managing Trustee Sree Radha Madho Trust (1946) 14 ITR 470 (Nag); Re. Lokmanya Tilak Jubilee National Trust Fund (1942) 10 ITR 26 (Bom).
125. Addl. CIT v Sherwani Charitable Trust (1975) 99 ITR 284 (All); Hakim Abdul Hamid v CIT (1973) 90 ITR 203 (Del) (F B). These cases related to the provisions of the 1922 Act, but the position has not altered, so far as actual expenditure is concerned.
126. A deity in a private *debuttar* estate is assessable to tax in the status of an "individual" : Sri Sri Sridhar Jiew v ITO (1963) 50 ITR 480 (Cal.); Jogendar Nath Naskar v CIT (1969) 74 ITR 33 (SC) ; Official Trustee of West Bengal v CIT (1968) 67 ITR 218 (Cal); (1974) 93 ITR 348 (SC); Sri Bhagwan Radha Krishna Ji v CIT (1962) 46 ITR 741 (All). An endowment may fail for uncertainty if the donor does not instal or even name or specify any particular idol, but a gift for building a temple to the formless and absolute *Brahman* would not be void : Veluswami v Dandapani ILR (1947) Mad 47 ; Phundanlal v Arya Pratinidhi Sabha ILR 30 All 793; Chandi Charam Mitra v Hariboladas 1919 ILR 46 Cal 951. A Hindu image irrespective of whether it is permanent or is immersed in a river after a festival, has been recognised by the courts as capable of suing and being sued : Purna Chandra v Kalipada Roy AIR 1942 Cal 386. Property which is dedicated to it vests in it. Its interests are attended to by its *shebait*, i.e., its human ministrant, who enjoys the same powers as the manager of an infant heir and is competent to file tax-returns on its behalf: Pramatha Nath Mullick v Pradyumna Kumar Mullick (1925) LR 52, IA 245 ; Jagadindranath Roy v Rani Hemantha Kumari Devi LR 31 IA 203 ; Sri Sri Sridhar Jiew v ITO (1963) 50 ITR 480 (Cal). A gift may be made on behalf of one deity to another : Bhupatinath v Ramlal ILR 37 Cal 128. However, it is a moot point whether such a gift will be liable to the gift tax.
127. Sree Sree Iswar Gopal Jew v CIT (1950) 18 ITR 743 ; Official Trustee of West Bengal v CIT (1968) 67 ITR 218 (Cal) ; Jogendar Nath Naskar and Hemchandra Naskar (decd) *shebaits* of Sri Sri Kubeswar Madhav v CIT (1969) 74 ITR 33 (SC). The Supreme Court has outlined the principles governing dedication in S. Shanmugam Pillai v K. Shanmugam Pillai AIR 1972 SC 2069. For determining whether an endowment is fictitious or real, see Ramratanlal v Kashinath Tewari AIR 1966 Pat 235 ; Shri Thakurji v Sukhdeo ILR 42 All 295 (F B).
128. CIT v Sri Jagannath Jiew (1977) 107 ITR 9 (SC) ; Trustee to the Debuttar Estate of Sri Iswar Radha Govind Jiew v CIT (1972) 84 ITR 150 (All).
129. CWT v H H Sri Rama Varma Maharaja of Travancore (1975) 100 ITR 91 (Ker).

130. CIT v Kokila Devi (1970) 77 ITR 350 (SC); CIT v Trustees of the Trust Estate of Tarun Kumar Roy (1974) 94 ITR 361 (Cal); Official Trustee of West Bengal v CIT (1974) 93 ITR 348 (SC); CIT v Uma Maheswari, through *shebait barat* (1969) 71 ITR 614 (Pat); Sri Sri Sridhar Jiew v ITO (1963) 50 ITR 480 (Cal); Sri Sri Sridhar Jiew v ITO (1967) 63 ITR 192 (Cal) ; CIT v Pulin Behari Dey (1951) 20 ITR 314 (Cal).
131. CIT v Official Trustee of West Bengal for the Estate of Smt. Chitra Dessi (1981) 7 Taxman 109 (Cal) (1981) 23 CTR (Cal) 276.
132. Panchanan Das v CIT (1951) 20 ITR 57 (Cal); Bankim Chandra Dutta v CIT (1966) 62 ITR 239 (Cal).
133. CIT v Pulin Behari Dey (1951) 20 ITR 314 (Cal); CIT v Ashalata Devi (1951) 20 ITR 326 (Cal); CIT v Bhimchandra Ghosh (1956) 30 ITR 46 (Cal) ; Sri Jyotishwari Kalmata v CIT (1946) 14 ITR 703 (Pat) ; Raja Bahadur Visheshwar Singh v CIT (1951) 19 ITR 522 (Pat) doubting the correctness of the view in 14 ITR 703 (Pat.) Gopi v Musamat Jaldhara (1911) ILR 33 All 41 : Jogeshwar Narain Deo v Ramchandra Dutt (1896) ILR 23 Cal 670. For a case in which there was only one deity as beneficiary : CIT v Kokila Devi (1970) 77 ITR 350 (SC).
134. N.C. Sen and B.C. Sen v ITO (1964) 51 ITR 218 where the Court negatived the objection of the trustees that the certificate issued by the Income Tax Officer to the Certificate Officer for recovery of the tax outstanding against the deity did not show them as trustees but made it appear that taxes were due from them and was, therefore, invalid.
135. Hamid Hussain v CED (1972) 83 ITR 309 (All); Khatizabai Mohamed Ibrahim v CED (1959) 37 ITR (ED) 53 (Bom).
136. Janabal Sardar v Sabiha Khatun AIR 1938 Cal 257 ; Abdul Sattar v Advocate-General AIR 1933 Bom 87 ; Habib Ashraff v Syed Wajihuddin AIR 1933 Oudh 222 ; Pathukutti v Avathalakutti (1890) 13 Mad 66 ; Mohamed Safi v Khadim Ali AIR 1944 Oudh 291 ; Commissioner of Waqfs, West Bengal v Haji Rashid Ali Dina AIR 1958 Cal 413.
137. CIT v Hassan Koya (1967) 63 ITR 791 (Ker); Ahmed G.H. Ariff v CWT (1970) 76 ITR 471 (SC) ; CWT v Smt. Rani Kaniz Abid (1974) 93 ITR 332 (All) ; Sri Vidya Varuthi Thirtha Swamigal v Baluswami Ayyar AIR 1922 PC 123.
138. M. Habibur Rahman v CIT (1945) 13 ITR 189 (Pat) where the settlor's family and all his descendants were to share the *waqf* income concurrently and in equal shares. The court held that it was not a discretionary trust. Also, Mohd. Ishaq v CIT (1951) 19 ITR 70 (All); Neilliyil Ummer Kutty v State of Kerala (1970) 77 ITR 489 (Ker); Abdul Jalil Khan v Agl. IT Board (1958) 34 ITR 421 (All); CIT v Sir Muhammad Yusuf Ismail (1944) 12 ITR 8 (Bom), approved in Col. H.H. Raja Sir Harinder Singh v CIT (1972) 83 ITR 416 (SC).

139. CIT v Managing Trustees, Nagore Durgah (1965) 57 ITR 321 (SC), affirming (1954) 26 ITR 805 (Mad).
140. CWT v Puthiya Ponmani Chintakam Waqf (1967) 63 ITR 787 (Ker) ; CWT v Begum Hashmat Bai (1970) 77 ITR 581 (MP) ; Umar Baksh v CIT AIR 1931 Lah 578 ; 5 ITC 402 ; CIT v Sir Muhammad Yusuf Ismail (1944) 12 ITR 8 (Bom) ; CIT v Aga Abbas Ali Shirazi (1944) 12 ITR 179 (Mad) ; Nelliyil Ummer Kutty v State of Kerala (1970) 77 ITR 489 (Ker) ; CIT v Abubakar Abdul Rahman (1939) 7 ITR 139 (Bom) ; CIT v Ibrahim Hakimji (1940) 8 ITR 501 (Sind) ; CIT v Jamal Mohamad Sahib (1941) 9 ITR 375 (Mad-FB) ; CIT v Karim Brothers Charity Fund (1943) 11 ITR 603 (Bom) ; Mohammed Ishaq CIT (1951) 19 ITR 70 (All) ; CIT v P.P. Hassan Koya (1967) 63 ITR 791 (Ker) ; CIT v Humayum Raza AIR 1936 Pat 532 ; Nawab Bahadur of Murshidabad v CIT (1955) 28 ITR 510 (Cal).
141. CWT v Waqf K.B. Syed Ahmed Hussain Rizvi (1979) 116 ITR 344 (All).
142. Section 160(1)(iv) of the Income-tax Act : CIT v Puthiya Ponmani Chintakam Waqf (1962) 44 ITR 172 (SC). But where a *waqf* had come into existence for the maintenance of a mosque out of the income from some lands, and the maintenance of the male descendants of the grantee out of the balance income, it was the *mutawalli's* duty to see that all the descendants got the benefit of the usufruct by the application of the per capita rule. No income accrued to the *mutawalli* and only his proportionate interest in the property would pass on his death : CED v S.M. Kamaluddin Fakri (1980) 124 ITR 98 (Mad).
143. CIT v Puthiya Ponmani Chintakam Waqf (1962) 44 ITR 172 (SC) ; Hoosein Kassam Dada v CIT (1937) 5 ITR 182 (Cal) ; Mohammad Ishaq v CIT (1951) 19 ITR 70 (All) ; CWT v Puthiya Ponmani Chintakam Waqf (1967) 63 ITR 787 (Ker) ; CIT v P.P. Hassan Koya (1967) 63 ITR 791 (Ker).
144. Sec. 164(2) of the Income-tax Act. The corresponding provision for assessment of the wealth tax in case of diversion of property or of income from property held under trust for public charitable or religious purposes is in sec. 21A of the Wealth-tax Act, 1957. For wealth tax levy, the trust is treated like an individual.
145. A 'body of individuals' indicates a combination of individuals who have unity of interest but not a common design, e.g., trustees of a trust or the executors of an estate : M/s Deccan Wine & General Stores v CIT (1977) 106 ITR 111 (AP) ; Meera & Co. v CIT (1979) 120 ITR 564 (Punj) ; CIT v Harivadan Tribhuwandas (1977) 106 ITR 494, 503 (Guj) ; CIT v Deghamwala Estates (1980) 121 ITR 684 (Mad) ; CIT v T.V. Suresh Chandran (1980) 121 ITR 985, 995 (Ker). An association of persons connotes not only unity of purpose but common action. An association of "persons" implies also a wider group than a body of "individuals" since a "person" can include a company, etc. : CIT v Indira Balkrishna (1960) 39 ITR 546, 551 (SC) ;

CIT v N.V. Shanmugam & Co., (1966) 62 ITR 701 (Mad) affirmed in (1971) 81 ITR 310 (SC). Trustees can operate as an association of persons : CIT v Ibrahimji Hakimji (1940) 8 ITR 501 (Sind). There is deemed to be an association of persons in the circumstances covered by sub-secs. (2) and 3(a) and the provisos to sub-secs. (1) and (3)(a) of sec. 164, despite there being strictly no "association" in terms of sec. 2(3) : Smt. Santimoyee Bose v CIT (1969) 74 ITR 133, 137 (Cal). For wealth-tax assessment a group of trustees will have to be treated as an "individual" in respect of the wealth held by them and not as an association of persons : Abhay L. Khatau v CWT (1965) 57 ITR 202 (Bom) ; Suhasini Karuri v WTO (1962) 46 ITR 953 (Cal).

146. Ahmad G.H. Ariff v CWT (1970) 76 ITR 471 (SC) ; Purshottam N. Amarsay v CWT (1973) 88 ITR 417 (SC).

147. CWT v Trustees of HEH Nizam's Family (Remainder Wealth) Trust (1977) 108 ITR 555 (SC) ; CWT v Trustees of the Estate of V.R. Chetty Brothers (1979) 120 ITR 329 (Mad).

148. CWT v Kripashankar Dayashanker Worah (1971) 81 ITR 763 (SC) ; Chintamani Ghosh v CWT (1971) 80 ITR 331 (All) ; Abhay Khatau v CWT (1965) 57 ITR 202 (Bom), affirmed in (1973) 88 ITR 47 (SC) ; Trustees of Gordhandas Govindram Family Charity Trust v CWT (1968) 70 ITR 600 (Bom), affirmed in (1973) 88 ITR 47 (SC) ; Currimbhoy Ebrahim Baronetcy Trust v CIT 5 ITC 484 (Bom), affirmed in (1934) 2 ITR 148 (PC) ; C.R. Nagappa v CIT (1969) 73 ITR 626 (SC) affirming (1968) 67 ITR 740 (Mys) ; Suhasini Karuri and another v WTO Calcutta and another (1962) 46 ITR 953 (Cal); Vedakannu Nadar v N.T.S. Annadhana Chatram AIR 1938 Mad 982 ; Shri Mahadeo Jew v Balkrishna Vyas AIR 1952 Cal 763 ; Lewin on Trusts, 14th ed., p. 196.

149. See 21 (1A) inserted in the Wealth-tax Act by the Finance (No. 2) Act, 1980 with effect from April 1, 1980. See also p. 38ff above.

150. CWT v Trustees of HEH the Nizam's Miscellaneous Trust (1980) 126 ITR 233 (AP) ; CWT v Kripashankar Dayashankar Worah (1971) 81 ITR 763 (SC) ; CWT v Arvind Narottam (1976) 102 ITR 232 (Guj) ; CWT v Administrator General of West Bengal (1971) 79 ITR 154 (Cal) ; Prince Ranjit Singh P. Gaekwad v CWT (1969) 73 ITR 206 (Guj).

151. CWT v Harshad Rambhai Patel (1964) 54 ITR 740 (Guj).

152. CED v John D'Souza (1974) 95 ITR 460 (Ker).

153. CED v John D'Souza (1974) 95 ITR 460 (Ker) ; CED v The Estate of the late Mrs. Oakshott (1977) 106 ITR 126 (Mad). In this case, the deceased was entitled to receive only the residual income from dividends on shares of an Indian company held in a trust created by her husband domiciled in the UK. The Court held that there was no liability to duty on the death of the lady, since she was not interested in any of the shares, her right being limited to the residuary income of the estate.

154. Shakuntala Banerjee v CED (1980) 125 ITR 488 (All); CED v Hussainbhai Mohamedbhai Badri (1973) 90 ITR 146 (SC).
155. CED v Bai Suntokbai Damodar Govindji (1981) 132 ITR 6; Manian Natesan v CED (1965) 56 ITR (ED) 5 (Mad); CED v Jameela Begum (1975) 101 ITR 165 (Mad).
156. Mahendra Ram Bhai Patel v CED (1967) 63 ITR 645 (SC). No interest will cease on the death of a husband where a house has been transferred by his wife to a trust to be held for her life to the benefit of both and the settlement in his favour lapses if he predeceases her. An interest contingent upon the donee's surviving the life-tenant is not capable of measurement under sec. 40 of the Estate Duty Act: CED v State Bank of India (1981) 131 ITR 700 (Mad).
157. T.A. Devaki Ammal v CED (1978) 111 ITR 403 (Mad).
158. Badri Vishal Tandon v CED (1982) 136 ITR 426 (All).
159. Official Trustee of Bombay v CED (1979) 117 ITR 190 (Bom).
160. Where one of the grand-daughters of the settlor was entitled to certain benefits from the settled funds during his wife's life-time, and the income became fully payable to his grand-daughter on his wife's death, no duty was held to be leviable on the value of the settled property on the wife's death: CED v Trustees HEH The Nizam's Jamily Pocket Money Trust (1973) 87 ITR 33 (AP). But where the income of the trust was required to be spent on the widow of the deceased, her sons and their families during her life-time, and the property vested in the two sons equally and they became entitled to the beneficial enjoyment of the full income after her death, the property was held to be liable to the duty: CED v Govindji Jethabai Virjee (1978) 115 ITR 664 (Bom).
161. CED v Govindji Jethabai Virji (1978) 115 ITR 664 (Bom).
162. Suhasini Karuri & Another v WTO Calcutta & Another (1962) 46 ITR 953 (Cal); Gour Chandra Das v Smt Monmohini Dasi AIR 1921 Cal; Sarnath Sanyal Hrishikesh Sanyal AIR 1949 All 93; Estate of Lala Shankar Shah v CIT (1945) 13 ITR 500, 509, 510 (Lah). A testator may create trusts by his will and appoint his executors as trustees to carry out the trusts: Estate of J.K. Dubash v CIT (1948) 16 ITR 90 (Bom), approved in (1951) 19 ITR 182 (SC).
163. CIT Madras v Sri T.P. Ramaswami Pillai (1962) 46 ITR 666 (Mad); Raghavalu Naidu and Sons v CIT (1950) 18 ITR 787 (Mad); Court Receiver v CIT (1964) 54 ITR 189 (Bom); K.P. Narayanan v CIT (1975) 98 ITR 130, 140, 141 (Ker); Rev. Lionel Corbett v IR (1937) 4 All ER 700 (CA); IR v Smith (1930) 1 KB; 15 TC 661, 668; Carlish v IR (1958) 38 TC 37, 63.
164. Amal Kumar Chakraborty v CED 1976 Tax LR 62 (Cal).
165. CIT v Estate of V. L. Ethiraj (1979) 120 ITR 271 Mad).
166. P Gangadharan Pillai v CED (1968) 70 ITR 640 (Ker); Sneddon v Lord Advocate (1954) 25 ITR (ED) 6; CIT v Prahlad Rai (1972) 83 ITR 321; Mrs. Monie Ardeshir Baria & Mrs. Piloo F. Antia v CED

(1977) 106 ITR 203 (Bom); Smt. Gunwantibai v CED (1981) 130 ITR 122 (MP).

167. Baidyanath Banerjee v ACED (1965) 35 ITR (ED) 31 (Cal).

168. But see Deokinandan Khetan v CED (1968) 69 ITR 801 (All), where it was established that the income from endowed property and also the expenses relating to it were accounted for in the trust-books though the property stood in the name of the deceased long after his death. The court held that no other document was necessary for an endowment. In CED v Usha Kumar (1980) 121 ITR 735 (SC) it has been held that a partial dedication for religious purposes may have the effect that the properties endowed become subject to a charge for a religious purpose. Though they may retain their private and secular character, there may be no liability for the estate duty on the relevant portion of the property in such a case.

169. Smt Pan Kumari Kochar v CED (1969) 73 ITR 373 (AP). Transfer of funds in the books of the joint family to a separate trust account in accordance with the instructions of the *Karta's* wife, to whom the funds belonged is evidence of the creation of the trust : Jai Narayan Jai Govind v CED (1963) 49 ITR (ED) 105 (Mad).

170. CED v Estate of Late Sri E.M. Gopala Krishna Kone (1981) 129 ITR 738 (Mad) ; Khatizabai Mohd. Ibrahim v CED (1959) 37 ITR (ED) 53 (Bom); Ravindra Gunvantlal v CED (1969) 74 ITR 498 (Guj). The English cases on this point are discussed at length in this case by the Bombay High Court. The concept of mutually exclusive categories—property actually passing and property deemed to pass—as stated in the celebrated dictum of Lord Macnaghten in the case of Earl Cowley v IR (1899) AC 198 was held to be not relevant in the context of the provisions of the Estate Duty Act in India. The English law on "reserved interest" is analogous : Attorney General v Grey (1898) 1 QB 318 ; Cochrane, Cochrane & another v Turner (1945) CL 285. Where a number of properties had been settled in trust for running a school, it was held that each property had to be considered separately for the purpose of the exclusion of the settlor. If he held the right to residence in only one of the properties, his death would result in the "passing" of that property alone. Where, however, the settlor had reserved for himself a maintenance allowance out of funds of the school run by the trust, all the properties held by the trust would be deemed to pass on his death : K.C. Srivastava v CED (1979) 117 ITR 221 (All); Clifford John Chick v Commissioner of Stamp Duties (1959) 37 ITR (ED) 89 (PC) ; CED v Smt Parvathi Ammal (1974) 97 ITR 621 (SC) ; George Da Costa v CED (1967) 63 ITR 497 (SC) ; Norman Clyde Oakes v Commissioner of Stamp Duties of New South Wales (1954) 26 ITR ED 1 (PL) ; V.S. Mani v CED (1966) 60 ITR 810 (Mad) ; Rashmohan Chatterjee v CED (1964) 52 ITR (ED) 1 (Cal). The mere fact that the settlor resides with his wife in one of the settled properties

will not imply the reservation of interest in his favour : CED v Nirmal Kumar Roy (1981) 128 ITR 593 (Cal).

171. Kikabai Shamsuddin v CED (1969) 73 ITR 241 (Guj).

172. Gajra Bai v CED (1972) 86 ITR 92 (Mys).

173. CED v R. Kanakasabai (1973) 89 ITR 251 (SC).

174. CED v K.A. Kader (1974) 96 ITR 289 (Mad).

175. Official Trustee of Bombay v CED (1979) 117 ITR 190 (Bom).

176. Pran Kishan Das v CED (1968) 69 ITR 139 (Cal) ; Usha Kumar Banerjee v CED (1972) 84 ITR 6 reversed by the SC on other grounds in CED v Usha Kumar (1980) 121 ITR 735 (SC). The *shebait's* apanage which is usually heritable but not alienable, is liable also to the wealth tax. But the mere right to reside in a portion of the property dedicated to a deity which may be appurtenant to the duties that the *shebait* has to perform does not pass on his death : Satyanarain Bagla v CED (1982) 133 ITR 710 (Cal.).

177. Mahanth Umesh Narain Puri v CED (1982) 135 ITR 139 (SC), affirming (1970) 75 ITR 310 (Pat) ; Public Trustee v IR (1958) 2 All ER 720 affirmed in (1960) 1 All ER 1 ; (1959) 37 ITR ED 32, and (1961) 43 ITR Suppl. 19. While there is no estate duty liability on the death of a *mahanth*, the *mahanth* is subjected to the income tax on the income of the estate : Mahanth Ramswaroop Das v State of Bihar (1961) 42 ITR 770 (SC), affirming (1956) 30 ITR 640 (Pat), where the issue was liability to Bihar agricultural income tax. The *mahanth* is also entitled to protection of his "mahantship" which contains elements of office and property, under article 19(1) of the Constitution : Commissioner, Hindu Religious Endowments v Shri Lakshmindra Thirtha Swamiyar of Shirur Mutt (1954) SCR 1005 ; AIR 1954 SC 282.

178. Khatizabai Mohamed Ibrahim v CED (1959) 37 ITR (ED) 53 (Bom).

179. Hamid Hussain v CED (1972) 83 ITR 309 (All) ; Mohamed Hussain Sait v CED (1979) 117 ITR 654 (Mad).

180. Hamid Hussain v CED (1972) 83 ITR 309 (All).

181. CED v Sultan Alam Khan (1976) 116 ITR 360 (Bom).

182. CED v Hussainbai Mohamed Bai Badri (1973) 90 ITR 146 (SC) ; CED v S. M. Kamaluddin Fakri (1980) 124 ITR 98 (Mad).

183. Sitanath Mukherjee v CED (1968) 70 ITR 53 (Cal). Even where possession of settled property has been postponed till the death of the trustees, the property does not pass on the death of the trustee ; CED v H.N. Markandan (1974) 94 ITR 144 (Mad).

184. Ravindra Gunvantlal v CED (1969) 74 ITR 498 (Guj).

185. Mohindra Nath Mukherjee v ACED (1982) 11 Taxman 161 (Cal).

186. State Bank of India v CED (1968) 69 ITR 270 (P & H).
187. CED v Bhagwandas Valji Joshi (1981) 6 Taxman 202 (Bom), (1983) 139 ITR 316 (Bom).
188. CED v Mrs. Sushila Umedlal Zaveri and others (1982) 135 ITR 727 (Bom).
189. CED v Usha Kumar Banerjee (1980) 121 ITR 735 (SC).
190. Ravindra Gunvantlal v CED (1969) 74 ITR 498 (Guj).

4

The Law and Practice in Other Countries

SINCE private trusts originated in the UK, it will be useful to compare their interaction with taxation in that country with the Indian experience. The doctrine of separate equitable and legal interests in the same estate preceded the income tax by centuries in the UK, unlike India where they were introduced at about the same time. It is, therefore, obvious that trusts had grown in the UK out of genuine needs that had little to do with taxation. It was only with their increasing involvement in tax avoidance exercises, that family settlements came to acquire an unsavoury reputation. It is difficult to say whether the high rates of tax drove the taxpayers to devise ingenious financial arrangements or the high rates were the consequence, partly or wholly, of the large-scale tax avoidance and evasion with which the United Kingdom has been vexed as much as India. The truth is probably that the damage was mutual, the contribution of sheer cupidity being no less than that of the frustration and despair caused by an unrealistic tax burden.

Conceived at the beginning of its development as a means of getting over the legal prohibition on alienation of property, a settlement in trust turned out to be a convenient, ready-made shelter for conserving income and consolidating property, without being exposed to the onslaughts of the Revenue. The earlier provisions of the income-tax legislation aimed at over-taking and circumventing the efforts made by the taxpayer for the disposal of his property in such a manner that the income from it was not received by him though he retained certain

powers over it or over the income : the efforts were foiled by holding that the income of which the taxpayer tried to disembarrass himself was his income for tax purposes. But as the Meade Committee has pointed out, no effort has been made in the UK to harmonise the treatment of trusts in the taxes introduced from time to time.[1]

The treatment of disposition of income and property in the UK is broadly similar to that prevalent in India. Income from revocable or determinable settlements and those in which the settlor retains an interest is deemed to be that of the settlor. Dispositions which do not last beyond six years are taken to be revocable.[2] The income is assumed to be the topmost slice of the taxpayer's income and liable accordingly to tax at the highest marginal rate appropriate to it. When the settlor retains interest in a settlement made by him, any income which is not distributed is held to be the income of the settlor from the property comprised in the settlement.[3] If the settlement provides for the payment or application of the whole or any part of the income arising from the property covered by it, for the benefit of the settlor or the spouse of the settlor, under a power exercisable at the settlor's discretion, the income is attributed to the settlor.[4] It is immaterial that in fact the income is paid to or applied for some other person. The mere existence of the discretionary power brings the provision into operation.[5] Even capital sums paid to the settlor or the settlor's spouse may be treated as the settlor's income upto the amount of the trust's undistributed income, especially if they reached the settlor[6].

Payments made through settlements, on divorce or annulment of marriage or legal separation or agreement to live apart, are not liable to tax in the hands of the settlor if the settlement is required to be made by a court order. Income from trusts in favour of unmarried children below the age of 18 will be includible in the income of the creators of the trusts, unless they have been set up under court orders. The term "children" includes step-children, adopted children and illegitimate children. Settlements for the children of others or for grand-children of the settlor are not hit, unless there are reciprocal arrangements. Cross settlements, e.g., by two

brothers simultaneously for each other's children, will be taken to constitute a single arrangement and treated as parts of one deed.[7] Income derived from investments made out of payments taxed to the settlor will not be included in the settlor's income.[8] Capital sums and loans received by the settlor from a settlement or a connected body corporate are taken as the income of the settlor to the extent that the settlement has available or undistributed income.[9]

Trustees of a trust are liable to tax in their representative capacity, in accordance with the schedule relevant to the income which they are receiving. The income tax is payable at the basic rate, with an additional 15 per cent charge on the income of discretionary and accumulation trusts. The total tax worked out to 48 per cent in 1978-79 and 45 per cent in 1980-81. The income of the trust attributable to the beneficiary's vested interest in it, is included in his total income, whether or not he has actually received it, the tax paid by the trustees being treated as tax paid by him against this income.[10] Expenses incurred by the trustees of a trust are not deductible from the income computed for tax purposes, but other reliefs for which the income tax law provides will be admissible, as in the case of any other taxpayer. The trust expenses are deductible, however, in computing the income of the beneficiary in the sense that the beneficiary is taxed only on his receipts, as grossed up for the taxes paid thereon.[11] Most trust income is investment income from which tax is withheld at source. Where a business is conducted by a trustee, the income is treated in his hand as unearned income, unless he is himself a beneficiary.[12]

A trustee is not the agent of a beneficiary, except where the beneficiary is incapacitated. He is directly taxed because he is in receipt and control of the income. Even if there is only one beneficiary and he is also *sui juris*, the trustee is assessed to tax for this reason. Any distribution made by a trust will be treated as distribution of income upto the amount of the undistributed income of the trust.[13]

Trustees of a settlement are a single, continuing body, though the persons who happen to be trustees may change from time to time. They will be ordinarily resident in the

UK, unless the trust is administered abroad and the majority of the trustees are not resident in the UK. A resident beneficiary entitled to any income from a trust which has non-resident trustees can be assessed to tax on the trust income : even if he receives a capital payment, he can be taxed on the income of the trustees. Trust management can be done as a business, e.g., by corporate trustees.

Income accruing directly to the beneficiary is taxed in his hands without involving the trust.[14] Annuity payments out of the capital of the trust are the beneficiary's income, whatever their description may be in the trust instrument.[15] In certain situations the income taxed to the beneficiaries may exceed the income of the trust. When beneficiaries are exempt from tax, the trustee may not be charged to tax, on application by them to the revenue authorities.

Discretionary and accumulation trusts have been object lessons in tax avoidance in the UK as in India. As far back as 1965, GSA. Wheatcraft observed that "in Great Britain, it is probably true to say that 95 per cent of all discretionary and accumulation trusts are created solely for tax-saving reasons."[16] Estimates of the value of property settled on discretionary trusts have ranged from £ 200 million by Revell in 1961 to £ 1000 million assumed by Lyddall and Tipping in 1954.[17] However, discretionary trusts have been shorn of most of their attraction by the Finance Act, 1969, the Finance Act, 1970, and the Capital Transfer Tax Act, 1975, and the sharp increase in the rates of tax applicable to them, including income surcharge of 15 per cent.[18]

What had made discretionary and accumulation trusts more popular than specific trusts was that the former did not give the beneficiaries an interest in possession.[19] Where the trustee had also the power to accumulate the income, the beneficiaries could not be taken to have an interest in possession in the settled property, whether the trustee decided to accumulate the income or refrained from doing so. The interest could not go in and out of possession, depending on the trustees' uncertain decisions.[20] Discretionary and accumulation trusts served to reduce the high voltage of tax to which the beneficiaries would have been exposed if they had an

immediate right to enjoy an interest or claim the whole or part of the income from a property in the hands of the trustees. Compulsory accumulation of income under a will or a settlement till the occurrence of a contingency, say. the beneficiary's reaching a certain age or marrying, secured not merely a tax deferral but also conversion of the accumulated income into capital for the beneficiary.[21]

Trust property came within the estate duty charge in the UK between 1894 and 1914. A life-estate was taxed at 1 per cent in the initial stages, and later at 2 per cent, before its aggregation with the separate property of the deceased from 1914.[22] The Finance Acts provided for some of the contingencies affecting trusts and also dealt with the possibility of avoidance of duty through dispositions of shares in controlled companies. While control of a company which a person had in a fiduciary capacity was disregarded for the purpose of levy of duty on his death, it would assume significance if he was the sole trustee of his own funds, settled on his family. Where the directors of a company did not have a controlling interest in it, in their own right, they were held to exercise control if they held enough shares as trustees, to make up the balance of power required for the purpose.[23] It was not, however, towards company control so much as the discretionary trust that the ingenuity of the tax-planners was directed. Since no property passed on the death of a "discretionary" beneficiary and there was no new trust for a new group of persons with new qualifications,[24] discretionary trusts offered an easy method of escaping estate duty. Section 36 of the Finance Act, 1969, and section 31 of the Finance Act, 1970, countered it by providing that estate duty should be paid on the death of such a beneficiary on the same proportion of the trust property as the proportion that the deceased had received of the trust income during the seven years before his death.[25] The Capital Transfer Tax, which came into force in 1975 and which is charged whenever an interest in possession terminates or is deemed to have terminated, whatever the duration of the interest might have been, went further. A discretionary trust is liable to pay the tax every ten years as if 30 per cent of its capital has been transferred even if no transfer has actually

been effected. Credit will, however, be available for all the tax so borne when any distribution is in fact made and the tax liability is determined with reference to the distribution. If a settlement made by a domicile in the UK is not locally administered and the majority of the trustees are abroad, there will be an annual charge at 3 per cent on the capital deemed to have been distributed. This annual levy will be available as a credit against the tax payable in any subsequent distribution, including the tax raised on 10-yearly basis. This amounts to collection of the 10-yearly charge in annual instalments. It remains to be seen whether this periodic charge will render discretionary trusts prohibitive and totally uninteresting, as apprehended by a section of the taxpaying public. It has been pointed out in this connection, that it may not be equitable to assess the trusts at relatively high rates even when the rates are likely to be low if the income is to be taxed in the hands of the beneficiaries.

As a result of the increasing fiscal attack on discretionary trusts, accumulation and maintenance settlements which have been receiving a treatment which is less harsh, are reported to be coming up in large numbers. Accumulation trusts become attractive, particularly when they are transferred to or created in one of the tax havens.[26] If an accumulation trust is set up and it has all its assets in a low tax country, there is still scope for considerable reduction of tax liability.[27]

Canada

It is a curious fact that private trusts have been thriving better in the English-speaking countries than elsewhere. In Canada, for instance, trusts have been found to be used primarily by the wealthy and their efforts are directed to avoidance of succession duties on the "inter-generational transfers" of property.[28] Spouse trusts lost their importance with the trend towards the repeal of the provincial succession duties. Tax planners have concentrated in the recent years on more sophisticated channels for reducing tax liability, like trusts controlling corporations, trusts for the benefit of private quasi-charitable foundations, partnership of trusts which distribute their assets to their beneficiaries after winding up the

partnership, etc. The Minister has been statutorily vested with the discretion to treat multiple trusts as a single trust where the corpus has come from one individual and the income of all the trusts will be ultimately enjoyed by the same beneficiary or group or class of beneficiaries.[29]

The Carter Commission[30] went into the functioning of trusts in some detail, and the recommendations made by it included the conferment of an option to the beneficiary to pay tax directly on the income distributed by a trust and the treatment of the initial tax paid by the trust as withholding tax, credit being available to the beneficiary ; no election is possible in a discretionary trust in which the prospective beneficiary is not identifiable. The Commission pointed out that there appeared to be a definite correlation between the size of estates and the use of the trusts : as income and wealth increased, there was a greater flexibility in the mode and timing of gifts. There would ordinarily be no gift tax on reversion, unless the reversion occurred by reason of the release or renunciation of the interest by an intended donee, in which case there would be a completed gift and a gift-back to the original settlor. The Commission was of the view that every trust should file returns of income realised by it or accruing to it, but the ultimate burden of tax on the beneficiaries would be measured by their own ability to pay : the trustees' liability to pay tax would obviously have to be limited to the assets under their control. The Commission considered also various problems incidental to the assessment of trusts, e.g., accumulated income, distribution of capital, carry-forward of losses incurred by a trust, multiple trusts and the possibility of aggregation of income, trusts as tools for income-splitting, etc. As for the residence of trusts, the Commission suggested that a trust should be taxed as a Canadian resident where the majority of the trustees were resident in Canada or where most of the business of a trust was carried on or substantially all of its property was situated in Canada.[31]

Australia

The provisions of the Australian law are broadly similar. Assessment of a beneficiary is made on the basis of his present

entitlement to any interest in the income of a trust. As in the UK discretionary trusts, in which one has only a right to be considered for grant of a benefit by the trustees and one cannot therefore be taken to enjoy an interest of any value, have provided considerable scope for death-duty avoidance. The interest of a deceased in a discretionary trust which continues after his death is not a part of the estate of the deceased. Death duty is also avoided by a settlement expressed to operate upto a specified date calculated to fall a short while after the death of the deceased.[32] It has been held that the settlement does not take effect on the death but on a predetermined date ; and the considerations which have weighed with the settlor in fixing the date are of no relevance in this connection.

Until 1964, income accumulating in a trust was taxed as if it were the income of an individual. Thereafter, an alternative was prescribed by way of tax at a flat rate which was 50 per cent in 1975, in order to discourage tax avoidance practices. The Taxation Review Committee, known as the Asprey Committee,[33] has recommended that the rate of levy on income taxed to a trust should, in general, be the maximum marginal rate applicable to an individual taxpayer. This was expected to operate as a disincentive to the creation of accumulation trusts having tax avoidance as their object.

The United States

Under the law in 1913, trusts in the United States were treated as merely agents of the beneficiaries. The tax was assessed to the beneficiaries. Difficulties arose in cases in which accumulation trusts were set up for individuals not yet born. The fiduciary was then made a taxable entity under the Revenue Act of 1916.

The trust is now liable to tax separately on its retained income on the basis of the rate schedule for married persons filing separate returns. Tax exemption of $ 300 is allowed in the case of a trust that distributes all its current income among its beneficiaries within the year, as against $ 100 available to other fiduciaries. The amount paid to the beneficiaries is deducted from the trust income subject to the over-all limit of

the distributable income of the trust. The balance is taxed to the trust. The prerequisite for the deduction of the income paid to the beneficiaries is that the latter should have disclosed the receipts in their respective returns of income and cleared the tax due thereon.

The methods of tax avoidance practised in the United States have been similar to those elsewhere—multiple trusts for the benefit of the same persons, accumulation and discretionary (called "spray") trusts, generation-skipping settlements, gifts, with reservation of interest and powers of appointment, etc. The author of a trust could control the disposal of the trust income through his reserved powers and also by the appointment of a member of his family, or a friend or a bank as trustee, if he did not himself want to be a trustee.[34] The direct or indirect control enabled him to have the trust income accumulated and taxed for the time being at rates less than those applicable to him. When the accumulated income was distributed, it was taxed, with certain exceptions, to the beneficiaries under an averaging or "throw-back" provisions enacted in 1954, credit being available for the tax, if any, paid earlier by the trust. Despite the throw-back rule, the intervening postponement of tax liability at the highest rate was of advantage in the cases of several families and the advantage could be enhanced through trusts in tax havens. The Senate Committee on Finance Tax Reform Act 1969 suggested, what was in effect, a 6 per cent interest on the tax that was put off if the rate of tax attracted by the trust was less than that at which the beneficiaries were liable, but this suggestion was not pursued because of the tough opposition encountered from trust companies and the tax bar.

As regards the reduction in tax rates that was secured through multiple trusts, it has been countered by taking all trusts that have the same beneficiaries and that are motivated by tax deferral or avoidance, as a single trust for tax purposes.

In the past, there was a tax on the death of the owner of a property but not on the death of a life tenant who had been enjoying the income from the property. A transfer tax has been imposed on generation-skipping transfers by the Tax

Reform Act of 1976, but outright gifts are exempt even if they skip generations. For example, if a property is transferred by G, the grandfather, to a trust for the benefit of his son S for life, with reminder to R, his grandson, there will be a tax on the death of S, determined on the basis of the rates appropriate to the value of the estate of S, after certain exclusions for each child of the grantor. The object is to collect tax to the extent of the tax liability which would have resulted if the property passed from generation to generation.[35]

There is a view that tax considerations may or may not weigh in testamentary trusts but most irrevocable *inter vivos* trusts are tax motivated.[36] Total income of less than a billion dollars had been reported by nearly 360,000 trusts in 1956, and the income taxed in the hand of the trusts was less than $ 700 million, the tax liability being about $ 250 million. Jantscher's inference is that the great majority of trusts for which returns were filed were either testamentary trusts or *inter vivos* trusts created by deceased grantors, and that the amounts of taxable income actually shifted each year from living grantors to trusts or to beneficiaries might be relatively small during that period.[37]

The tax treatment of foreign trusts is somewhat vague and uncertain in the United States. The factors taken into consideration are the residence of the trustees, the place of management and the situs of the trust property.[38]

Other Countries

Trusts are not popular in the European countries where, it would appear, trust income is not ordinarily accumulated. In family settlements, in which the settlor and members of his family hold more than 50 per cent of the income or property, income and wealth tax liabilities arise, even if there is no distribution of income or capital. The income and wealth of the foundation or settlement is assessed as the income of the settlor or the beneficiaries, depending on the facts of the individual cases. In Sweden, the capital is attributed and taxed to the beneficiaries in the case of a specific trust. Assessment is made on the trust itself, as if it is the case of an individual, where it is discretionary and has accumulated

income. While the life-tenant is assessed on the entire corpus in the Scandinavian countries, only 80 per cent of the value of the corpus is taxed in the Netherlands. The actual share of the beneficiary is taxed to the beneficiary, the balance being covered in the hands of the owner.[39]

The treatment of trusts is not uniform in the tax haven countries. Taking the Isle of Man, for instance, the trust itself is taxable at 21 per cent of the income that is accumulated. The beneficiaries are directly assessable, when the income is distributed. The general approach is to look through the trust, for the individual beneficiaries, wherever possible.[40]

There is no country which had found the operation of trusts prepossessing from the tax angle. But the possibilities of the use of trusts as a vehicle for the avoidance of the estate duty have been explored to the maximum extent in the UK, the US, Canada and Australia. Though the English experience has been the longest and most valuable in the income tax, the UK is yet to have a tax on wealth, and it has already abandoned the estate duty for a capital transfer tax, covering all transfers of property, including gifts during a person's lifetime, property that passes on death and all settlements.

NOTES

1. Meade, J.E. (1978), *The Structure and Reform of Direct Taxation*, The Institute for Fiscal Studies, London, pp. 401-10.
2. CTA 1970 : Section 434(2) : A trust does not become inoperative if a beneficiary dies within the 6 years. It does not also become revocable if the settlor does not make a payment due under the settlement deed and the beneficiary does not enforce the payment : Lee v IR 25 TC 485.
3. For the sweep of the term "interest", see IR v Wachtel (1971) 46 TC 543.
4. CTA 1970, Sec. 448.
5. Vandervell's Trusts v IR (H/L) (1967) 1 All ER 1 ; 43 TC 519 where certain shares were transferred to a college and after dividend was declared in respect of the shares, an option could be exercised by the taxpayer's nominee to acquire the shares for a stipulated consideration. The House of Lords supported the claim of the Commissioners of Inland Revenue for levy of surtax on the dividend income in the hands of the taxpayer on the ground that the shares were held by the college on a resulting trust for the taxpayer.

6. Sec. 451, ICTA 1970 : IRC v Bates (1968) 44 TC 225, in which the settlor's overdraft was repaid. But contrast Pott's Executors v IR (1951) 32 TC 211 where a company covered by a settlement cleared the settlor's debts to third parties who were not accountable to him.
7. Sec. 444(1).
8. Re. Clarkson-Webb 17 TC 451.
9. See 451, but *bona fide* loans are not hit : IR v Sansom (1921) 8 TC 20 (CA).
10. Corbett v IR (1938) 21 TC 449, 460, Dreyfus v IR (1963) 41 TC 441, *Cf.* Cornwell v Barry (1955) 36 TC 268 where the income of the beneficiary was liable to be diverted, though he had a vested interest in it.
11 Aikin v Macdonald's Trustees (1894) 3 TC 306. Income from foreign investment to the extent that it was utilised in the costs of administration of a foreign trust was not, however, taxed in Baker v Archer Shee (1927) AC 844 ; 11 TC 749 (HL).
12. Fry v Shiel's Trustees (1915) 6 TC 583. The contrary view has been taken in India : CIT v P. Krishna Warrier (1970) 75 ITR 154, 157 (SC) ; CIT v Uma Maheswari (1969) 71 ITR 614 (Pat). However, there are no special provisions governing earned income in the Income-tax Act in India at present.
13. Drummond v Collins (1915) 6 TC 525 (HL).
14. Williams v Singer (1920) 7 TC 387—Case of a beneficiary domiciled and resident in the US directly receiving income from investments in the US on the instructions of the trustees in the UK. Also see Reid's Trustees v IR (1929) 14 TC 512. It has been held that the source of a beneficiary's income would be securities and not the trust deed where the trustees held securities upon trust for the beneficiary's life : Archer-Shee v Baker (1927) 11 TC 749 (HL).
15. Jackson's Trustees v IR (1942) 25 TC 13 ; Brodie's Will Trustees v IR (1933) 17 TC 432; Cunard's Trustees v IR (1946) 27 TC 122; Williamson v Ough (1936) 20 TC 194 ; Milne's Executors v IR (1956) 37 TC 10 ; Lawson v Rolfe (1969) 46 TC 199. The position is not different in a discretionary trust : Lindus & Hartin v IR (1933) 17 TC 422 ; Peirse-Duncombe Trustee v IR (1940) 23 TC 199.
16. (1965) *Estate and Gift Taxation* : A *Comparative Study*, Sweet and Maxwell, London, p. 136. For use of trusts and settlements to avoid tax, see Chapman v Chapman (1954) 1 All ER 798 ; Re. Drew's Settlement (1966) 2 All ER 844 ; Re. Lloyd's Settlement (1967) 2 All ER 314 ; Clitheroe's Settlement Trusts (1959) 3 All ER 789 ; Re. Sainsbury's Settlement (1967) 1 All ER 878.
17. See the UK Green Paper on the Wealth Tax (CMND) 5704.
18. Discretionary trusts outside the UK are subjected to the surcharge of 15 per cent in respect of dividends on shares in the UK

companies : IR v Regent Trust Company Ltd. (1980) STC 140 ; (1979) TR 401.

19. For the meaning of interest in possession, see Pearson v IR (1980) 2 All ER 479.
20. Brodie's Will Trustees v IR (1933) 17 TC 432.
21. Stanley v IR (1944) 1 All ER 230 ; 26 TC 12 (CA) ; IR v Blackwell Minors' Trustees (1924) 2 KB 351 ; 10 TC 235 ; Hamilton Russel's Executors v IR (1943) 25 TC 200 (CA).
22. William J. Shultz (1926), *The Taxation of Inheritance*, Houghton Mifflin, pp. 223-24, quoted by Gerald R Jantscher, (1967), *Trusts and Estate Taxation*, Brookings Institution, p. 5.
23. IR v J Bibby & Sons Ltd., 29 TC 167 (HL), (1946) 14 ITR (Suppl) 7 ; Barclay's Bank Ltd. v IR (1960) 3 All ER 173, (1962) 45 ITR (Suppl.) 1 (HL) ; Shields (John) & Co. (Perth) Ltd., v IR, (1950) 29 TC 475.
24. Weir's Settlement Trust, Re. (1970) 1 All ER 297 ; (1970) ITR 53 (CA) ; Gartside v IR (1968) 1 All ER 121 ; (1968) 70 ITR 663 (HL) ; Sainsbury v IR (1970) 75 ITR 388 (CD) ; (1969) 3 All ER 919.
25. The Board of Inland Revenue Press release on 11.9.70 reproduced on pp. 283-84 of BTR 1970 ; Lovell, *Discretionary Trusts and Estate Duty—the Dutiable Slice* (1970) BTR 220 ; Goldberg, *The Curious Case of the Finance Act and Sub-trusts* (1971) BTR 117 ; C.W. Keeton and L.A. Sheridan, 1974, *The Law of Trusts*, Tenth Edition, Professional Books Ltd., London, p. 346.
26. See David B. Parker and Anthony R. Mellows, *The Modern Law of Trusts*, 4th ed., Sweet & Maxwell, p. 65. Bermuda, the Bahamas, the Caymen Islands, Gibraltar, Honkong, the Carlos Islands, Luxembourg, New Hebrides, Norfolk Island, Netherlands, Antilles, Panamas, and Switzerland are among the popular tax resorts. Nepal and Bhutan serve as tax shelters for India. The Middle East is also free of taxes.
27. Re. Weston's Settlements (1968) 3 All ER 338 involving arrangements in Jersey, where some of the beneficiaries acquired a domicile and took up permanent residence to avoid the capital gains tax and estate duty. The court declined to approve the arrangements for the minor children. "Trust exporting" continues, however, despite Weston's Settlements case, as pointed out in Underhill's *Law of Trusts and Trustees*, 13th ed., by David J. Hayton, p. 400. For cases in which arrangements for the transfer of assets to off-shore trusts were approved by the courts : Re. Windeatt's Will Trusts (1969) 2 All ER 324 ; Re. Seale's Marriage Settlement (1961) 3 All ER 136 ; Re. Whitehead's Will Trusts (1971) 2 All ER 1334.
28. Robin W. Boadway and Harry M. Kitchen : *Canadian Tax Policy*, p. 80 ; Canadian Tax Papers, No. 63, Canadian Tax Foundation, 1980.

29. It has been held that this power is of no avail where the children of the taxpayer are beneficiaries of separate trusts : *Reports of Proceedings of the Thirty-first and Thirty-third Tax Conference*, Canadian Tax Foundation.
30. *Report of the Royal Commission on Taxation*, Chairman : K.L. Carter, 1966.
31. Ibid. Vol. 4, pp. 195-96
32. Watkins v Commissioner of Probate Duties (Vic).
33. *Final Report*, Taxation Review Committee, January 31, 1975, Chairman : K.W. Asprey.
34. Some of the problems that arise when the settlor is also trustee and beneficiary for life and when the trust deed does not indicate the need for property accourting for the income and assets of the trust are evident from the case of Home for Destitute and Crippled Children v Boomer 308 Ill. App. 170, 31 NE (2d) 812 (1941). For brief details, vide Eleanor K. Taylor (1953) *Public Accountability of Foundations and Charitable Trusts*, Russel Sage Foundation, New York, p. 41.
35. Kluwer Deventer (1978), *International Tax Avoidance* : A study of the Rotterdam Institute of Fiscal Studies, Vol. B, Country Reports, Netherlands.
36. Ray M. Sommerfelt, Herschel Manderson and Horace R. Brook (1977), *An Introduction to Taxation*, Harcourt Brace Jovanovich, Ch. 9-8.
37. G.R. Jantscher : *Trusts and Estate Taxation*, p. 85, Washington : Brookings Institute (Studies of Government Finance).
38. B.W. Jones Trust v Commissioner 132 Fed (2d) 914 Maximor Trustees v United States 373 US 49 (1963) : Both the cases have been quoted at p. 229, Richard A. Green, *The Residence of Trusts for Income-tax Purposes*, Canadian Tax Journal, Vol. XXI, No. 3, May-June 1973. Canadian Tax Foundation, Toronto. The cases related to trusts with the bulk of their assets and also some of the trustees in the US though the settlors and beneficiaries belonged to the UK.
39. C.T. Sandford, J.R.M. Willie and D.J. Ironside (1975) *An Annual Wealth Tax*, Institute of Fiscal Studies.
40. H.W.T. Pepper, "Isle of Man : Viking Haven in a Celtic Sea", *Accountant*, November 9, 1978.

5

Vagueness in the Law

Revenue losses in a business conducted by a trust

There is a general criticism that the English trust concept has been grafted not only on the Indian Trust Act but also on the Indian tax laws without due consideration of all its implications. The structural flaws are many and it is not fair to expect all of them to get sorted out through judicial pronouncements. For instance, the Income-tax Act does not indicate clearly whether the income to be assessed in the hands of the beneficiaries, either directly or through the trustees, is the income computed in accordance with the provisions of the Act or the income actually distributed by the trustees to the beneficiaries. In the case of a partnership that is registered under the Income-tax Act, its entire assessed income is apportioned among the partners, whether they receive a larger or a smaller amount. In the case of a private trust, however, a beneficiary is generally taxed only on the basis of the income actually received or receivable by him.

There are also other complications resulting from the interaction of the trust law and tax statutes. A private trust is an esoteric, specialised and individualistic financial arrangement, which defies routine application of some of the provisions of the tax laws. For instance, the income of a trust may be assigned to one individual and the corpus to another by the author of a trust. In such a case, in the event of a loss from any business conducted by a trust, it is not evident from the Income-tax Act whether the loss that is carried forward should be set off only against the income of the trust under the same

head in the succeeding years or it may be adjusted against the beneficiary's income, if any, from any other business, particularly in a case in which the beneficiary has an interest only for a few years in the business of the trust. Will he get the benefit of off-setting the unadjusted loss even in the years in which he has ceased to have any interest in the trust business? In fact, the Income-tax Act does not have any separate provision at present for the treatment of the losses suffered by a trust. Some trust instruments may indicate how the trustees should deal with the losses, if any. Income is an accretion to the capital, while a loss depletes it. If a beneficiary is entitled only to the income of a trust and there is a remainderman who will eventually get the trust capital, it is an open question whether the brunt of the losses will be borne by the former or the latter. If the trust-deed requires the capital to be maintained at the same level, the losses may not merely be adjusted against the subsequent income but even where no losses are brought forward, the current income payment may be pruned and reserves built up to safeguard against unexpected losses and diminution in capital. If the settlor has not given any direction in the matter, losses will operate to the detriment of both the life-tenant and the remainderman. The annual income may decrease with the erosion of the capital and the remainderman may eventually get a reduced volume of capital. There is also the possibility that the loss may not be deducted from the trust income in the following year in calculating the income entitlement of an income beneficiary, but may be either immediately met out of the trust capital or carried forward and charged against capital gains, if any. There is a view that the loss cannot be deducted from the net income of the trust estate in determining the tax liability on the income beneficiary in a subsequent year in such circumstances. How far such denial of loss off-set is strictly tenable under the Income-tax law as it is, is controversial, even if it is assumed that the loss has been suffered under the head "business". Such denial may be inevitable if the income beneficiary ceases to have an interest in the income after the loss year, i.e., if he is entitled to the income for a limited period and the period expires with the close of the year in which the loss is incurred. There will be complications if the taxable income is larger and the trust income is reduced to the extent of the

brought-forward losses, and there is a new income beneficiary. Such difficulties will be unavoidable as long as the person who, in fact, bears the loss in terms of the trust deed is different from the person who reaps any advantages from it in tax assessments.[1]

Capital allowances

When the income and the capital beneficiaries are not identical, capital receipts[2] and also allowances, like the investment allowance or even depreciation, ordinary or accelerated, may pose similar conundrums. Since the capital allowances are meant to compensate or serve as an incentive to the owners of the capital assets, there is no warrant in equity, for allowing the relief to the beneficiaries entitled to the income from the assets. The inherent anomaly can be illustrated with reference to a trust in which a beneficiary is entitled to an annuity for his life, irrespective of whether income from the trust is adequate or not to cover the annuity and the interest in the corpus of the trust is assigned to some other beneficiary.[3]

Losses due to maladministration of trust

Losses due to fraud may cause slightly different problems. They are not deductible in the computation of taxable income unless it can be established that they have been incurred in the ordinary course of the business or they are incidental to the business. The position in regard to trusts needs clarification. It is settled law that a trust is not voided by the misfeasance or mismanagement of a trustee, irrespective of whether the trust is an *inter vivos* or a testamentary one; but there can be two opinions on the admissibility of claims of losses due to the trustee's defalcation or errors of omission in the assessments of the trust or of the beneficiaries. If the losses resulting from any misappropriation or negligence on the part of the trustees are disallowed, there is bound to be some hardship in the assessment of the beneficiary.

Trust expenses

Trust expenses are deductible in working out the income payable to a beneficiary but not in determining the income of the

trust for tax purposes.[4] This difference in the treatment of a trust and its beneficiaries will always lead to anomalies.

Capital gains

A related issue is the treatment of trust receipts including capital gains as against losses or expenditure. The capital gains are added to the capital in some trusts while some others contain directions for their distribution. Where a trust gets a property by way of bequest or gift, the market value determined for estate duty or gift-tax purposes may reasonably serve as its cost to the trust and later, on its disposal, there may be gain or loss, depending on the consideration, if the sale is genuine. The treatment of the capital gains or losses has become the subject of dispute in several cases.

Transfer of assets by or to a trust is regarded as a disposal in the UK, except when a transfer is made by way of security. If a trustee has been vested with any property for the benefit of a single beneficiary, whether a child or a person suffering from any disability, the gain, if any, from the disposal of the property, will be attributed to the beneficiary unless the beneficiary's interest is contingent on his reaching a particular age.[5] Where a beneficial interest in the property is not held by a single person, the trustee pays tax at a flat rate in the UK.[6]

In the USA where a taxpayer sold her life estate in a testamentary trust to the trust's remainderman, for cash consideration of $ 55,000 and claimed a capital loss of $ 8,000 in the process on the ground that the actuarial valuation of her interest was $ 63,000, her claim was allowed by the Court[7]. This is one extreme view. On this logic, will the person who acquired the interest in the income from the property for his life be assessable to the wealth tax on the amount paid by him or on the actuarial value? If he is already the remainderman with a right to the corpus, he gains to the extent that he can seek the termination of the trust. Since he has become the absolute owner of the income as well as the corpus of the property and he can take any measures he considers fit to increase the income or the value of the property producing the income, should not the market value of the property be charged to the wealth tax without reference to the consideration he has paid for the life-interest ?

At the other extreme is the case of a taxpayer who was the sole beneficiary for her life-time under a trust-deed.[8] The trustees were to utilise the income from the trust funds for her maintenance, support and education for her life-time and thereafter the trustees were to hold the trust funds for all her children in equal shares and, if she had no child, for the benefit of the person appointed by her. The trust-deed empowered the trustees in their absolute discretion to spend a portion of the corpus of the funds for the maintenance, support and education of the beneficiaries or on the occasion of serious illness or an emergency. The trustees sold some shares forming part of the corpus of the trust funds which resulted in capital gains, and the question was whether the capital gains could be taxed in the hands of the beneficiary under section 166 of the Income-tax Act. The Court held that the capital gains received by the trustees were not assessable in the hands of the beneficiary. The mere fact that the trustees were to hold the corpus of the trust for the benefit of the assessee and in her absence for those beneficiaries specified in the trust deed, would not mean that accretion to such corpus would, because it might fall under the definition of "income" under the Income-tax Act, be virtually an income received by the trustees specifically on behalf or for the benefit of the present beneficiary. There is an obvious saving in tax in getting the trustees assessed separately on gains which are accumulated and also on receipts which are deemed to be income under the law but for the distribution of which the beneficiaries are not entitled.[9]

Other legal issues

i. Income accruing in one year and paid to beneficiary later

The income of a trust may not be receivable by a beneficiary as and when it accrues or immediately after it has accrued.[10] If a trustee is empowered to make payment to a beneficiary not when the income actually arises but in a later year, the questions that come up for consideration are (a) whether the beneficiary or the trustee should be assessed to tax for the year in which the income arises, (b) whether any action should be taken in the beneficiary's case in the year in which the income is paid to the beneficiary, and (c) whether

the beneficiary should be taxed on the entire income of the trust or only on so much of it as is distributed to him.[11]

ii. Life insurance policies on settlor's life kept up by trust

Disputes arise at times in respect of life insurance policies on settlor's life maintained by a trust for different beneficiaries. The disputes in such cases centre round the question whether the amount of premium should be treated as the income of the donor on whose life insurance has been affected or as the income of the beneficiary of the trust. It is reasonable to hold that when a policy is maintained by a trust, the amount of premium should be treated as the income of the settlor and appropriate relief allowed as if the premium has been paid by him out of his income.

But, unfortunately, the Revenue tends, sometimes, to adopt a legalistic attitude and impose an unfair tax burden, in disregard of reality. For instance, there is liability to the estate duty on the settlor's death where a policy "is wholly kept up" for an assignee. This provision operates harshly where the policy amount is fully paid up long before the death of the assured but the insurance company expresses inability to make it over to the trustees to whom it has been assigned till his death. It is obviously unrealistic and unfair to levy the estate duty on the amounts receivable in respect of such policies which are paid up more than two years before the death of the disponer.[12]

iii. Treatment of expenses incurred by a trust for political or private religious purposes

A trust for influencing the legislature or for political propaganda or for advancing the interests of any particular party or group, is not entitled to tax exemption, no matter what it calls itself—"Education Centre" or "Fund for Adult Education" or "Institute for Social Services". The problem for consideration is how such trusts should be taxed—in particular, whether voluntary contributions received from the public should be taken to be income or capital receipts, since they are not covered by the definition of income in section 2(24) of the Income-tax Act, and whether it would make any difference to the situation if the donations are large and anonymous.[13] The expenditure

incurred in a trust for political purposes may not lend itself to check, or be inadmissible under the current provisions of the Income-tax Act, but if the casual donations are treated as income while the expenses are disallowed, it will be inconsistent and the trust may be taxed out of existence.

Similarly, the scope of an income tax assessment on a private trust for religious purposes is not also very clear from the Act. An idol can get a donation of property not only when it is consecrated but also later, from either the founder of the *debuttar* or even outsiders. What the law should specify is whether donations received by the trust should be treated as income or non-income receipts and whether expenditure incurred in connection with the daily worship of a deity and so on should be allowed in computing the total income of the trust. Merely because the object of the trust is to ensure regular observance of rituals, performance of daily worship, etc., the expenses do not become admissible deductions. The logical course would be to treat the idol just like an individual and levy tax on that basis. Receipts which will be ignored in the assessment of an individual will not assume the character of "income" in the case of a private trust, but if the receipts are large and it is not possible to verify the identity of the donors, the question of including them in the assessment of the trust as income from undisclosed sources may need consideration. Expenses which would not be allowed in the case of an individual as being of a personal nature should not also be deductible in the assessment of a juridical entity. If the claims are inadmissible in the case of an individual, there is no reason why they should become chargeable to the revenue account only because the individual has transferred some of his income-yielding assets to the deity as symbolised by an idol. It may be pleaded that the imposition of tax will reduce the amount of income available for meeting the expenses for which the trust has been set up, but the obvious answer to this plea is that the income tax should be treated as an item of cash out-go like the other expenses of the trust and there is no justification for the author of the trust to expect the expenses of the deity to be borne by the State.

iv. Anonymous receipts in a private trust

The problem of secret or unverifiable contributions to a private trust may prove to be intractable in certain circumstances. If the trustees of a trust are unable to offer a satisfactory explanation about the source and nature of any money received by them in trust, the sum will be liable to the income tax as the income of the trust from undivulged sources, in terms of section 68 of the Income-tax Act. But should the Revenue be content with invoking section 68 of the Income-tax Act? The rate of tax may be much higher in the unseen hands that have transferred their presumably unaccounted funds to the trust. Since, in the very nature of its scheme, a trust cannot have undeclared assets or sources of income, it may not be improper or harsh to tax the funds as also the value of other assets which a trust gets from unknown quarters, as the maximum rate of income tax to which an individual may be liable, plus an additional tax based on (a) the gift tax avoided by the pseudonymous donor, and (b) a suitable penalty for his concealment of the income in his own income tax assessment. Where a trust is for minor children or an individual with a richer spouse, it may not also be unkind to draw an adverse inference about the identity of the donor : for the purpose of aggregation of income under section 64 of the Income-tax Act and wealth under section 4 (1) of the Wealth-tax Act, transfers of cash or other assets unsupported by sufficient details which may serve to check the source, can be reasonably attributed to the parent or the spouse, as the case may be, and treated in the latter's assessments on the same lines as openly-transferred assets. It will also be appropriate to deny the relief for which section 71 of the Income-tax Act provides, *viz.*, setting off loss under one head against income from another, in respect of all such receipts deemed to be secreted income, since they are really somebody else's money, subjected to tax through the trustee or beneficiary only because the person who has made it is using the trust as his stalking-horse. There can be no injustice in permitting losses iucurred by a trust to be set off only against income which it has itself earned and not the tax-evaded income of a third party transferred to it.

v. Need for acknowledgment of interest by beneficiaries

A trust may occasionally be faced with the problem not merely of an anonymous donation but a reluctant beneficiary or a beneficiary who is not even aware of the benefit that is being conferred on him. In Scotland, a trust does not become effective unless and until the beneficiaries concerned are intimated their rights; even the knowledge of the beneficiaries may not suffice without their specific concurrence. A lady took out a policy of assurance on her life to be held by her upon trust as trustee for three other ladies each of whom was to be entitled to a separate portion of the policy moneys. Unfortunately, she failed to notify two of the beneficiaries of their interest in the trust. It was held that the portions of the policy moneys belonging to these two beneficiaries should be aggregated with the rest of the estate of the settlor when she died, since the trust was not complete to that extent.[14]

In India, a formal communication to the beneficiary is not required.[15] If he is aware of his interest in the trust and has not rejected it, the trust is valid. In the UK, the declaration of trust may be a purely unilateral act and the beneficiary's acceptance of his interest, express or even tacit, is not needed. The settlor has to be unequivocal in the declaration of the trust but he may be the trustee himself and retain any document that he executes without any intimation to the beneficiaries.

It is desirable to bring on record all the parties involved in any *inter vivos* trust as soon as possible after the trust comes into existence, as in the case of a partnership which is sought to be registered for tax purposes. It is also essential to insist on the acknowledgment of the interest by the beneficiaries as a prerequisite for the completion of the trust, since no one can be compelled to accept a benefit; and a reversion of the interest to the settlor after it becomes an interest in possession for the beneficiary has further tax implications. A trust which does not take even the beneficiaries fully into confidence can only be an avenue for tax avoidance.

vi. Residence of Trust

With the steady increase in the number of Indian nationals abroad, and the measures being taken by the Government to

induce them to invest in India, thought has to be given to the treatment of trusts created outside the country with some beneficiaries, properties or trustees in this country and also trusts set up in this country with some of their beneficiaries, properties or trustees in other countries. No data are readily available to show how many such trusts exist at present.

In the case of a beneficiary who is ordinarily resident and who has an interest in an off-shore trust, section 5 of the Indian Income-tax Act enables the Revenue to reach all the income which may accrue or arise to him in the foreign trust or may be paid to him by the trust.[16] A trust is administered in accordance with the law of the country in which it is constituted. The income of the beneficiary of such a trust, who is resident in India, cannot be worked out as if it is income from his personal investment abroad, since he does not own the trust property but has only a beneficial interest in it. His income will, therefore, be unavoidably affected by the application of the foreign law.[17] Where, for instance, a trust instrument provides for the accumulation of income in the hands of non-resident trustees or leaves the discretion with the trustees to make payments as they consider fit, the beneficiary can be assessed only on the basis of payments made to him.[18]

Though the trust income or wealth may be assessed to tax, the trustee really pays the tax on behalf or in respect of the beneficiaries who should, therefore, be eligible for the deductions and exemptions admissible under the law.[19] The beneficiary's tax liability will be determinable with reference to his residence, domicile, allowances and reliefs, if any income is directly payable to him or his bankers under the trustee's mandate.[20]

Where income has been accumulated by a foreign trust on the ground of the beneficiary's disability and paid to him later in a lump sum, it may be contended that he has not received income but an amount paid to him in satisfaction of his interest in the trust. In all such cases and also where a foreign source income has been applied, directly or indirectly, to the beneficiary's advantage, the amount so paid or applied should be deemed to be the assessee's income in the year of payment or application and taxed to him if he is ordinarily resident.

The problem is complicated by several variable factors

where the trust is itself to be assessed to tax through the trustees. A settlement in trust may be made by an Indian citizen or a foreign national, in this country or abroad. The settlor may either be a resident or a non-resident, depending on the length of his stay in India during the relevant period, i.e., the year in which he creates the trust. Some of the properties or trustees may be in India and some outside; and the trustees may be either residents or non-residents. The Indian tax laws do not indicate how a trust should be treated for tax purposes in different situations and what attributes or combination of them should determine the residence and accordingly the tax liability of the trust.

NOTES

1. See Wolfe D. Goodman (1983): "The Allocation of Tax Burdens Between Income Beneficiaries and Capital Beneficiaries," *Canadian Tax Journal*, Vol. 31, No. 2, (March-April), pp. 169-82.
2. Bouch v Sproule (1887) 12 App. Cas. 385.
3. The impracticability of holding that any income belonged to any particular beneficiary from the moment it arose and became payable to the time it was paid has been indicated by Viscount Sumner with reference to a trust for accumulation, in Archer-Shee v Baker 11 TC 749.
4. Vide Chapter 4. Also Macfarlane v IR (1929) 14 TC 532; Murray v IR (1926) 11 TC 133. Payments made for the services of a trustee amount to an expense in the administration of the trust but they are not allowable deduction in the computation of the income of the trust for tax purposes.
5. Tomlinson v Glyns Executor & Trustee Co. (1970) Ch. 112; (1970) 1 All ER 381; 45 TC 600.
6. 30 per cent.
7. McAllister v Commissioner [157 F 2nd, 235 (2nd CIR) (1946)].
8. Kumari Pallavi S. Mayor v CIT (1981) 127 ITR 701 (Guj); CIT v J.B. Wadia (1963) 48 ITR 135 (Bom); Anarkali Sarabhai v CIT (1982) 138 ITR 437 (Guj).
9. A life tenant entitled to the income of a trust cannot be subjected to tax on receipts which are to be treated as part of the corpus of a trust under the trust-deed but which are deemed to be income under the Income-tax Act. Capitalised distributions made to the shareholders of a company on its liquidation, which are attributable to its accumu-

lated profits or the gains made in frequent variations of investments can be taxed to the trustees but not to the beneficiaries: CIT v J.B. Wadia (1963) 48 ITR 135 (Bom); CIT v Arvind Narottam (1963) 73 ITR 490 (Guj); R.H. Pandit v CIT (1972) 83 ITR 136 (Bom).

10. In the UK, a beneficiary is liable to tax on income to which he is entitled by virtue of his "interest in possession" in a trust, irrespective of whether he receives the income or not. The law in the USA is different : Archer-Shee v Garland (1931) AC 212. A mistaken assumption regarding the American law on this point had resulted in Lady Archer-Shee's losing her case earlier in the House of Lords: Baker v Archer-Shee (1927) AC 844.
11. In the UK, when a beneficiary is assessed on the trust income that he receives, it is related back to the appropriate years : IR v Hawley (1928) 13 TC 327.
12. In re. Hodge's Policy : Hodge v IR (1958) Ch. 239 (1959) 37 ITR ED 1.
13. For the tax exemption claim of trusts for political propaganda etc., see *Halsbury's Laws of England*, Vol. 4, 3rd ed., p. 242, para 523. Donations made by a company to the corpus of a private discretionary trust formed by it for providing financial assistance to its employees cannot be treated as the income of the trust liable to tax : order dated Feb. 4, 1983 in the case of Escorts Employee Welfare Trust v ITO, ITAT (Delhi Bench C) (1983) 5 ITD 226.
14. Allen's Trustees v IR (1969) TR 377.
15. P.L S.K.R. Chettiar v CIT 5 ITC 50.
16. In the UK, foreign trust income is liable to tax, whether remitted or not, unless the beneficiary is domiciled abroad or is a British subject not ordinarily resident in the UK. The resident trustee is taxed on the income from foreign securities, etc., if the beneficiary is not a non-resident entitled to accumulation of income under a foreign trust: Kelly v Rogers (C/A-1935) 19 TC 692.
17. Archer-Shee v Garland (1931) AC 212; 15 TC 693; Baker v Archer-Shee (1927) AC 844; 11 TC 749; Ransom v Higgs (1974) 1 WLR 1594; (1973) STC 330; Drummond v Collins (1915) AC 1011; 6 TC 525.
18. In the UK, remittances from foreign trustees of discretionary trusts are assessable when the trustees exercise their discretion and make remittances: Drummond v Collins 6 TC 525.
19. Williams v Singer (1920) 7 TC 387; (1921) 1 AC 65.
20. Reid's Trustees v IR (1929) 14 TC 512 ; Kelly v Rogers 19 TC 692; Baker v Archer-Shee 11 TC 749 (HL).

6

No Equity in Tax Treatment of Trusts

IT has been observed that the tax laws in India present the spectacle of seemingly high rates of tax, which are practically nullified by loopholes which are open invitations to tax avoidance. For example, if a trust having four beneficiaries, with equal shares in a business conducted or assets owned by it, makes large long-term capital gains in the sale of some of its assets, deduction of Rs. 5,000 under section 80T in respect of the gains can be claimed separately for each beneficiary. This seems to be an unintended benefit, for it is not available to a registered firm with several partners or a limited company with a large number of shareholders.[1]

There are special provisions in sections 78 and 79 of the Income-tax Act regarding the carrying-forward of losses if there is a change in the constitution of a firm or one firm is succeeded by another or the controlling interest in a close company has changed hands. A trust carrying on a business is free from such restraints, even if the same beneficiaries do not continue to have an interest in the trust during its periods of losses as well as its periods of profits or a beneficiary has transferred his interest to somebody else.

Though there is not much difference from the point of view of objectives and methods between a family trust, a firm and a family corporation, a trust pays less tax than a firm and much less tax than a close corporation. Table 6.1 shows the sharp difference in incidence.

TABLE 6.1

TAX (INCLUDING SURCHARGE) PAYABLE IN RESPECT OF INCOME EARNED BY A TRUST WITH FOUR BENEFICIARIES (INDIVIDUALS), A FIRM WITH FOUR PARTNERS (INDIVIDUALS) AND A CLOSE COMPANY IN THE ASSESSMENT FOR FINANCIAL YEAR 1982-83

(Rs.)

Income	*Tax payable by the beneficiaries of a trust*	*Tax payable by a registered firm and its partners*	*Tax payable by a close company*
1,00,000	13,200 (all the four beneficiaries together)	11,000 (by firm) 12,872 (by the four partners together) 23,872 (in the aggregate)	66,625
2,00,000	55,880 (all the four beneficaries together)	37,400 (by firm) 39,524 (by the four partners together) 76,824 (in the aggregate)	

Notes : 1. It has been assumed that the beneficiaries of the trust and the partners of the firm have no other source of income.

2. The shareholders of the company will have to suffer additional tax on the income they derive from the company by way of dividend, depending on their other taxable income.

The disparity in tax rates between close companies, firms and trusts puts a premium on tax avoidance through trusts as against tax avoidance through companies and firms. The very simplicity of the action required to avoid tax through trusts makes a trust more attractive than a company or a firm. It has been held, for instance, that one who is assessed as an indivi-

dual on the income from the business he carries on can straightaway constitute himself as the trustee for the same business in a trust for the benefit of his sons, and the income is split instantaneously.[2]

It may be argued that a company enjoys several privileges like recognition as a legal entity, perpetuity, and the right to sue which are denied to a trust. The argument is averted by the fact that firms are more popular and have increased in much larger numbers in recent years than companies, despite their not having these rights. In any case, the practical value of the privileges of a company is negligible. Moreover, a trust has advantages which are not available to companies and firms. The corporate veil can, for instance, be pierced by the Revenue but a trust is entitled to protection from its prying eyes[3]. A distinctive feature of a trust is that it is made to order. It is tailored to suit the requirements of the beneficiaries in whom a settlor is interested. Unless prohibited expressly under the terms of the trust, a beneficiary's interest can be transferred to a third party. While a remainderman's interest or a life-tenant's interest is disposable, just like the shares of a company in the articles of which there is no restriction on transfers, a partnership stands dissolved when a partner retires or dies. By and large, a trust has as much privacy as a partnership or a close company; and it is a charmed circle which outsiders cannot enter except on sufferance. There is, therefore, no ground, equitable or other, for letting it get away with a lighter tax burden.

It is not merely the disparity in the tax rates that is anomalous; certain other aspects in the assessments of persons interested in a firm and in trusts are equally incongruous. For example, the income of minor children from partnership concerns is added, at present, to the income of either of their parents, depending on whose income is the higher. On the same principle, income of children who have not attained majority (other than married daughters) from all trusts conducting business, should also be aggregated irrespective of whether or not the business runs with capital provided by either of the parents of the beneficiaries. Such a step will remove one of the adventitious benefits currently offered by trusts.

Another example of the operation of an unconscious bias

is the aggregation of the income of a husband and his wife when they are partners in the same firm. This rule is not applicable to a trust in which both are beneficiaries or in which one of them is a beneficiary and the other is a trustee whose services are at the disposal of the trust. The role of a trust is not limited to its utility as an alternative medium for conducting business[4] It can also be used to divert the income of a partnership concern or an individual through an over-riding title in favour of persons in whom the firm or individual may be interested.[5] An assignment of the income before it accrues or arises, for the benefit of the widow of the deceased partner of a firm, or the minor grandsons of a beneficiary with life-interest in a property held under trust, will reduce the tax liability of the firm or the individual, as the case may be.[6]

Doctrine of Double Taxation

In the UK, the trustees are charged a tax on the trust income in the first instance at a flat rate of 30 per cent or 45 per cent, as the case may be. Later, when a beneficiary receives any income from the trust he is also liable to be assessed, taking into consideration the tax paid by the trustees. As mentioned earlier,[7] the present legal position about the income tax and wealth tax assessments of trust income is that they can be made either in the hands of the trustees or in the hands of the beneficiaries, but not in both. The courts have pointed out that wherever any income is excluded from chargeability to tax, either expressly or by implication, the exclusion operates for all purposes in computing the total income. It cannot be taken into account for determining either the tax payable on the income, or even the rate at which the tax is payable on the rest of the income. The courts have been of the view that if the intention of the legislature was to exclude such income from the computation of the total income only for the purpose of chargeability to tax, and not for the purpose of determination of rate, a specific provision should have been made in this behalf. Unless such a specific provision is found in the statute, exclusion of such income from the total income for the purpose of chargeability to tax must be held to carry with it the exclusion from the total income for the purpose of determination of rate. If the trustees have been assessed to the income tax under

section 160, read with section 161, the income receivable by the beneficiaries will not accordingly be included in their total income, even for determining the rate of tax applicable to the rest of their income.[8] The Revenue has also countenanced this untenable position.[9]

But, what is the basis in equity, for this view? Why should the Revenue suffer if the assessing official has not taken the trouble to find out what course is really more advantageous to it? Why should there be any discrimination between tax-payers in identical circumstances, one being taxed at a higher rate and the other at a lower rate, though the sources and even the extent of their income may be similar? While it may cause hardship if the same income is taxed twice, where is the difficulty in subjecting the other income of the beneficiaries to tax at the average rate applicable to their aggregate income, including the income taxed to the trustees? The principle of double tax avoidance should not be so exaggerated as to negate the obligation of every taxpayer to pay the tax due on his income. The two rules may not be found incompatible or irreconcilable if an *a priori* construction of the existing legal situation is avoided.[10]

It is the option given to the Revenue that creates the avoidable chaos. There is bound to be a confusion if some of the beneficiaries are assessed directly and others are not. The Act should, therefore, make it clear that while it may be open to the assessing officer dealing with a beneficiary's case to assess him on the income shown as received from a trust, such an assessment does not preclude the trust's being subjected to tax on its entire income at the maximum rate or the appropriate marginal rate, where so required by the law. The law should impose no time limit or other restriction on the revision or rectification of the assessments of the beneficiaries in the light of the assessment made on the trust. At present there may be loss of revenue as a result of even a discretionary trust's not being assessed to tax by reason of the prior assessment of one of the beneficiaries who might have received any payment from the trust. Such a loss can be prevented only if it is made possible to tax a trust, discretionary or specific, without reference to the assessments made, earlier or later, on any of the beneficiaries. Similarly, the beneficiaries should not be permitted to escape

the tax due from them in respect of their income from a trust in the event of the trust's not being assessed for any reason.[11] The appropriate marginal rate of tax should be applied to their total income, including their share in the trust income, even if the trust income has already been taxed in the hands of the trustees.

In the case of beneficiaries who are mentally incapacitated and also in the case of non-residents, the responsibility for compliance with the requirements of the tax laws should be fixed on the trustees.

Unequal treatment of oral trusts and benami property holdings

It is not always that a trust is pampered with a preferential treatment. Oral trusts provide an example of the unmerited hardship imposed by the Revenue's excessive reaction to the methods adopted by some of the tax-dodgers.

Oral trusts may be cheap attempts to avoid tax; but, sometimes, they may also be necessitated by circumstances beyond the control of the persons creating them. A trustee may also be prevented by genuine difficulties from declaring details of the trust before the Income Tax Officer within the period pescribed in explanation I to section 160 (1). An oral trust shall be deemed to be a trust declared by a duly executed instrument in writing if a statement in writing, signed by the trustee and setting out the purpose of the trust and particulars as to (a) the trustees, (b) the beneficiaries, and (c) the trust property, is forwarded to the Income Tax Officer. This had to be done where the trust had been declared before the 1st June, 1981, within a period of three months from that day; and in any other cases, compliance is required within three months from the date of declaration of the trust[12]. Let us suppose the trustee is prevented by genuine reasons from complying with this requirement, or he is dead and another trustee is to be appointed in his place by the court. The Commissioner of Income Tax should have the discretion to extend the period for compliance if he is satisfied that the trustee has been prevented by sufficient cause from filing the statement as prescribed. In any case, the moment a formal instrument is executed by the trustee, it ceases to be an oral trust. If the author is alive, he can join and reaffirm that declaration. The Indian Trusts Act

does not specify when exactly an instrument of trust has to be executed and how. There is nothing to prevent the author of an oral trust from making a formal declaration in a written document and registering it after the lapse of some time. The limitations laid down in the Income-tax Act will cease to have any relevance, once an instrument is executed. The trust cannot be treated as an oral one after the deed is drawn up and the immovable property, if any, held in trust is registered in the name of the trustee, irrespective of whether or not the trustees have complied with the requirements of explanation 1 to section 160 (1) of the Income-tax Act. And even a formal declaration of the trust before the tax authorities or the execution of a trust deed will not make the trust complete till the immovable properties are transferred from the name of the creator of the trust to the name of the trustee, unless the author of the trust is himself the trustee. An oral trust can be immediately effective only in respect of movable properties.

An oral trust for immovable properties registered in the name of the trustee will, in effect, involve a transaction, where the holder of the properties is not a bare trustee for the owner, as visualised in sections 81 and 82 of the Indian Trusts Act[13] but a secret trustee for some other beneficiary. An oral trust for movable properties has also all the characteristics of a *benami* transaction. This underlines the need to subject all *benami* income and wealth to a treatment not less stringent than that accorded to oral trusts. Section 281 A of the Income-tax Act rules out a suit to enforce any right in property held *benami* if the property has not been disclosed and the income from it returned for income tax purposes with a "notice in the prescribed form and containing the prescribed particulars" to the Income Tax Officer. Neither the income nor the wealth would suffer any additional tax if, at the appropriate time, the taxpayer who is the beneficial owner of the property, declares it in his income-tax return. Why should the beneficiary of an oral trust, the genuineness of which is not doubted by the revenue authorities, be taxed at the maximum marginal rate if the settlor-cum-beneficiary of the oral trust that goes under the name of *benami* holding pays taxes at the rates applicable to his income and wealth? One can settle immovable property in a third party's name for the benefit of a person in whom he is interested; the

settlement becomes an oral trust if it is not supported by an instrument. It gets the stigma of a *benami* transaction but enjoys a less unfavourable tax treatment, if the person in whose name the immovable property is registered or any business is conducted, is not called a trustee but a *benamidar* for the beneficial owner. This is an anomaly which calls for correction.[14]

NOTES

1. In contrast, the development rebate granted to a firm is withdrawn under section 155(5) of the Income-tax Act when its assets and liabilities are transferred to a trust in which all the partners of the firm are beneficiaries : Radhas Printers v CIT (1981) 132 ITR 300 (Ker).
2. A. Razzak v CIT (1963) 48 ITR 276 (Cal).
3. K.T. Doctor v CIT (1980) 124 ITR 513 (Guj).
4. CIT v V.S. Kumaraswamy Reddiar Trust (1982) 138 ITR 808 (Ker) relating to transfer of a business from a firm to a trust.
5. CIT v Smt. Nandiniben Narottamdas (1981) 7 Taxman 389 (Guj).
6. CIT v Crawford Bayley & Co. (1977) 106 ITR 884 (Bom); CIT v Smt. Kamlabai Juthalal (1977) 108 ITR 755 (Bom).
7. Vide Chapter 3, pp. 33, 34, 39, 43, 46, 53. Curiously, the Revenue's action to reassess the value of trust property under sec. 17 of the Wealth-tax Act in the hands of the beneficiary, despite the actf that the trustees had been assessed to tax on that property has been sustained in Mrs. Gladys S. Koder v ITO (1976) 104 ITR 220 (Ker).
8. C.R. Nagappa v CIT (1969) 73 ITR 626 (SC) affirming C.R. Nagappa v CIT (1961) 67 ITR 740 (Mys); CIT v Arvind Narottam (1969) 73 ITR 490, 497 (Guj); CIT v Balwant Rai Jethalal Vaidya (1958) 34 ITR 187 (Bom); Panna Sanjay Trust v CIT Gujarat (1969) 74 ITR 396 (Guj); Trustees of Chaturbhuj Raghavji Trust v CIT (1963) 50 ITR 693 (Bom); CIT (Central) v N.M. Raiji (1949) 17 ITR 180 (Bom); CIT v Trustees of Miss Gargiben and others (1980) 130 ITR 479 (Bom); Saifuddin Ali Mohammed v CIT (1954) 25 ITR 239, 247 (Bom); Saldhana v CIT 6 ITC 114, 117 (FB-Mad).
9. Vide CBDT Circular No. 157, dated 26.12.1974, published in (1975) 98 ITR 41 (Statute) and Circular No. 45-78/66 ITJ 5, dated 24.2.1977.
10. Ganpatrai Sagarmal v CIT (1981) 7 Taxation 279 (Cal); (1981) 25 CTR (Cal) 36; (1982) 138 ITR 294 (Cal). See pp. 48-49 and nn. 7 and 9 above.

11. In the UK, receipts from discretionary trusts as also amounts applied by the discretionary trusts for a beneficiary's education, etc., are treated as part of his total income: Drummond v Collins (1915) 6 TC 525; IR v Blackwell Minors' Trustees 10 TC 235. This income will be includible in his total income for the year in which the trustees exercise their discretion in his favour: Lindus and Hortin v IR (1933) 17 TC 442. The payment received by the beneficiary is grossed up at the tax rates relevant to the year in which the trustees take their decision.

12. Vide Chapter 3, pp. 37-38, 41.

13. The following is section 82 of the Indian Trusts Act :

    "Where property is transferred to one person for a consideration paid or provided by another person, and it appears that such other person did not intend to pay or provide such consideration for the benefit of the transferee, the transferee must hold the property for the benefit of the person paying or providing the consideration."

    In CED v Aloke Mitra (1980) 126 ITR 599 (SC), the Supreme Court has observed that the cardinal distinction between a trustee known to the English law and a *benamidar* lies in the fact that a trustee is the legal owner of the property standing in his name and the *cestui que* trust is only a beneficial owner, whereas in a *benami* transaction the real owner has the legal title though the *benamidar* has lent his name to the property. What the Supreme Court had in mind was apparently the case of a person who admitted that he was a name-lender. The very purpose of resorting to registration of property in the name of a third party is to hide the ownership. If the real owner and the *benamidar* go about proclaiming the secret arrangements into which they have entered, it will be a very unusual *benami* transaction. The fact is that in the eye of the general public, the *benamidar is* the legal owner of the property standing in his name, unless his title to it is disputed by anyone. If the *benamidar* claims the ownership of the property standing in his name, the burden of establishing that the apparent is not the real will rest on the person who makes such an allegation, i.e., who seeks to dislodge the title-holder on the ground that he is a mere name-lender.

14. This is all the more necessary because according to the Supreme Court [CIT v S P Jain (1973) 87 ITR 370 (SC)] it is not sufficient if the revenue authorities establish that a person is a mere *benamidar* of somebody. They should go further and prove that he has lent his name to a particular assessee, before the income in his name can be treated as the assessee's and properly taxed.

7

Tax Avoidance in India

Confusion caused by family trusts

IN 1969, Jerome Kurtz, former Legislative Counsel to the Treasury Department in the USA, pointed out that the drafting of wills and trusts had developed into a practice concerned primarily with taxes.[1] This is no less true of trusts in India.

Even if they are not deliberately designed to nullify the progressive element in the tax structure, intricacies in settlements leave a trail of confusion in their wake[2]. A will may create complex settlements. One document may provide for various strata of interest; and a multiplicity of trusts providing for diverse interests may compound the difficulty for the revenue authorities.[3] Where the same donor sets up several trusts, the trustees of a particular trust may often become beneficiaries in other trusts and similarly the beneficiaries of the trust may become trustees in others. A network of checks and counter-balances is a safeguard against trustees who may be vindictive or indifferent : all the beneficiaries have a built-in guarantee of even treatment.

In some of the trusts, life-tenants are specified and are also given powers to appoint the remaindermen. In such cases, the trust is discretionary only in regard to the assets receivable by the remaindermen and this will have repercussions in the wealth tax assessment alone.

Difficulty has been frequently experienced in deciding whether a trust is discretionary or specific. For instance, a certain trust was created in 1968 for the male members of the family of a settlor who reached the age of 50. Each such

member was to be given Rs. 6,000 per annum or such sum as made up Rs. 6,000 in a year if he had separate income. According to the Comptroller and Auditor General, the trust fell within the discretionary category, in view of the uncertainty of the number of beneficiaries. The assessing authorities had, however, treated it as a specific trust and did not apply the maximum marginal rate.[4]

The Comptroller and Auditor General has also given several instances of the confusion resulting from the game of hide and seek to which some of the taxpayers have recourse. A lady set up three trusts in 1957, each for the exclusive benefit of one of her sons. Since there was only one beneficiary in each trust, the only reason for resorting to the medium of a trust was apparently to cause complication, and she did succeed in her design. The fact that each of the sons had separate properties and that he would be liable to the wealth tax if the value of the trust property was added to the value of the rest of his properties, escaped the attention of the revenue authorities. It is significant that revocable transfers of certain shares had also been made by the same lady to her father-in-law and mother-in-law, and these were also not declared by her as part of her wealth.[5]

The Comptroller and Auditor General has similarly pointed out that a large industrial house escaped substantial wealth tax by holding unquoted equity shares of some companies under its control in a number of firms in which private family trusts were partners through their trustees. The firms and the trusts served as conduits for storage of valuable shares of the close companies. On a test check of the assessments in the cases of 13 of the private trusts, it was discovered that the book value of the unquoted shares had been accepted as the base for valuing the partnership interests of the trusts, and the under-assessment of wealth tax would be Rs. 4,57,384 for the assessment year 1976-77 alone, if the intrinsic worth of the shares or their probable market value in the event of their becoming saleable were taken into consideration.[6]

Since the same official does not always deal with the cases of the trusts as well as the beneficiaries, such escapement of properties from wealth tax assessment has been noticed by the Comptroller and Auditor General in several other cases also.

The avoidance is not limited to the non-filing of wealth tax returns or non-aggregation of the income of the beneficiary with his other income or under-valuation of assets.

The Comptroller and Auditor General has referred to a case in which the tax withheld from dividends has not been taken into account in evaluating the life-interest of the concerned beneficiary on the basis of his average income.[7] In one of the trusts, the trustee was himself the sole beneficiary. He sold some properties of the trust, making "long-term" capital gains to the extent of Rs. 2,51,155. While he accounted for his other income from the trust in his personal assessment, he offered the capital gains separately for tax in his capacity as a trustee, thus securing reduction in his tax liability to the extent of Rs. 84,873.[8]

The ruler of an erstwhile state, which has since been integrated with the rest of the country, created a trust for his wife with a sum of Rs. 6 lakh. He did not include the income from the amount so transferred in his own income or the asset in his wealth. The wife was separately assessed to the income tax and wealth tax, though if her income and wealth had been added to her husband's under section 64 of the Income-tax Act and section 4(1) of the Wealth-tax Act, the tax liability would have been heavier.[9]

The position in regard to the gift tax is no better, as evident from some of the cases scrutinised by the Comptroller and Auditor General. For example, unquoted shares of the same private limited company were transferred by a family group to several connected persons in 1973. The transferors and transferees were assessed to tax by different officers exercising jurisdiction over different "wards", though in the same city. While the shares gifted to the donees in one ward were valued at Rs. 7035 per share as against Rs. 7400 determined by the departmental valuer, shares transferred to two trusts in another ward were valued at Rs. 2668 per share, on the basis of an estimate made by a valuer appointed by the donor. The same lack of coordination between the concerned authorities is exhibited also in the cases of three private family trusts which contributed unquoted equity shares of three different private limited companies to certain firms in which they became partners, as part of their capital in the firms in the previous year

for their assessment for 1974-75. The values declared for the purpose of these transfers were Rs. 1800, Rs. 1404 and Rs. 122 per share as against the market values of Rs. 7730, Rs. 3650 and Rs. 219, respectively, per share, worked out by the departmental valuer and adopted in various other income tax assessments. Another private family trust of the same group made a similar capital subscription to a partnership concern in the form of shares. The value of the shares shown for the purpose of the transfer was only Rs. 1713 per share while the market value was Rs. 7200 per share. The Comptroller and Auditor General has calculated the gift tax which escaped assessment at Rs. 11,26,780 in the cases of all the four trusts together. A no less blatant case of evasion of gift tax was the transfer of 1000 shares of the admitted value of Rs. 2,57,620 to a private family trust which subsisted for the sole benefit of the transferor's son. The gift tax which had been avoided in this case was Rs. 44,655 in the assessment for 1976-77.

Cases of such escapement of not merely the gift tax but also the wealth and income taxes are not negligible in number, and the escapement cannot be attributed entirely to lack of coordination among the revenue authorities. The main object of the creation of trusts in most of these cases was only to bewilder the assessing officers: the smoke-screen created by the trusts hides and diffuses the tax liability. The Comptroller and Auditor General has referred, for instance, to a case in which two individuals created revocable private trusts in October 1969 and December 1971 and the revenue authorities failed to subject the income of these trusts amounting to Rs. 65,805 to the income tax for the assessment years 1977-78 and 1978-79 though they included the value of the assets in the relevant wealth tax assessment of the settlors : the short levy of income tax in these two cases amounted to as much as Rs. 53,040.[10] It will, however, be wrong to assume from such cases that if the revenue authorities are more alert, escapement of tax can always be prevented. As long as there are loop-holes in the law, it may not be possible to eliminate tax avoidance.

Common tax avoidance devices

A broad survey of some of the contrivances adopted by private trusts in India shows that they are not feeble imitations

of models elsewhere. Some of the methods that have come to notice through reports of cases which have been taken to the courts or through the annual audits made by the Comptroller and Auditor General are described below.

(*i*) *A specific trust as a mask for personal business*

Tax avoidance through family settlements, which assume the form of specific trusts, is sought to be counteracted through section 64 of the Income-tax Act.[11] The provisions of this section have been amended repeatedly, but many lacunae still remain. For instance, *A* can reduce his tax liability, distributing income from a source among as many beneficiaries as he likes, if he can find somebody, say *B*, to set up a trust for him (i.e., *A*), his wife and the other members of his family. *A* can be the trustee with power to commence a business with funds borrowed on behalf of the trust. *B* should be a person other than the relatives mentioned in section 64, *viz.*, husband, wife, father-in-law and grandfather. A big initial capital is not required : a nominal amount may serve as the nucleus. The power to borrow will enable the trust to obtain its working capital from *A* or concerns with which *A* is connected or the beneficiaries themselves or even banks or other outsiders. The profits of such a business, carried on by the trust, for all practical purposes, like a proprietary concern or a partnership, can be distributed to the beneficiaries, *viz.*, *A* and his family members, without attracting the aggregation provisions of section 64. If the concern is treated as *A*'s personal business, it may suffer tax at high rates. If it is held as a "registered firm" in which *A* and members of his family are partners, it will have to pay the income tax at rates ranging from 5 per cent on income in excess of Rs. 10,000 to 24 per cent in excess of Rs. 1,00,000 in addition to surcharge at 12½ per cent on the income-tax[12]. A specific trust is the simplest method of lowering one's tax liability.

If a business is transferred to a trust as a going concern, the income from the business may become liable to be included in the transferor's own income, if the beneficiaries are either the spouse or minor children or both.[13] If, however, the trust conducts a business with the transferred assets, e.g., dealings in shares of companies, it is only the income from the transferred assets, say dividends from shares, that will be caught by the

aggregation provisions of section 64 and not the gains from share-dealings.[14] The profits from the business in shares may be taxed to the beneficiaries either directly or through the trustees, but not to the author of the trust. It is the trust corpus that triggers the attribution provisions and its target is limited to the direct yield; a new business founded on loans is outside the firing range.

The innovation which dispenses with the annual rituals which firms have to go through for the continuance of their registration with the revenue authorities, has been getting increasingly popular after the courts held that there was nothing legally wrong with it. Since the income is derived by the beneficiary not from any asset entrusted to the trustee but out of the trustee's income-producing skills, the provisions of section 60 which seek to nullify transfers of income without transfer of assets, cannot be invoked for assessing the income in the hands of the trustee who conducts the business, though it is obvious that he is deliberately deflating his own income and average tax-rate by this means. The contention that the income from the business belongs to the trust and that it is receivable for or on behalf of the beneficiaries is supported by a court ruling.[15] There is also a ruling to the effect that if, under a settlement, a portion of the gains from speculation made with the settled resources is to be made over to the settlor, it cannot be held that the settlor is having a portion of the assets or income of the trust retransferred to himself and the trust is, therefore, revocable.[16]

An interesting illustration of the extent to which the Revenue is required to suspend its disbelief, is provided by the case of a lady who settled Rs. 5,000 in trust for the benefit of her son, his wife and his two minor sons. The son and his wife were appointed as the trustees. The trust-deed expressly authorised them to undertake a new business or industry. The trustees obediently ventured into business, which included consultancy services based on the professional experience of the son, in the interest of the four beneficiaries including himself, his wife and his two minor children. The revenue authorities sought to tax the son on the entire income of that business, but this was not approved by the court. The court held that the Revenue had no right to see through the

business to ascertain whether it was in reality the son's "show". According to the court, it is not permissible in law, so far as trusts are concerned, to pierce the veil as in the case of a company, with a view to finding out the person behind the scene. The trustees have been held to be under a legal obligation to carry out the objects of the trust and follow the directions in the trust-deed, subject to the provisions of the Indian Trusts Act. If they fail in their duty they are accountable for their omissions and commissions in their capacity as trustees.[17] This seems to be a case of the triumph of form over the substance of a settlement.

It is obvious that it will not be proper to leave the choice of taxable persons to judicial construction alone. If trusts are to have unrestricted freedom to manoeuver, resort to *benami* transactions will be rendered unnecessary. Tax can be comfortably avoided within the framework of the trust law.

(ii) Trusts for daughter-in-law and son's minor children

The utmost care will be required in making any modifications in the statute that may be called for, since the plugging of one loop-hole may sometimes result in the opening up of another. How an oversight in drafting can leave a gap, which the taxpayers are quick to exploit, can be illustrated with reference to trusts which are created for daughters-in-law and grandchildren, as substitutes for direct and indirect transfers of assets, which were covered by a provision in section 64(1)(vi) of the Income-tax Act, in accordance with one of the recommendations of the Direct Taxes Enquiry Committee (Wanchoo Committee).[18] However, it appears that generation-skipping is feasible even without a separate trust : a grandmother who has a life interest in the income from some settled property is free to assign it to her grandchildren. When there is diversion of income before it accrues in favour of the life-tenant there is no scope for taxing the life-tenant[19].

(iii) Cross trusts

Since direct transfers to spouse, minor child, daughter-in-law or minor child of a son are hit by the aggregation provisions of sections 64(1)(iv) and (v) of the Income-tax Act and 4(1)(a)(i) and (ii) of the Wealth-tax Act, log-rolling is resorted

to. If *A* and *B* find themselves in the same predicament, i.e., if both have close relatives to whom they want to transfer funds without being stalked by the Revenue, *A* can set up a trust for *B*'s relatives and *B* can create a trust for the members of *A*'s family.[20] The inter-relation between the trusts should not be manifest, for the courts have held that covenants actuated by a mutual understanding can be taken to form a single disposition.[21] But even replicated operations may be made less vulnerable if they are skilfully devised and staggered over a period of time. It is difficult for the Revenue to establish the motive of every transaction and to bring on record definite evidence to show that two transactions occurring on different dates were planned at the same time.

(iv) Trusts of brief duration in which discretion is exercised by beneficiaries

Since the scope for tax avoidance through the conventional specific trusts is limited and discretionary trusts have got into disrepute, new types of trusts have been evolved during the last ten years, with the following features :

(i) The period of duration of the trusts is divided into several sub-periods and the beneficiaries, who are usually young and have relatively small income, are shuffled from time to time. The trust provisions are also diversified for the different sub-periods, which never stretch beyond six years.

(ii) The income beneficiaries in each sub-period are specified, say, as *A*, *B*, *C*, and *D*. The trustee is authorised to offer the income of the trust first to *A*, say between the 1st September and the 30th October. If the offer is rejected by *A*, the trustee turns to *B* between the 1st November and the 31st December, and goes through a similar drill. The same motions are followed on every disclaimer. If the income cannot be distributed on account of renunciation by all the specified beneficiaries, the trustee can apply it to charities. This ritual is repeated with varied beneficiaries in each sub-period, till the end of the drama. In the last sub-period, the corpus of the trust fund is

distributed in definite, prescribed proportions either to the beneficiaries or their legal heirs or their nominees. The beneficiaries, who receive any income may declare it as part of their total income; and the trust itself will not be assessed to tax on it.

This is a type of trust in which the last word rests with the beneficiaries; and the trustees are not armed with any discretionary powers. How far annual disclaimers of interest are tenable is not free from doubt : a disclaimer is considered ineffective in Canada unless it is absolute and unqualified.

For purposes of the wealth tax, however, the uncertainties in regard to the quantum of wealth receivable by a beneficiary may result in the application of the provisions of section 21(4) of the Wealth-tax Act. Under section 2(e)(i)(v) of the Wealth-tax Act, an asset is so defined as not to include any interest in property, where the interest is available to an assessee for a period not exceeding 6 years from the date on which it vests in him. Since, in these trusts, the duration of the sub-periods is less than 6 years, none of the beneficiaries is likely to derive any interest from the trust fund for more than 6 years and therefore, the present value of the interest for such sub-periods cannot be considered as an asset assessable to the wealth-tax in the case of any of them. In the result, the wealth tax may be levied on the value of the assets held on trust either at the rates specified in Part I of Schedule 1 or at the rate of 3 per cent, whichever is more beneficial to the Revenue.

(*v*) *Charity as a beneficiary in a private trust*

The competence of a trustee of a charitable trust to embark on a business which does not subserve the primary purpose of the trust is open to doubt. However, if a business is held in a private trust, there can be no objection in law to making a charitable institution a beneficiary in it.[22] In such a private trust, the shares of the beneficiaries, including the charity, may be identifiable and the income of the charity will be liable to tax like the income of an individual or an association of persons. If one is unable to make donations to a public charity in excess of the ceiling prescribed for tax relief purposes under section 80G of the Income-tax Act, one can get round the restriction

by setting up a trust for carrying on his business and assigning a part of the business income to charity[23].

An interesting variant is a trust which is a public charity and a private family settlement by turns. Charity is declared as the sole intermediate beneficiary of the income and the corpus during the minority of a person in respect of whom the provisions of section 64 regarding income-splitting may otherwise be applicable.[24] Gift tax is also avoided in such a case.[25]

(vi) Ambivalence in regard to accumulation trusts

Accumulation trusts have not fared badly, thanks to judicial construction of the implications of accumulation of income in terms of a trust deed.

Section 64(1) (vii) of the Income-tax Act provides that in computing the total income of an individual, there shall be included all such income as arises, directly or indirectly, to any person or association of persons from assets transferred otherwise than for adequate consideration 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.[26] This provision does not appear to be adequate for aggregating the income accumulating for the benefit of an infant during the period of his minority, with the income of the parent who has made the settlement. It may cover a benefit that is immediately available, but the actual enjoyment of which is put off to a subsequent year but not one dependent on his becoming a major.[27] The distinction is between an income or a benefit that has materialised but that is stored for the beneficiary's advantage later and income or benefit that will accrue to the beneficiary only on a certain contingency.

When a settlement by a parent directs the capitalisation of the income every year till a child attains majority or for a specific period extending beyond the minority of the child, when the enlarged capital, with all its accretions, will be paid to him, the beneficiary has only a contingent interest, which will not ripen into a vested interest before he reaches the age of majority or the stipulated period expires. No benefit has immediately arisen and been shelved. In such circumstances, therefore, there is no income to be added to the income of the settlor.[28]

When the accumulated income becomes payable to the beneficiary eventually, he is no longer under the disability of infancy. He is capable of exercising his rights; and the income ceases to be includible in the income of the parent who made the settlement under the existing provisions of the Income-tax Act which cover only income accruing or arising to the child, immediately or on deferred basis, while he is still a minor.

The value of the property, which is held in trust, is includible, however, in the wealth of the parent who has transferred it to the trust as long as the beneficiaries are minor sons or minor unmarried daughters in terms of section 4(1)(a) of the Wealth-tax Act.[29] Such inclusion may be challengeable where a public charity is made the sole beneficiary of the income as well as the corpus for the duration of the minority of the settlor's children with the further stipulation that the charity will have the interest in the remainder, if the children do not survive their minority.

Where three separate trusts were created for accumulation of the income from shares in a private company for a period of ten years, the interest of the beneficiary, though contingent on his being alive beyond ten years, was held to be still includible in his taxable wealth from the vesting date.[30] The position would be different if the beneficiary had no right to demand that the trustees should spend any particular amount out of the trust fund for any of the purposes mentioned in the trust deed and the trustees had the absolute discretion to expend such part of the corpus as they thought fit for the benefit of the beneficiary. In such a case, the beneficiary's interest which is contingent, say, on his completing a certain age, will not be an asset includible in his or his parent's wealth.[31] The interest cannot be taken to be even contingent, if the trustees are empowered to distribute the corpus among the income beneficiary, his wife, and his children in the manner they consider best and on a date of their choice.[32]

(vii) A trust for a Hindu Undivided Family

While a discretionary trust has been surviving like a cat with nine lives and the accumulation trust is tied to minors, the specific trust has been widening the range of its service. It is possible to set up a trust exclusively for the benefit of all the

members of a family.[33] The converse, *viz.*, the creation of a trust by a Hindu undivided family for the benefit of its members is, however, disapproved by some of the courts because a trust cannot alter the course of devolution of property under the Hindu law of succession. Trusts can be created only with properties that can be gifted; and the assets of a Hindu undivided family cannot be abstracted from the family estate or gifted even to the members by the *karta* except in certain specific circumstances.[34] It may not, therefore, be proper to set up a trust with any assets of the family as the corpus for the benefit of some of the corparceners or even of all of them.[35]

Settlements are not, however, precluded in a case in which there is only one male member. No partial or total partition can be effected in such a family, in the absence of a coparcener entitled to demand partition; but settlements can be made by the *karta*, distributing assets among the ladies in the family. Shares in firms can be allotted by him to the individual ladies and the income from them cannot be added to the family's. The Hindu undivided family can thus divest itself of some of its sources of income and reduce its tax liability.

Even where the *karta* of a Hindu undivided family that has several coparceners sets up a trust with cash and other movable assets of substantial value, it is not free from controversy whether such a trust which may be voidable if the coparceners object, can be taken to be, *per se*, void[36], particularly if the claims of all the members of the family have been given due consideration in devising the trust. A family settlement, in which all the coparceners acquiesce, may sidestep partitions. A trust of this type offers an alternative to a partial partition, of which the income-tax authorities may refuse to take cognisance under sub-section 9 of section 171 of the Income-tax Act.

Apart from by-passing the legal objections to recognition of a partial partition, the creation of a trust safeguarding the interests of all the members of the family and making suitable provisions for them in conformity with the line of devolution prescribed under the Hindu Succession Act, 1956, has the advantage of avoiding the gift tax. Since the instrument of trust will merely define and specify the benefits which the individual members of the family will be entitled to and which they have been enjoying through their dormant rights in the family, there

is no transfer, as such, of any property. The coparceners will continue to hold in severalty what they would have obtained by the law of survivorship or on a partition, in the normal course.

It is open to a coparcener, who has interest in a trust property, to impress his interest under the trust with the character of Hindu undivided family property. Since section 58 of the Trusts Act permits any beneficiary, who is competent, to contract to transfer his interest, the coparcener can throw his right to receive any income from a trust property into the common stock of the joint family by making a unilateral declaration to that effect.[37] Section 64(2) of the Income-tax Act and section 4(1A) of the Wealth-tax Act have been recently amended to frustrate avoidance of tax by an individual's impressing his own property in this way with the character of a "Hindu undivided family" property. However, the amendment can still be made ineffective by creating a trust for the benefit of the members of the family individually, instead of transferring the income or the corpus to the joint family as such. The income and the assets cannot be added to the individual's income or wealth after the creation of the trust, unless the beneficiary is the spouse or a minor child.

(viii) A trust for a company or a chamber of commerce

There can be a trust of the shares of a company for the company's own benefit. While a company is prohibited from purchasing or holding its own shares by section 77 of the Companies Act in India, there is no bar on a shareholder's bequeathing his shares to the company. If a shareholder sets up a trust, a trustee appointed by the shareholder may hold the shares for the benefit of the company. Where a company holds its own shares directly, the effect is a reduction in its capital to that extent. The position is slightly different where the shares are registered in the name of a trustee; there is no reduction in capital, though the trustee will have to vote in accordance with the company's directions, whenever necessary.[38] A trust of this type raises the question of the tax treatment of the dividend declared by the company in respect of the shares in trust. The Companies Act, 1981, in the UK now allows a limited company to buy back its own shares out of distributable profits

or out of the proceeds of fresh issue. Earlier, this was prohibited by section 54 of the Act.

Equally intriguing is the case of a trust set up by a chamber of commerce for constructing a building and letting it out for meetings, etc., 75 per cent of the net collections being payable to the chamber. While the Comptroller and Auditor General has taken the view that the trust is liable to the wealth tax, the revenue authorities have assumed that it is saved from the tax, since the chamber, which is the main beneficiary of the trust income, is exempt from the tax. The Comptroller and Auditor General's point is that the ownership of the property does not vest in the chamber and the wealth tax liability, which attaches itself to the trust under section 21(1A), of the Wealth-tax Act, is not affected by the limited interest enjoyed in the income by the chamber.[39]

(ix) Partnership concern for thwarting the gift tax

A trust is a multi-purpose tool. It can secure large savings not merely in the income and wealth taxes, but also in the companion taxes, *viz.*, the gift tax and the estate duty. A gift has been defined to mean the transfer by one person to another of any movable or immovable property, made voluntarily and without consideration in money or money's worth. Accordingly, any property settled in trust in favour of any person other than a public charitable or religious institution is liable to the gift tax. The tax is avoided, however, by the transfer of a property, in the first instance, to a partnership concern which is formed temporarily. Since one cannot trade with oneself, there is no tax liability when properties which were acquired at a nominal cost years ago are passed on to the firm as part of the partner's capital.[40] As there is no bar under the Partnership Act to a trust's being a partner through a trustee,[41] the settlor and the trust that he has created can both be partners in a firm. The partnership may be dissolved after some time, the under-valued assets held by the firm being transferred to the trust at the value at which they have been transferred to the firm by the settlor against his capital in the firm. The transfer of the properties to the trust cannot be subjected to either the capital gains tax or the gift tax, in view of section 47 (ii) of the Income-tax Act and the general trend of opinion in the courts that is there is no

tax liability when assets are distributed by a firm to its partners.[42]

(x) *Artificial stipulations in regard to sale of trust property*

Where a covenant provides that a certain property held in trust can be sold only to the beneficiaries and at a price fixed in the covenant or the trust deed, the market value of the property is, for tax purposes, ordinarily to be pegged to the value specified in the covenant or trust deed. A provision has been made in the Wealth-tax Act with effect from April 1, 1980, to ignore any such restriction in the valuation of the property for wealth-tax purposes.[43] In the absence of a similar provision in the Gift-tax Act, the gift tax and estate duty liability can be substantially lowered through such covenanted restrictions when any property is gifted in settlement. If *G* has thus left a property to *S*, his son, subject to the condition that if he sells it, the first option to make the purchase should go to his grandsons or any other relatives who need pay only a specified amount (which is much less than the market value), gift tax and estate duty will be assessable only on the value so frozen, though the market value may be the basis adopted in a comparable case without any such condition. An amendment to the Gift-tax and Estate Duty Acts, similar to the one already made in the Wealth-tax Act, may remove this discrimination. The market value does not diminish merely because there is a dynasty situation, i.e., a gift is made within the family and the asset gifted has been received as a part of the family heritage. The anomaly is heightened when a larger tax is demanded in similar circumstances where the only element that is lacking is the grandfather's fiat.

(xi) *Deemed gifts outside the purview of the Estate Duty Act*

A novel technique use to foil the gift-tax liability was utilisation of powers of appointment and release of interest. The beneficiary who had the powers of appointment and also the right to release his interest in a trust, designated several other trusts as beneficiaries in his place and thereafter relinquished his interest in the trust. By this process a beneficiary transferred his interest from one set of trusts to another without incurring any gift-tax liability on the transfers. This device was counteracted by amending the definition of the expression "transfer

of property" in section 2 (XXIV) (c) and also including a provision covering renunciations of interest in section 4(1)(e) of the Gift-tax Act. The exercise of a power of appointment of property vested in any person who is not the owner of the property, to determine its disposition in favour of any person other than the donee of the power, is to be taken as "transfer of property" with effect from April 1, 1980. It will be immaterial whether the power of appointment is general, or special or subject to any restrictions as to the persons in whose favour the appointment may be made. Similarly, where a life tenant or a remainderman surrenders or relinquishes his interest in the property or otherwise allows his interest to be terminated without consideration or with inadequate consideration, the value of the interest surrendered or forfeited shall also be deemed to be a gift after April 1, 1980.[44]

There are, however, areas where these amendments to the Gift-tax Act may not achieve their object. To illustrate, the terms of a settlement were altered and the settlor's son made the sole beneficiary under the powers reserved to the settlor. The settlor thereafter released and disclaimed his power of revocation and alteration or new appointment of beneficiary. The court held that the change in the beneficiary was a unilateral act and the subsequent *bona fide* surrender of the power of appointment would not be chargeable to the gift-tax. The contention of the Revenue was that in view of the power of revocation, the settlor should be taken to have been the absolute owner of the trust assets till he appointed his son as a beneficiary and surrendered his powers of fresh appointment or change. This was not accepted by the court.[45]

The estate duty is chargeable on gifts other than charitable gifts, made by the deceased less than two years before his death. In the absence of any provision to hold that, in this context, gifts should be taken to include releases of life interest, etc., deemed to be gifts under the Gift-tax Act, there is no scope for including the value of the relinquished life interest, etc., in the estate of the deceased for estate duty purposes. There is no transfer of property within the meaning of section 53 of the Transfer of Property Act where the life-estate holder surrenders his interest and thereby accelerates the interest of the remaindermen. The courts have held that there will be no estate

duty liability where the surrender has been made in favour of the entire body of persons with reversionary and absolute interest and not in favour of any chosen individuals forming part of the body of remaindermen. The release of life interest is a self-induced, unilateral action, while a gift is, ordinarily, a bilateral transaction.[46]

(xii) Discretionary trusts

The reduction in the maximum rate of income tax including surcharge to 67.5 per cent in non-company cases and the levy of tax at that rate on discretionary trusts have diminished their attraction but not put them out of commission. The reason is that the proviso to section 164(1) makes exceptions in certain circumstances. One of these exceptions relates to a trust in which "none of the beneficiaries has any other income chargeable under this Act exceeding the maximum amount not chargeable to tax in the case of an association of persons or is a beneficiary under any other trust." If a trust has two private limited companies as its beneficiaries and the income of each of them is below Rs. 15,000 they will gain by this provision, since the tax-exempt threshold for an association of persons is Rs. 15,000 at present. This is a gap in the fence which requires mending. The proviso to section 164(1) lays down that tax shall be charged on the discretionary part of a trust's income "as if it were the total income of an association of persons",[47] and once the trust is charged to tax, the beneficiary companies cannot be assessed on the same income again on its distribution to either or both of them. Persons controlling or owning non-industrial private limited companies which are liable to tax at 65 per cent plus surcharge on their total income may plan to form trusts if the other income of the companies is below Rs. 15,000.

There is also scope for tax savings schemes based on the absence of a definition of the term "beneficiary". One can contend that he does not become a beneficiary till he actually receives a benefit and that the mere right to consideration by the trustee while distributing the trust income does not make that income belong to him. He can not, on this count, be deprived of the benefit conferred by clause (i) of the proviso to section 164(1). If two persons are eligible to receive benefits

under several discretionary trusts and they have no other income of their own chargeable to the income tax, and if the trustees of none of the trusts distribute any income to them during the relevant year of account but accumulate the income under the terms of the trust deed, the trusts having income above the tax-exempt threshold will be liable to pay tax as if their total income is that of an association of persons.

Another exception to the operation of the provisions of section 24(1) seems also to be unwarranted. A discretionary trust that has been constituted under a will escapes the automatic application of the maximum marginal rate to its entire income, if it is the "only trust so declared" by the testator. This stipulation has little relevance to the issue, for even a single discretionary trust can cause a large loss of revenue. And if it is a "warm body trust", its corpus may continue to receive transfers of valuable properties from relatives and friends of the testator or the beneficiaries even after the testator's death. It will not cease to be a testamentary trust merely because of its subsequent growth.[48]

Some confusion has been created by the introduction of section 167-A dealing with "associations of persons" from April 1, 1981. The new provision charges tax on the total income of an association at the maximum marginal rate, where the individual shares of the members (other than a company or a cooperative society) in the income of the association are indeterminate or unknown.[49] What are the implications of the proviso to sub-section(1) of section 164 in this context ? Will all the exceptions to the general rule regarding application of the maximum marginal rate to a discretionary trust cease to be relevant after April 1, 1981, since the income of a discretionary trust which satisfies any of the conditions set out in the proviso to sub-section (1) of section 164 will suffer tax "as if it were the total income of an association of persons"? There is a fear that the proviso may be taken to be nullified by section 167-A on the ground that a discretionary trust is, in effect, an association with members whose shares are indeterminate or unknown. The argument is that if the beneficiaries of a trust are to be assessed like an association of persons, section 167-A coalesces with the proviso to sub-section (1) of section 164. Tax will accordingly be chargeable at the maximum rate, even if none of the bene-

ficiaries is a beneficiary under any other trust or has any other income chargeable under the Act. The position may be the same where the trust is a testamentary one and the testator has not been responsible for any other trust. This fear may be unjustified in view of the fact that section 164 is directed against the trustees, who are representative assessees and not against the beneficiaries, and that in the absence of an express provision to the contrary, trustees of the discretionary trusts coming within the purview of the proviso will be liable to pay tax under the proviso and not as an association under section 167-A. The fact that discretionary trusts which conform to the provisions of the almost identically worded proviso under section 21(4) of the Wealth-tax Act are required to pay tax at the relevant marginal rates specified in Part I of Schedule I to the Act and not like an association of persons with members whose shares are unknown, governed by section 21AA of the Wealth-tax Act, supports the view that the proviso to section 164(1) is unaffected by the new section 167-A of the Income-tax Act.

The attack on discretionary trusts under the Wealth-tax Act is two-pronged. In determining their total wealth, no deduction under clauses XV, XVI, XXII, XXIII, XXIV, XXV, XXVI, XXVII, XXVIII and XXIX of section 5(1) of the Wealth-tax Act is allowed, vide explanation 2 to section 21(4) of the Wealth-tax Act. This means that even if the funds of discretionary trusts are invested as deposits in banks or cooperative societies or under schemes notified by the Central government or in Government securities, shares, approved debentures, etc., such investment will not enable them to get any relief in the computation of their net wealth. Apart from this, a discretionary trust has to pay tax on its net wealth at the rate of three per cent or at the rates specified in Part I of Schedule I, whichever course is more beneficial to the revenue. The categories of trusts that are saved from the operation of section 164(1) of the Income-tax Act are, however, excepted for wealth tax purposes also, under the proviso to section 21(4) of the Wealth-tax Act. Tax will be levied in the excepted cases at the rates specified in Part I of Schedule I.

If the discretionary trusts have not been jettisoned despite the severe damages they have suffered through the amendments to the Income-tax and Wealth-tax Acts during the last few

years, it is because they have not ceased to be serviceable, in certain circumstances, even for avoidance of these taxes, and they are not hit by the estate duty. The estate duty is attracted only by property which "passes" on an individual's death, i.e., property which he has left or which changes hands or in which rights have been modified by reason of his death. Since no such consequence can follow where any property is held in a discretionary trust and the deceased is only one of several persons eligible for consideration by the trustees while assigning the benefits available in the trust, the property is unharmed by the estate duty.

Properties under discretionary trusts were escaping the duty in the UK also till, by an amendment of the law, the dutiable slice of the trust capital was worked out on the basis of the income paid to a beneficiary during a specified period preceding his death, expressed as a fraction of the entire income of the trust during that period. As pointed out in Chapter 4, the change in the law to enable the determination of the property passing on the death of a discretionary beneficiary at a proportionate value of the corpus based on the ratio of the income derived by the beneficiary discouraged the formation of these trusts to some extent; and the current levy of a periodical capital transfer tax on all properties held in discretionary trusts may further contribute to their discarding.

Where a settlor is himself one of the discretionary beneficiaries, he has been held in India to have reserved to himself an interest in the settled properties and thus been trapped by section 12 of the Estate Duty Act which subjects settlements with reservation to the estate duty.[50] The implied assumption is that the trustees are likely to be susceptible to the settlor's influence. If this assumption is carried to its logical conclusion, the trustees may follow the settlor's secret instructions even if he is not a direct beneficiary himself, and the settled property should be deemed to pass on his death. This conclusion is not, however, acceptable to courts. A trust does not cease to be discretionary even if there is only one surviving beneficiary, and the trustees can either refrain from application of the trust income or make payments to the beneficiary. It is only if the beneficiary is entitled to assign or surrender or release his interest in the trust that he will be liable to the wealth tax and

that the estate will be subjected to the estate duty on his death. The need for a modification of the Estate Duty Act is obvious.

(*xiii*) *Purchase of interest after death*

Certainty has been counted as one of the principal merits of the levy of the estate duty; but how one can give the slip to the duty on death is shown by a trick taking its cue from a decision in the House of Lords in the UK. All that is necessary is the acquisition of the remainderman's interest for a short period extending beyond the life-tenant's death, and its "grafting" on the life tenancy. This results in the continuance of the life-tenant's interest in the property in question till the expiry of the stipulated period, even after he has closed his eyes on this world. According to the House of Lords, what passes on the death of the life-tenant in such a case is only the actuarial value of the interest superimposed on the life-tenancy for the short while that it is projected beyond the grave.[51]

(*xiv*) *Reservation of benefit without charging it to any specific asset*

Certain provisions of the Indian Estate Duty Act are in *pari materia* with those which were in force in the UK till 1975. Despite this fact, however, there is an occasional divergence in the construction of almost identical provisions.

The Supreme Court in India has, for example, held[52] that duty cannot be charged under section 10 of the Estate Duty Act unless the benefit reserved to the deceased has arisen out of the gifted property itself and that a collateral benefit will not be adequate to attract it. This differs from the view taken in the UK.[53] The Supreme Court decision can lend itself to abuse by enabling a settlor to reserve all the benefits he wants for himself without specifically charging them on the estate settled by him. As long as the benefits do not attach themselves to any particular asset, the Revenue cannot reach them.

(*xv*) *Annuities payable by a trust*

A good way of reducing tax liability for the head of a family owning and managing a thriving business may be to have the ownership of the business transferred in trust for the benefit of his children, keeping for himself only the right to a

fixed annuity for life. The same course can be availed of for transfer of patents, copyright and the like to the family without attracting gift tax liability, for the annuity can be reasonably argued to be the consideration for the transfer of the assets. The trust is thus used as a pipe through which assets as well as the taxpayer's income pass to the recipients.

While a life interest in the income from a property is, in a sense, a life interest in the capital, an annuity does not have to be correlated to any fixed proportion of the capital.[54] An annuity is a fixed amount, unaltered by changes in the yield of a trust property[55], and where a beneficiary receives an annuity from a trust, it cannot be said that his interest in the trust is indeterminate or unknown.[56] What is important is the intention of the settlor—whether the beneficiary has been offered a pre-determined sum every year, encroaching on the capital if there is a short-fall in income, or whether he can get only the net income of the trust fund.[57] Section 40 of the Estate Duty Act provides that the value of the benefit accruing or arising from the cesser of interest on the death of the beneficiary shall

(i) if the interest extends to the whole income of the property, be the principal value of the property; and

(ii) if the interest extends to less than the whole income, be the principal value of an aliquot part of the property, i.e., proportionate to the income to which the interest extended.[58]

Where an annuity of a fixed amount is payable, the annuitant can accordingly be taken to be entitled to such proportion of the capital as his annuity bears to the whole income of the settled property[59].

It is interesting to see how the drafting of an instrument can determine whether a receipt is liable to or exempt from tax. If a settlement provides for an annuity, vesting the trustees with the discretion to make up deficiencies in income by drawing on their capital, the entire annuity is treated as income.[60] Capital sums which are successively received, stand the risk of being treated as income[61], unless the amounts vary, there is no regularity in the receipts and the payments are not planned in the trust deed. Sometimes the settlor is stung by

the income tax when he receives his own capital back.[62] But in the UK where a capital sum was paid by a charitable organisation in consideration of which the recipient covenanted to make annual payments, it was held that the payments were not really annuity in terms of section 52(1) of the Taxes Act 1970; the payments were treated as contributions to charity, in respect of which the charitable organisation claimed tax refund. When it was argued that Parliament could never have intended to exempt from the taxing provisions any arrangement solely designed to obtain fiscal advantages as in this case, Lord Wilberforce observed that such a canon of interpretation would not be workable. The question to be decided was whether a certain series of transactions in a certain legal form did or did not fall within the taxing words. If they did not, Parliament could change the law if it liked but the subject was entitled to be judged under the law as it stood at the relevant time.[63]

The precise terms of an instrument of trust are no less decisive in determining the liability to the wealth tax where an annuity is granted to a recipient for life and thereafter equally to all his children. If the annuitant is not entitled to call upon the trustee to commute the annuity into a lump sum grant or sell it for a capital payment or otherwise dispose of it, its value is excluded from his net wealth under section 2(e)(1)(iv) of the Wealth-tax Act.[64] It is only if the annuitant is vested with powers of disposition over the annuity, that the capitalised present value of the annuity will be included in his wealth for tax purposes. It is odd that the present value of life tenancy should be subjected to the wealth tax, but an annuity for a fixed amount for the life of the beneficiary should be exempted from the tax, though the value of the annuity can also be computed, like the value of life tenancy, on the basis of the life expectancy of the annuitant. An annuitant may have no more freedom to negotiate with the trust for a lump sum in settlement of his annuity than a life tenant in regard to his life tenancy. Any tax differentiation based on their respective rights to demand commutation would be artificial.

(*xvi*) *Personal services and income-earning assets*

There is no scope for setting up a trust for professional services.[65] Section 5 of the Indian Trusts Act visualises only

an obligation attached to property; and the most important characteristic of a property is that it shoulb be capable of being owned. The personal skill of a person cannot be classed as property for which a trust can be constituted. A trust cannot hinge on the services or professional competence of a third party. There cannot be a vested right to the services or the income earned by any individual. A trust cannot be founded on a transfer of income, but on the property which yields the income.[66] However, there is no legal impediment to a business being conducted by a trust and the services of individuals being fully utilised by it, with or without remuneration. Thus, if a doctor functions as a free consultant in a medical shop held in trust for his wife and minor son, to which he has not himself transferred any asset, no income can be attributed to the doctor and assessed in his hands. Since the object is to minimise the family taxes by accepting no fee or less than full compensation for the services, where a father undertakes to manage a corporation or a business that is held in trust for the benefit of his wife or children, there is reduction in the overall tax obligations of the family. There is no remedy in law, at present, to escapement of proper tax liability through the use of an individual's initiative, expertise and experience in the service of his family through the trust ploy. It is only the transfer of his financial and physical assets that is caught by the Income-tax and Wealth-tax Acts.

In the USA,[67] a taxpayer, on the termination of his insurance agency, assigned to a family trust his right to receive the renewal commission which he had earned through the insurance policies secured by him in the earlier years. Since the taxpayer was following the cash method of accounting, the commission could not be taxed to him unless he actually received it in cash. The commission was subsequently collected by the trustees and held for the benefit of the family members. The question was whether the commission was includible in the taxpayer's income or the assignee's income. The Court of Appeal held that it was a case of transfer of a property right. However, the Supreme Court reversed the order, holding that the mere power to collect commission was insufficient to shift the income to the assignee for tax purposes. Personal services income did not become property which could be transferred to any other tax payer. It

is difficult to say what view courts in India would take on the facts of this case. It is evident, however, that this is a case in which the services which had earned the right to the income had already been rendered. What had been postponed was the mere realisation of the income. Irrespective of whether the commission agent was taxable on the cash or mercantile system of accounting, the income was his and what he had assigned to his nominees was only his right to receive it or a debt. A case of this type does not pose as much difficulty as one in which some of the important ingredients of a business other than capital, e.g., entrepreneurship, managerial skill and personal labour are placed at the disposal or a trust by the settlor.[68] This is analogous to an individual's running a company for the advantage of his family, the shareholders of the company being members of his family. It is the difference in the tax treatment of a company and a trust that operates in favour of trusts; a company suffers tax at a relatively high rate on its entire income, while a specific trust entails tax on the beneficiaries at the marginal rates appropriate to their respective incomes.

(xvii) *The advantage in unauthorised use of trust assets by settlor*

Under section 63(a) of the Income-tax Act, a trust may be deemed to be revocable and its entire income added to that of its author if its instrument contains any provision for the retransfer, directly or indirectly, of even a part of its income or assets to him. While it will be courting trouble to provide for the exercise of unlimited powers by him which may result in the treatment of the trust income and assets like his income and assets[69], a subtler way of achieving the same end is probably to reserve only the power to advance loans.[70] Courts have held that this power is subject to the general law of trusts and will not be hit by section 63(a).[71] Even if the loan is availed of by the settlor himself and not by any concerns connected with him, money that is lent cannot be construed as retransfer of the income or assets of the trust to its author.[72] And if a benefit is enjoyed from the trust, despite there being no provision in the instrument authorising it, the beneficiary may protest or take legal action against the author and the trustees, but the revenue

has no cause for grievance. An impropriety on the part of the trustee or even settlor cannot justify the trust's being deemed to be revocable for tax purposes.[73] It is only a lawful right to reassume power over the trust assets that can result in the trust's being held revocable,[74] not an abuse of power.

(xviii) Trust assets used by beneficiary or his nominee or a concern in which he is interested

Trusts are also copying some of the tax-avoidance methods orginally patented by companies, without being subjected to the latter's disabilities. For instance, where a trust lends money to the nominee of a beneficiary, or a firm or a company in which the beneficiary or a close relative of the beneficiary is interested, without charging any interest, or on an interest which is much lower than the commercial rate, the advantage enjoyed by the beneficiary or his nominee or relative or associate from such a loan cannot be deemed to be income derived by the beneficiary for purposes of determining his liability to the income tax.[75]

Where a house which a trust can let out on a good rent is occupied by the beneficiary, the beneficiary can be assessed to tax on the basis of the rent that may be payable or might have been ordinarily paid for the house earlier, and also for the tax, if any, paid by the trustee.[76] If the house is permitted to be occupied by a nominee or a relative of a beneficiary for his residence at a pepper-corn rent or for being sublet to the advantage of the nominee or relative, there is no reason why the income which the trust has deliberately foregone should not be reckoned to be a part of its income for tax purposes.

These are not mere theoretical niceties but possibilities which have been recognised in section 13(1)(c) of the Income-tax Act dealing with cases in which the income or property of a charitable or religious institution is applied or used for the benefit of the author of the trust, any of the trustees or any of their relatives. It is only because discretionary trusts have been diverting their income to such of their beneficiaries as are liable to less tax than the others, that they have received so much legislative attention.

A typical example of the constant battle of wits between the taxpayer and the Revenue is provided by the wealth tax treatment of jewellery. A benefit in kind which was exempt

from the wealth tax till March 31, 1963, was use of jewellery held in trust.[77] The amendment of section 5 (1)(viii) of the Wealth-tax Act in 1971, with restrospective effect from 1963, withdrawing the tax exemption in respect of jewellery, had the effect of chasing the jewellery to take refuge in "close" companies which were not liable to the tax. Trusts were driven to hold shares of the close companies instead of the jewellery. This shelter has now been pulled down by section 40 of the Finance Act, 1983, which has revived the levy of the wealth tax in the case of close companies with effect from the assessment year 1984-85.

(*xix*) *Provisions out of step with public policy*

Under the Hindu law, the illegitimate son of a *brahman*, *kshatriya* or *vaishya* is entitled to maintenance and not to any share of inheritance, while the illegitimate son of a person belonging to any other castes is entitled to a share of the inheritance subject to certain conditions.[78] An illegitimate Muslim child does not inherit at all from either of its parents under the *Shia* law, while under the *Sunni* law, it inherits from its mother and other relations though it cannot inherit from the legitimate son of the same mother.[79]

The position in regard to a couple who cohabit without being married or whose marriage is voidable is similar. Neither of them has any claim on the other's property as a matter of right.

The treatment of income from assets transferred directly or through a trust to a child born out of wedlock or to its mother is, however, more liberal under the Income-tax and Wealth-tax Acts in India. "Child" includes an illegitimate child under section 444(1) of the UK Income and Corporation Taxes Act, 1970, but not under section 2(15A) of the Indian Income-tax Act, 1961.

The minor's income from a trust created by either of his parents is aggregated with the income of the concerned parent; and if the trustee is a partner in any firm for the benefit of the child, the share income is also included in the tax assessment of the parent with the larger income. These aggregation provisions do not, however, apply to persons who have illicit relations with each other or their offspring.[80] This differential treatment

is not in harmony with the provisions of any of the personal laws, and it serves to encourage the rich to enter into what have been called *Maitreyi Krar*—a friendship or companionship "contract"—which may be mere euphemism for concubinage.

It is significant that the English and the Australian laws have specifically removed the disabilities from which children born out of wedlock suffer; and such reform merits consideration in India too. However, irrespective of any reform that may be brought about in the personal law, particularly the law of inheritance, in this regard, it is evident that there is hardly any justification for extending a more favourable tax treatment to assets and income diverted to a person with whom one has been living in contravention of the law or a child born of a relationship not recognised in law, than to one's lawfully wedded spouse or a child of such union. It is true that tax laws do not have to take up moral postures but they certainly have to conform to the law of inheritance and other laws. Any concession, even if it is unintended, to those involved in transgressions of the law is untenable. A few stray deviations from conventions may not require notice in a permissive society, but what has been publicised as *Maitreyi Krar* is a recent phenomenon which cannot be ignored, since it is not negligible in scale, and it is incident to money-power and high life.

A similar anomaly resulting from the same blind attachment of importance to formal connubial relationship in disregard of realities is noticed in the treatment of direct or indirect prenuptial and post-nuptial transfers to a spouse. If a taxpayer transfers funds or other assets directly to his wife or has them held in trust for her, section 64 of the Income-tax Act and section 4 of the Wealth-tax Act immediately swing into operation. They require the inclusion of the income and the value of the transferred assets in the taxpayer's assessments to the income tax and wealth tax. If he is careful to do his tax-planning, he will set up a trust for the lady of his choice before he leads her to the altar.[81] It is passing strange that marriage, which unites a couple, should be taken to be the dividing line for tax purposes. Pre-marriage financial arrangements are considered sacrosanct and the revenue cannot go behind or ignore them; but the husband and wife are treated as one flesh and the tax

liability in respect of transfers of assets made after their marriage fastens on the transferor.

(*xx*) *Liability to the wealth-tax and estate duty where property is held in a private religious trust*

A Hindu deity is assessable as an individual through its *shebait*.[82] Trusts for worship of family deities are subject accordingly to the income tax[83]. Similarly, the *mutawalli* of a *waqf* functions like a *shebait* and is assessed to the income tax, although the *waqf* property is dedicated to God. The position is, however, not clear in regard to the wealth tax and estate duty. Properties settled in trust for "poojas" (offering of prayers to God) and other ceremonies that have been and are being performed for the benefit and well-being of the author and the members of his family cannot be aggregated with the author's wealth, since they are not for his individual benefit or the benefit of his wife and minor children alone. The trustees would be liable for assessment under section 21 of the Wealth-tax Act but there is no scope for the inclusion of the properties in the wealth of the settlor under section 4(1)(a)(iii) of the Wealth-tax Act[84] or for subjecting them to estate duty liability on the death of any of the members of the family who might have derived any spiritual benefit from them. So far as *waqfs* are concerned, it has been held that the right of a beneficiary to receive remuneration[85] or an aliquot share of the net income of the *waqf* property is an asset within the meaning of the Wealth-tax Act and that the capital value of such a right is assessable to the wealth tax[86].

It would appear that it is only the right of the *shebait* to any benefit from a Hindu private religious trust that is liable to the estate duty on his death. All properties dedicated to a deity in a Hindu endowment seem to be outside the purview of the Estate Duty Act, since the property belongs in perpetuity to God.[87] But, if the matter is considered objectively and realistically, the conclusion is irresistible that every private religious or quasi-religious trust, including a *debuttar* estate that is served by a *shebait*, a *math* that is managed by a *mahant* and a *waqf* that has a *mutawalli* to superintend it, should be subjected to both the wealth tax and the estate duty. Semi-religious endowments in which the public have no interest provide easy

means of avoidance of the wealth tax and the estate duty. The argument against the levy of the wealth tax on the estate as a whole is that God is treated as an individual only for the limited purpose of income tax liability of a *debuttar* estate. How far section 21(A) of the Wealth-tax Act will aid the Revenue in taxing the entire value of a *debuttar* or a *waqf* estate is yet to be tested in the courts while the estate duty is clearly out of the question[88]. The tax liability will be negligible if it is determined with reference to the usufruct of the individual beneficiaries, if any. In fact, even the income tax liability is inconsiderable in the case of a private religious trust, which is free from the inhibitions imposed by sections 11, 12, 12A and 13 of the Income-tax Act on a public religious or charitable trust, e.g., treatment of voluntary contributions as income. A private religious trust enables enjoyment of the exclusive privileges and other obvious advantages of privacy, including the performance of personal acts of piety, at the cost of the Revenue. The corpus of the trust, which is inalienable, passes also to the legal heirs and successors of the settlor, in perpetuity, without any erosion attributable to tax at any point of time. A private religious trust may not even come to the notice of the Revenue because it is not required to be registered with the Commissioner of Income Tax under section 12-A of the Income-tax Act.

NOTES

1. Hearings on Tax Reforms Act of 1969 before the House Committee on Ways and Means, 91st Cong., 1st Sess., pt. 11 at 3978-85 (1969).
2. CIT v Smt. Sindhubai Vasant Sahukar (1981) 7 Taxman 188 (Bom.); (1981) 24 CTR (Bom) 153; CIT v Bai Savita Gouri and others (1975) 100 ITR 680 (Bom).
3. Manilal Dhanji v CIT (1959) 35 ITR 647, affirmed in (1962) 44 ITR 876 (SC), vide paras 2 and 4 of the statement of the case at pp. 468-9 of 35 ITR; CIT v Mrs. Jayalakshmi Duraiswamy (1964) 53 ITR 525 (Mad).
4. C & AG, 1977-78, p. 123.
5. C & AG, 1973-74, pp. 140, 143 and 144.
6. C & AG, 1981-82, p. 173.
7. C & AG, 1974-75, p. 211.

8. C & AG, 1978-79, p. 211.
9. C & AG, 1974-75, p. 211.
10. C & AG, 1981-82, pp. 205-6, 200-1 and 153-4.
11. Tulsidas Kilachand and Others v CIT (1961) 42 ITR 1 (SC). In this case the Court held that love and affection as the consideration for declaring a trust for the settlor's wife might be good enough to support a contract but not adequate to avoid tax.
12. The surcharge which used to be 10 per cent has been increased to 12.5 per cent with effect from April 1, 1983.
13. Tulsidas Kilachand v CIT (1961) 42 ITR 1 (SC). Occasionally, a scheme may recoil on the originator, as witnessed in the case of Radhas Printers v CIT, Kerala and Others (1981) 132 ITR 300 (Ker), where the partners of a firm chose to turn into beneficiaries of a trust and, in the process, lost the firm's development rebate.
14. Executors of the Estate of the late J.J. Kapadia v CIT (1968) 67 ITR 590 (Bom).
15. A. Razaak v CIT (1963) 48 ITR 276 (Cal); CIT v Balwantrai Jethalal Vaidaya (1958) 34 ITR 187 (Bom); Khan Bahadur M. Habibur Rahman v CIT (1945) 13 ITR 189 (Pat).
16. CIT v Jitendra Mallick (1963) 50 ITR 313 (Cal).
17. K.T. Doctor v CIT Gujarat IV (1980) 124 ITR 501, 513 (Guj). Also see J. K. Trust v CIT (1957) 32 ITR 535 (SC) where a managing agency was held by the SC to be property held in trust, and Dharma Vijaya Agency v CIT Bombay City (1960) 38 ITR 392 (Bom), where this SC decision was applied and insurance agency conducted by a partnership was also treated as "property" held in trust. Both the J. K. Trust and Dharma Vijaya Agency were found to be public charitable trusts. As for the doctrine of lifting the veil in tax matters relating to companies, the following is the Supreme Court's observation :

   "It is true that from the juristic point of view the company is a legal personality entirely distinct from its members and the company is capable of enjoying rights and being subjected to duties which are not the same as those enjoyed or borne by its members. But in exceptional cases, the court is entitled to lift the veil of corporate entity and to pay regard to the economic realities behind the legal facade". CIT Madras v Sri Meenakshi Mills Ltd. (1967) 63 ITR 609 (SC); Juggilal Kamlapat v CIT (1969) 73 ITR 702 (SC).
18. Direct Taxes Enquiry Committee's Report, 1971, p. 77, para 3.37.
19. CIT v Smt. Kamlabai Juthalal (1977) 108 ITR 755 (Bom).
20. Sec. 64(1)(a)(vii) of the Income-tax Act and 4(1)(a)(iv) of the Wealth-tax Act. Also see IR v Clarkson Webb (1932) 17 TC 415; CIT v A.N. Chowdhury (1969) 71 ITR 326 (Cal), calling for an interpretation of sec. 16(3)(b) of the Income-tax Act, 1922 and CWT v B.N. Chowdhury (1978) 112 ITR 725, regarding sec. 4(1)(a)(iii) of the Wealth-tax Act, which was in *pari materia* with it before its amendment hitting "indirect" transfers of assets under the Wealth-tax (Amend-

ment) Act, 1964, taking effect from April 1, 1965. See also CIT v Framji Commissariat (1967) 64 ITR 588 (Bom), where a distinction was made between direct cross transfers and cross transfers through trusts.

21. CIT v C. M. Kothari (1963) 49 ITR 107 (SC); CIT v Keshavji Morarji (1967) 66 ITR 142 (SC); Amarchand Jalan v CIT (1964) 54 ITR 80 (Bom). Also C & AG, 1977-78, p. 112, para 62(i).

22. Hakim Abdul Hamid v CIT (1973) 90 ITR 203 (Del), where 7/8th of the income of the business styled "Hamdard Dawakhana" was exempt from tax, being required to be spent on public charities, and 1/8th was to be paid to the sole *mutawalli*.

23. The business income of a charitable or religious trust/institution is liable to tax from the assessment year 1984-85 in terms of s. 11(4A) of the Income-tax Act. However, an individual may still derive tax advantages by giving a share in a business conducted by a private trust to charity. In some cases, this course may be preferable to a donation under section 80G of the Income-tax Act.

24. H.H. Yeshwant Rao Ghorpade v CWT Bangalore (1966) 61 ITR 444 (SC). It is open to question whether the amendment of section 4(1)(a)(iii) of the Wealth-tax Act by the Wealth-tax (Amendment) Act, 1964 whereby the aggregation rule was extended to assets transferred to a trust or a third party for the "immediate or deferred" benefit of a minor child would help the Revenue. If the asset is to be used for the benefit of a charity as on the relevant valuation date, and the settlor's son becomes eligible for its enjoyment only after he attains majority, it is possible to argue that there is no deferment of benefit to minor child. The minor child is not beneficiary at all during the period of his minority. See also n. 25 below.

25. CGT v Lady Hirabhai C. Jehangir (1982) 138 ITR 314 (Bom.); CGT v G. G. Morarji (1965) 58 ITR 505 (Bom); CGT v Yogendra N. Mafatlal (1965) 58 ITR 40 (Bom). The view that the children and others have only a contingent beneficial interest in such cases has been doubted in Vadulla Venkata Rao v CGT (1972) 85 ITR 249 (AP).

26. K.M. Sheth v CIT/CWT (1977) 107 ITR 45 (Bom); Additional CIT Gujarat v M.K. Doshi; CIT Gujarat III v Smt Devkunverben M. Doshi (1980) 122 ITR 499, 505 (Guj); Yogendraprasad N. Mafatlal v CIT (1977) 109 ITR 602 (Bom); Shardaben Mulji v CWT (1977) 106 ITR 667 (Bom); S.M.S. Ratnaswami Nadar v CIT (1975) 100 ITR 669 (Mad); CIT v B.A. Dalal (1974) 96 ITR 408 (Pat); Maharani Vijaya Kunverba Saheb v CIT (1975) 99 ITR 162 (Bom); CWT v Kumari Manna G. Sarabhai (1972) 86 ITR 153 (Guj); Col. H H Sir Harinder Singh v CIT (1972) 83 ITR 416 (SC); Manilal Dhanji v CIT Bombay City I (1959) 35 ITR 467, approved by the SC in (1962) 44 ITR 876; CIT Kerala v Hajee Hassan Yacoob Sait (Deceased) and others (1964) 53 ITR 5 (Ker).

27. The minor child will not obviously be entitled to enjoy a benefit as a minor, if the enjoyment is required to be deferred beyond the period of his minority; and it is only a benefit, enjoyment of which is postponed to some later date within the period of his minority, that will be caught by 64(1) (v) and (vii). A "deferred benefit" implies that a benefit has accrued or is available immediately but its enjoyment has been postponed. The emphasis is on the question whether a minor beneficiary or spouse has actually derived any benefit under the trust, or circumstances exist which can enable the minor to compel the trustees to apply any part of the trust funds in his favour immediately, consistently with the provisions of the trust deed, vide Chhaganlal Baid v CIT (1971) 79 ITR 258 (Cal); Maharani Vijayakunverba Saheb v CIT Bombay City I (1975) 99 ITR 162, 173 (Bom); CIT v B.A. Dalal (1974) 96 ITR 408 (Pat). Though these decisions relate to the provisions of the Act before the amendment covering deferred benefits, the points involved are still valid.
28. CIT v Arvind Narottam (1969) 73 ITR 490 (Guj). The law in Canada is similar : Harshman Trust v MNR 72 DTC 1191 (TRB).
29. Shardaben Jayantilal Mulji v CWT (1977) 106 ITR 667 (Bom). The interest in income is distinct from the right to possession of the property. See Sachs v The Queen 80 DTC 1369 (TRB), quoted at p. 592, Jack Bernstein, *Income-tax Consequences of Trust Distributions of Income and Capital*, 1981 Conference Report—Report of the Proceedings of the 33rd Tax Conference, Canadian Tax Foundation.
30. Tanil Ramdas v CWT (1981) 132 ITR 92 (Bom); CWT v Trustees of Mrs. Hansabai Tribhuwandas Trust (1968) 69 ITR 527 (Bom); Prince Ranjit Singh P. Gaekwad v CWT (1969) 73 ITR 206 (Guj). The contrary view was taken in Yeshwant Rao Ghorpade v CIT (1966) 61 ITR 444 (SC), in which the assets of the trust were held for the benefit of a charitable trust for some years, and thereafter absolutely for the settlor's children. This judgment was followed in CWT v Arvind Prasad N. Mafatlal (1975) 98 ITR 287 (Bom) in which the the annual accretions were added to the trust funds and the beneficiary was entitled to payments from the funds after a stipulated period. Both the cases related to the period before the amendment of sec. 4(1)(a)(iii) of the Wealth-tax Act to cover cases of "immediate or deferred" benefit w.e.f. the April 1, 1965. According to the Karnataka High Court, the amendment did not make any difference where, during the relevant period, the beneficiaries were minors and the assets in question were held for charitable purposes and not for their benefit: CWT v HH Yeshwant Rao Ghorpade (1978) 115 ITT 332 (Kar).
31. CWT Bombay v Master Jehangir H.C. Jehangir (1982) 137 ITR 48 (Bom).
32. CWT v Arvind Narottam (1976) 102 ITR 232 (Guj).

33. Manilal Dhanji v CIT Bombay City I (1959) 35 ITR 467, approved in (1962) 44 ITR 876 (SC); S. Raghbir Singh v CIT (1961) 42 ITR 410 (Pun), affirmed in CIT v S. Raghbir Singh (1965) 57 ITR 408 (SC); Badri Vishal Tandon v CED 136 ITR 427 (All); CIT v Mrs. Jayalakshmi Duraiswami (1964) 53 ITR 525 (Mad). Also CIT v Bhagwandas S. Malvi and others (1977) 107 ITR 426 (Bom), where the parents accelerated their children's interests by surrender of their prior life-interest. The interest intended to be given by the grantor—whether it is meant for the beneficiary as an individual or whether it belongs to his branch of the family—will have to be gathered from the language of the document: C.N. Arunachala Mudaliar v A. Muruganatha Mudaliar, AIR 1953 SC 495, 500; CIT v Gordhandas K Vohra (1974) 96 ITR 50 (Bom.).
34. A. Kannan Chetty v CIT (1963) 50 ITR 601 (Mad); Rajender Dutt v Shamchander Mitter (1881) ILR 6 Cal 106; In re. Kahandas Narandas (1881) ILR 5 Bom 154; Soorimoney Dossee v Deenabandhu Mullick 6 MIA 525; Tagore v Tagore 9 Beng, LR 377; Wilcock's Settlement (1875) 1 Ch. D. 229.
35. For the contrary view, CGT v Tej Nath (1972) 86 ITR 96 (Punj); CIT v Gangadhar Sikaria Family Trust (1983) 142 ITR 677 (Gau). A gift of the family property by the *Karta* to a trust of which the beneficiaries are members of his undivided family is only voidable and not void *ab initio*. Such a gift can be attacked only by the members of the family whose interests are affected thereby and not by strangers. Raghubanchamani Prasad Narain Singh v Ambika Prasad Singh AIR 1971 SC 776; CIT v Braham Dutt Bhargava (1962) 46 ITR 387 (Raj). Also see Ratilal Nathalal v CIT (1954) 25 ITR 426 (SC), affirming (1951) 20 ITR 307 (Bom).
36. CED v Estate of the late M.V.K. Papa Rao (1981) 128 ITR 813 (AP); CIT v Gangadhar Sikaria Family Trust; CIT v Kamakhya Rice Mill Trust (1983) 142 ITR 677 (Gau).
37. CIT v Gopaladas T. Agarwal (1979) 116 ITR 613 (Bom).
38. Castiglione's Will Trusts (1958) 1 All ER 480. Also AIR 1957 Cal 293; Kirby v Whitworth (1887) 12 App. Cas. 409.
39. C & AG, 1980-81, pp. 170-171.
40. D. Kanniah Pillai v CIT (1976) 104 ITR 520 (Mad); CIT v Abdul Khader Motor and Lorry Service (1978) 112 ITR 360 (Mad). The contrary view has been expressed in CIT v Kartikey Sarabhai (1981) 131 ITR 42 (Guj).
41. CIT v Abdul Rahim (1965) 55 ITR 651 (SC); CIT v Bhagyalakshmi (1965) 55 ITR 660 (SC). Explanations 1A and 2A to s. 64(1) implicitly accept the scope for a trustee's being a partner of a firm in a representative capacity.
42. CIT v Mohanbhai Pamabhai (1973) 91 ITR 393 (Guj); Velo Industries v Collector (1971) 80 ITR 291 (Guj); Addl. CIT v Naghdas Kilabhai (1975) 101 ITR 197 (Guj); CIT v Bankey Lal Vaidya 79 ITR 594, (SC); Ramanlal Khanna v CIT (1972) 84 ITR 217 (Punj).

43. Explanation to section 7(1) of the Wealth-tax Act, inserted by the Finance Act, 1980. The problem is discussed at length in the Twenty-ninth Report of the Public Accounts Committee (Sixth Lok Sabha) on *Incorrect Valuation of Assets*, presented to the Lok Sabha and the Rajya Sabha on Dec. 19, 1977. In Canada where a trust property is sold to the beneficiary for a price less than the fair market value, the benefit is taken to be equal to the difference: Sec. 105(1) of the Income-tax Act, Canada.
44. Para 138 of the Government's Memorandum explaining the provisions in the Finance (No. 2) Bill, 1980.
45. CGT v Ebrahim Haji Usuf Botawala (1980) 122 ITR 62, 67 (Bom).
46. CGT v Smt Ansuya Sarabhai (1982) 133 ITR 108 (Guj); Palanivelu v Ouseph Mathai (1973) I MLJ 264 (Mad); AIR 1973 Mad 309; CGT v Mrs. Jer Mavis Lubimoff (1978) 114 ITR 90 (Bom); V.S. Mani v CGT (1980) 123 ITR 414 (Mad); IR v Buchanan (1958) 34 ITR 173 (Court of Appeal, UK); (1958) 1 Ch. 289; 37 TC 365.
47. Amounts received by a beneficiary from a discretionary trust cannot be taxed in the hands of the beneficiary under section 166 : CIT v Smt. Kamalini Khatau (1978) 112 ITR 652 (Guj – FB); Kum. Pallavi S. Mayor v CIT (1981) 127 ITR 701 (Guj).
48. Jack Bernstein, *Income-tax Consequences of Trust Distributions of Income and Capital*, p. 588, 1981 Conference Report—Report of the Proceedings of the 33rd Tax Conference, Canadian Tax Foundation.
49. CBDT circular No. 320 dated 11.1.1982 clarifies that unrecognised provident funds and unapproved superannuation and other funds created for the benefit of employees will continue to be charged to tax in the manner prescribed in sec. 164(1) and not at the maximum marginal rate.
50. Ravindra Gunvant Lal v CED (1969) 74 ITR 498 (Guj).
51. Ralli Bros. Trustee Co. Ltd. v IR (1966) 1 All ER 65. Also see Kirkwood, The Public Trustee and another v IR (1964) 53 ITR ED 75 (1964) 2 WLR 680.
52. CED Madras v R. Kanakasabai (1973) 89 ITR 251 (SC).
53. Attorney General v Worrall (1895) 1 AB 99.
54. Duke of Norfolk, Public Trustee v IR (1950) Ch. 467.
55. CWT v Kali D. Cawasji (1981) 131 ITR 158 (Bom); CWT v Mrs. Dorothy Martin (1968) 69 ITR 586 (Cal).
56. Chintamani Ghosh Trust v CWT (1971) 80 ITR 331 (All).
57. CWT Lucknow v P.K. Banerjee (1980) 125 ITR 641 (SC), reversing P.K. Banerjee v CWT (1972) 83 ITR 117 (All) and over-ruling CWT v Nawab Fareed Nawaz Jung (1970) 77 ITR 180 (AP); CWT v HH Maharani Gayatri Devi of Jaipur (1971) 82 ITR 699 (SC); CWT v Arundhati Balkrishna (1970) 77 ITR 505 (SC); Ahmed G.H. Ariff v CWT (1970) 76 ITR 471 (SC); CWT v Kali D. Cawasji (1981) 131 ITR 158 (Bom); CIT v Dorothy Martin (1968) 69 ITR 586 (Cal);

CWT v Anarkali Sarbhai (1971) 81 ITR 375 (Guj). If the terms of an instrument do not expressly vest an annuitant with the right to commute the annuity, the implication may be that commutation is precluded, and wealth tax exemption under sec. 2 (e)(1)(iv) is justified : CWT v Sir Hirji Cowasji Jehangir (1981) 129 ITR 642 (Bom).

58. Shakuntala Banerjee v CED (1980) 125 ITR 488 (All).
59. An annuity payable equally to such of three persons as may be living is a continuing annuity which passes to the remaining annuitants on the death of any them and is accordingly liable to the estate duty : In re. Tapp : Granville and King's College, Cambridge v IR (1959) CB 443 (CA); (1960) 40 ITR Supl. p. 7.
60. Brodie's Will Trustees v IR (1933) 17 TC 432; Lindus & Hortin v IR (1933) 17 TC 442; Peirse-Duncombe Trust v IR (1940) 23 TC 199; Michelham's Trustees v IR (1930) 15 TC 737.
61. Postlethwaite v IR (1963) 41 TC 224; Inchyra v Jennings (1966) 42 TC 388; Lawson v Rolfe (1970) 1 Ch. 612.
62. Morant's Settlement Trustees v IR (1948) 1 All ER 732; (1948) 30 TC 147; Williamson v Ough (1936) 20 TC 194. Different but equally interesting, CWT v Late Nawab Sir Mir Osman Ali Khan Bahadur 1974 Tax LR 367 (AP).
63. CIR v Plummer, (HL) reported in the *Taxation*, 17th May, 1980, pp. 183-4; also (1979) 3 All ER 775.
64. CWT v Dr. E.D. Ankelesaria (1964) 53 ITR 393 (Guj) which discusses, in this connection the relevance of section 174 of the Indian Sucession Act and some of the English decisions indicating when an annuitant can claim payment of the value of the annuity as a gross sum. Also see CWT v Bhalchamora D. Jokhakar (1978) 112 ITR 238 (Bom).
65. Professional income cannot also be diverted to a charitable trust by an overriding title or obligation : CIT v Thakur Das Bhargava (1960) 40 ITR 301 (SC), the case of an advocate stipulating payment of the fees due to him to a charitable trust. There is even less scope for dedicating the services of a professor as trust property. The money receivable by him as salary will become trust property only when it is actually received by a trust : Eggar v CIT 2 ITC 286.
66. Westminster Bank Ltd. v Barford (Inspector of Taxes) (1958) WLR 406; (1959) 37 ITR 477 (in the Chancery Division), case of periodical payments under an agreement on special services: "The consideration for the contract was the services of the testator, and the consideration for the payments was the contract, which by its independent vitality generated income" (1959) 37 ITR at p. 483.
67. Helvering v Eubank 311 US 122 (1940).
68. Managing agency of a company and insurance and commission agencies are businesses which can be held in trust according to the Supreme Court: J.K. Trust v CIT (1957) 32 ITR 535, 543. A partnership conducting insurance agency has been treated as "property" held

in trust in Dharma Vijaya Agency v CIT Bombay City I (1960) 38 ITR 392 (Bom), following the SC decision. In the UK, arrangements made by film stars for avoiding surtax through trusts and companies have been ignored by the courts: Crossland v Hawkins (1961) Ch. 537, 39 TC 493, where an actor agreed to render his services exclusively to a company, the shares of which were held in trust for his children. While he received a modest salary from the company, the company was entitled to large sums from the producers of the films in which he acted. The case of IR v Mills (1975) AC 38 (1974) 49 TC 367, was not very different. Similar tax reduction devices are known to have been tried also by film artistes in India. For a case of transfer of a right to receive collections from a motion picture, see Smt. M.S. Subbulakshmi v CIT (1955) 28 ITR 561 (Mad).

69. CIT v Sri Kikabai Premchand (1948) 16 ITR 207 (Bom).
70. CIT v Jayantilal Amratlal (1965) 55 ITR 214 (Guj), affirmed in (1968) 67 ITR 1 (SC).
71. CIT v Jayantilal Amratlal (1968) 67 ITR 1 (SC); CIT v Shyamlal Bhuwalka (1978) 113 ITR 127 (Cal).
72. CIT v Smt. Nathi Bai Binani, IT Ref. No. 423 of 1970, Calcutta High Court order dated May 12, 1975; CIT v Trustees of Sreeram Surajmull Charity Trust (1971) 79 ITR 649 (Cal).
73. Smt. Leela Nath v CIT (1982) 134 ITR 507, 517 (Cal).
74. CIT v Jayantilal Amratlal (1982) 67 ITR 1 (SC).
75. S. Raghbir Singh v CIT (1961) 42 ITR 410 (Punj) affirmed in CIT v S. Raghbir Singh (1965) 57 ITR 408 (SC) where the settlor obtained a benefit from the trust by way of payment of his debts, but the income utilised to clear his liability was not found includible in his total income.
76. Lady Miller v IR (1930) 15 TC 25 (HL).
77. Trustees of HEH the Nizam's Supplemental Jewellery Trust v CWT 1975 Tax LR 1085 (AP); CWT v Trusteee of HEH the Nizam's Sahebzadi Anwar Begum Trust (1981) 129 ITR 796 (AP).
78. Mulla's *Principles of Hindu Law*, edited by S.T. Desai, Tripathi 1974, p. 108, para 43.
79. Mulla's *Principles of Mahomedan Law*, 18th ed., edited by M. Hidayatullah, Tripathi 1977, p. 34, para 114 and p. 109, para 85.
80. Executors of the will of T.V. Krishna Iyer v CIT (1960) 38 ITR 144 (Ker); CIT v C.S. Rajasundaram Chetty (1950) 18 ITR 145 (Mad); ITO v Nawab Mir Barkat Ali Khan Bahadur (1974) 97 ITR 239 (SC); A. Vairavan Servai v Commr of Agl IT (1980) 124 ITR 557 (Mad). See also Chapter 3, nn. 34, 81 and 82.
81. P.J.P. Thomas v CIT (1962) 44 ITR 937 (Cal) reversed on a different ground in (1963) 49 ITR 97 (SC).
82. Jogendra Nath Naskar v CIT (1069) 74 ITR 33 (SC).
83. Smt. Ganesh Devi Rami Devi Charity Trust v CIT (1969) 71 ITR 696 (Cal).

84. CWT v HH Sri Rama Varma, Maharaja of Travancore, (1975) 100 ITR 91 (Ker).
85. CWT v Smt Rani Kaniz Abid (1974) 93 ITR 332 (All).
86. Ahmed G.H. Ariff v CWT Calcutta (1970) 76 ITR 471 (SC); CWT v Puthia Ponmani Chintakam Waqf (1967) 63 ITR 787 (Ker).
87. EDA No. 20/Pn/1974/1974-75 (Assessment Year 1974-75) ITAT, Poone Bench Order dated March 23, 1977—Case of three private trusts, one of which was a private temple and the other two were meant to organise daily worship and provide for the performance of annual ceremonies, like *sradh* ceremonies of some of the members of the family of the deceased settlor.
88. See Ch. 3, pp. 42-49 and 78-79, nn. 176-187. Courts have taken a different view in the UK : Public Trustee v IR (1958) Ch. 865 (In the Court of Appeal); (1958) Ch. 513 (In the Chancery Division) 37 ITR ED 32-52, where bequest of income for life to a trustee "so long as he shall act as . . . trustee . . . by way of remuneration" was held liable to the estate duty under Section 1 of the UK Finance Act, 1894, notwithstanding the fact that the trustee was receiving the income "only as holder of office" within the meaning of section 2(1) (b) of the Act.

8
Remedies

Treatment of a trust as a taxable entity

THE concept of assessing the trustee in the same manner and to the same extent as the beneficiary, on which the existing provisions of the tax laws are based, assumes that the revenue authorities will be in a position to quantify the income which each beneficiary may get from the trust in a particular year. This assumption may not always be valid. A trust deed may not stipulate disbursement of all the trust income within the year in which the income is derived. It may permit payments over a period of time extending beyond the year in which the income arises. The trustees may be required to conserve the capital gains, if any, and also maintain a reserve to meet anticipated expenses or ensure the evenness of the annual payments made to the beneficiaries. The debit to the revenue account to create the reserve would not be allowable expenditure for tax purposes though it will reduce the distributable surplus of the trust. It will certainly hurt the beneficiaries if tax is collected from them on amounts which they have not actually received or to which they have no legal right, e.g., capital gains added to the trust corpus in terms of the trust deed. The Income-tax Act does not deem the entire trust income to be rateably theirs[1]. The beneficiaries can well plead that they can be called upon to pay tax only on amounts actually made over to them, unless the Revenue has reason to believe that disbursement of income is being avoided by the trustees with their connivance.

All things considered—the haziness of the provisions

covering trusts in the Income-tax Act, the deviations in the Act from the basic tenets of taxation like equity and neutrality and the tax avoidance techniques in vogue[2]—it appears advisable to have tax levied on the trust itself, treating it as a taxable entity. Once a trust is recognised as a taxable unit like a firm or a Hindu undivided family, which is not a legal entity but is still treated as an assessee in terms of the definition of a "person" in section 2 (31) of the Income-tax Act,[3] many of the legal issues that currently vex income tax assessment can be resolved without difficulty. When one talks of a business held in trust, what is denoted is a business carried on by a trustee in the interest of the beneficiaries. The trustee in India has no title to the trust properties, which vest in him only for administration and management.[4] The controversy about the circumstances in which trusts can be treated as bodies of individuals or associations of persons[5] can be avoided by the recognition of trusts which hold properties through trustees for the benefit of others as a new class of assessees. It has already been pointed out that, under the scheme of income taxation, whoever is in actual receipt and control of any income is generally charged with the tax on the income.[6] The Income-tax Act can provide for the filing of returns and the payment of tax by the trustees on behalf of a trust.[7] The trustees should be liable to be taxed for and on behalf of the trust which will be "personified" for this purpose, to use the Mead Committee's apt expression,[8] and not on behalf of the beneficiaries.

Alternatives in income tax assessment—maximum rate with or without tax credit for beneficiaries

There are four alternatives for the treatment of income so reported by the trustees of a trust :

(*a*) A private trust can be at par with a non-industrial close company, suffering the same rate of tax.[9]

(*b*) Unlike companies which, under the "classical" system of corporate taxation that is operative in India, bear tax themselves at the prescribed rate and also withhold tax at the specified rate from the dividends paid to the shareholders, a private trust can be required to pay tax at the maximum marginal rate applicable to individuals; and, unless it is a discretionary trust, the tax paid by it can be attributed to the beneficiaries on a

proportionate basis, with reference to the extent of the benefits enjoyed by them individually. To illustrate, if a trust has been taxed at 60 per cent[10] on an income of Rs. 1 lakh and income to the extent of Rs. 30, 000 out of Rs. 40, 000 with which the trust would be left is equally distributed to its two beneficiaries, each of the beneficiaries may get credit for tax to the extent of Rs. 22,500 if the total tax demand of Rs. 60,000 has actually been paid by the trust. No credit will be due to either of the beneficiaries for the balance of tax paid by the trust, *viz.*, Rs. 15,000. If any refund is due to either of the beneficiaries with reference to the tax assessed in his own case and the tax credit he gets for the payment by the trust, it may be made to him in the course of his own personal tax assessment. The beneficiaries of a discretionary trust should be given no tax credit for any income received by any of them from the trust. Tax imputation may be denied even in a specific trust, if the trust is engaged in any business or professional activity.

(*c*) On the analogy of a registered firm a trust can be subjected to an additional levy for which the beneficiaries will not be entitled to any credit. The additional trust tax will be deductible in the first instance and the balance of the trust income distributable among the beneficiaries thereafter. No tax credit will be available to the beneficiaries in respect of the income payments made to them by a trust, which will be added to their other income, if any, and subjected to income tax in the ordinary course.

(*d*) The trust will be liable to tax at the maximum marginal income tax rate applicable to individuals but no part of the tax will be ascribed to the beneficiaries. The tax will be collected from the trust, unless the trust assets have been distributed among the beneficiaries and there is any practical difficulty in effecting the recovery from the trust itself. On the other hand, the share of the income actually received by the beneficiaries from specific as well as discretionary trusts, *debuttar* estates and *waqfs* will be aggregated with their other income and considered for levying the income tax on the other income at the marginal rates applicable to the total income.

The first course may not be justified, in view of the fact that a private company is controlled and managed by the

beneficiaries or owners themselves and has greater freedom of operation than a trust, besides being entitled to some of the legal privileges not available to a trust. The Revenue will probably find the last course the most convenient from the administrative angle, since it will not be clouded by the uncertainty which the other two courses involve and will also dispense with the need for differentiating between discretionary and specific trusts, so far as their own tax assessments are concerned. Since a trust is frequently resorted to for disaggregating income and wealth, there is a view that no trust should be allowed a tax-exempt threshold, for such an allowance will encourage the splitting of wealth belonging to a single individual or family into innumerable trusts. If trusts proliferate primarily to fragment income and wealth and minimise tax liability, such proliferation may be stemmed by the levy of the income tax at the maximum rate and the wealth tax at a relatively high rate on the entire income and wealth of a trust. Whichever of the four alternatives indicated above is adopted, it will be necessary to provide for the deduction of all allowances under the Act, including capital allowances, in the assessment of the trust itself. All losses incurred by a trust in any business conducted by it should be allowed to be carried forward and set off against the income of the trust alone in the subsequent years, subject to the same conditions as the other taxpayers.

In the second and third alternatives the beneficiaries in specific trusts may seek a "throw-back relief" in respect of the income received by them from time to time. That is to say, the income received by them may have to be made liable to tax at the rate appropriate to them in the manner and during the period in which the income had actually accrued or arisen in the case of the trust. Any manipulation of the rate of tax applicable to the beneficiaries, e.g., by arranging distribution of income in a year in which the rest of the income of the beneficiaries is lean, will necessitate a similar "throw-back" of realisations, and their aggregation with the other income in the years in which the trust itself earned the income, as in the USA. The second and third courses lack, therefore, the element of finality, which is essential for effective administration : the assessment of several beneficiaries may have to be disturbed for more than one year, either at the beneficiaries' request or on the initiative

of the revenue authorities. Such a scheme of assessment will call for maintenance of elaborate details of the income earned by a trust and the distributions made by it in the different years, so that correlation between the two will be facilitated.

Even the adoption of the last course may not do away with the need for the Revenue's keeping a record of allocations or applications of income made by the trustee to the extent necessary to give a finding on the portion of the beneficiaries' income that can be taken to have borne tax at the maximum rate in the hands of the trustee. There may also be situations where the assessment year to which the income will have to be ascribed may have to be ascertained on the basis of the available surplus after tax each year in the trust. Such a situation may arise, for instance, in a case in which the beneficiary has income from sources other than the trust, and there is ground for believing that payments are being deferred by the trust to keep down the level of the beneficiary's total income and consequently, the average tax rate applicable to the other income. The maintenance of records required to check such tax manoeuvres will not, however, disturb or delay the assessments of the trust or even of the beneficiaries : all that may be needed is the computation of the income or the value of the benefits to which each of the beneficiaries of the trust is entitled in the order of assessment in the case of the trust itself, like the apportionment of the partners' shares in a firm's income. While this procedure will take care of payment-postponement tactics in specific trusts, the solution in the case of a discretionary trust is to give the Revenue the option to correlate the payments to the year or years in which surplus income large enough to cover them emerged in the trust, or take the payments as the beneficiary's income in the accounting year in which they were made, whichever may be more beneficial to the Revenue.

As for the wealth tax, it may be levied on the trust at three per cent of the market value of the assets held by it[11], providing for exemption only in the case of a specific trust, if its wealth is less than the maximum not liable to tax and none of its beneficiaries is also likely to have wealth tax liability even if the value of his interests in different trusts are added to wealth directly held by him. Each of the beneficiaries should be required to file a statement of his wealth, together with parti-

culars of every trust in which he is a beneficiary and the value of his interest in each of the trusts as worked out and certified by a Chartered Accountant or a Government approved or empanelled valuer. Where there is more than one beneficiary and the sum of the values of all the beneficiaries' interests in a trust falls below the value of the wealth of the trust as a whole, the Wealth-tax Act provides for the assessment of the difference to tax in the case of the trust itself at 3 per cent or at the rates specified in Part I of Schedule 1, whichever would be more beneficial to the Revenue. In view of the difficulties and delays involved in evaluating individual interests and arriving at the balance to be covered by an assessment in the hands of the trustees, it is advisable to tax the trust, and give proportionate credit to the individual beneficiaries for the tax paid by the trust, if they file the actuarial valuation of their respective interests. Every beneficiary will be assessable to tax on his wealth including his interest in the trust, if it exceeds the maximum not liable to tax. But he may be given appropriate credit for the tax on his interest in the trust, as actually paid by the trust, subject to the condition that such credit does not entitle him to any refund of the tax paid by the trust, with reference to the value of his interest and the marginal rate of tax relevant to his wealth. If a beneficiary is a minor in a specific or accumulation trust, his income and wealth should be added to the income and wealth of either of his parents having the larger wealth, even if no part of the wealth was transferred to the minor by either of the parents. Such a provision will take care of cross transfers and gifts made to minors in consideration of any obligation to the parents. The analogous provision in regard to partnership concerns in which minors are given a beneficial interest should serve as a precedent in this connection. While a small specific trust, none of the beneficiaries of which has wealth that may be liable to the wealth tax, may be exempted from the tax, the Revenue should be free to assess the trust at the appropriate marginal rate, if the net wealth held in trust attracts the wealth tax at more than 3 per cent. So far as discretionary trusts are concerned, the existing provision of section 21(4) of the Wealth-tax Act may continue to govern them without any relief on the lines suggested for specific trusts which do not avoid or help anyone to avoid the tax.

A plain and simple trust which strictly follows the investment pattern prescribed for provident and other tax exempt funds, and which does not dabble in business or professional activities, can be allowed to pay tax at the marginal rate appropriate to its total income or taxed at a rate lower than that applicable to the other trusts. This relaxation should be confined, however, to a trust with a specified class of beneficiaries who deserve a special tax concession, e.g., orphaned minors, lunatics, mentally retarded persons, persons who are physically so handicapped that they are incapable of profitable employment, old people past the age of 70, or those who are suffering from incurable diseases or other serious disabilities. If such a guileless trust has more than one beneficiary of this category it may be given a tax remission equal to the difference between the tax raised against it on the basis of the total income derived by it and the sum of the taxes that may be demanded from the beneficiaries if the entire income had been disbursed to them according to the terms of the trust instrument. If any of the beneficiaries has any other independent income, additional demand can be raised in his own assessment, including the trust income in his total income only for rate purposes.

Residence of a trust

If a trust is to be assessed to tax *qua* trust, specific tests will have to be prescribed in the Income-tax and Wealth-tax Acts for determining its "residential status" as a taxpayer : without a statutory clarification on a trust's residence, there is likely to be avoidable litigation, for tax jurisdiction over income and wealth abroad depends on it. While every taxpayer is charged to tax on his income and wealth in India, it is only a person who is ordinarily resident in the country that is liable to pay tax on outside income and wealth. A company is said to be a resident in India in a year if it is an Indian company or, during the year, the control and management of its affairs is situated wholly in India. Likewise, a Hindu undivided family, a firm, an association of persons or any other person is taken as resident in India in a year unless, during the year, the control and management of its affairs is situated wholly outside India. If a trust is treated as a taxable entity, its residence will have to be determined on the same principles. It can be taken

to be resident in India if its managing trustees, or the majority of the trustees who administer it, are resident in India.[12] Beneficiaries who have merely the right to proceed against the executors and trustees for claiming the income from certain shares in companies in India cannot be said to have any assets in India chargeable to the wealth tax, where the testator, the beneficiaries and all the trustees are non-residents.[13] It should be possible, however, to tax the registered "owners" of the shares in such cases on the income from the shares in the status of a body of individuals or an association of persons, depending on the facts of the case.

A trust set up outside India by any person ordinarily resident in this country should also be held to be resident, if the spouse or the minor child of the author is one of its direct or indirect beneficiaries, irrespective of whether the benefits are immediately enjoyed or put off to a remote contingency. Since there can be no trust without some property, the decisive factors for levying tax will obviously be the situs and the nature of the property. The trust can reasonably be treated as a resident even where the managing trustees or majority of the trustees are resident abroad, if most of the trust properties lie in India and the trustees are required to supervise or manage the estate or conduct any part of the trust affairs in India. While immovable properties are subject to the exclusive jurisdiction of the country in which they are located, tax jurisdiction of the country where the taxpayer resides can be extended to reach his movables outside the country. Tax treaties under section 90 of the Income-tax Act and the provision for unilateral relief for double taxation under section 91 of the Act[14] will temper any liability that may be raised against the trust both in India and the country in which any assets are held, but that will not dispense with the need in India for a suitable provision like the one in section 25(1) of the UK Finance Act of 1965.[15] It is obvious, in this context, that a genuine overseas trust should be distinguished from a trust seeking refuge in a tax haven.

Other counter- measures needed

While many of the methods of tax avoidance outlined in Chapter 7, particularly those directed against the income tax, may be rendered pointless if all private trusts saving those

which are excepted by the special provisions, e.g., trusts for the mentally unbalanced or retarded, are taxed at the maximum marginal rate applicable to an individual or an association of persons, there will still remain a few devices requiring special curative amendments. A few of the important amendments that are called for are indicated below :

(*i*) *Cross trusts*

Since courts have found difficulty in holding that there are "cross trusts" where reciprocity is not immediately apparent, there should be provisions in the direct taxes statutes enabling the Revenue to take an overall view of family settlements. If a series of transactions appear to be connected and the settlors and beneficiaries are related to each other or have close business association, there should be no further need for proof of concerted attempt to avoid tax. The Revenue should have the right to draw the inference that if any member of the family of the donor benefited through any settlements made by any member of the families of the donees within a specified period, say five or six years from the date of the donation, all the settlements in question are parts of a single deal. The consequence of such a rebuttable presumption will be inclusion of the settled income and assets in the transferor's assessments to the income tax and wealth tax, subject to his right to lead evidence to vindicate his stand.

(*ii*) *Treatment of unauthorised benefits*

The existing law is unsatisfactory where the trust resources are scooped out without the necessary powers by the author or the trustees or even a nominee of the beneficiary. While it may be irrational to punish a beneficiary for the trustee's malpractices, there is no justification for not amending the law to make it clear that a trust will be taken to be revocable if its author yields to the temptation to make off with any benefits without the necessary sanction in the trust instrument, or utilises the trust funds in the form of loans to or deposits with concerns in which he is interested,[16] other than public companies in which he does not directly or indirectly control more than 5 per cent of the equities. Alternatively, tax may be levied at 10 per cent more than the maximum rate applicable to an in-

dividual in respect of so much of the income of the trust as is attributable to such misuse of the trust capital. This may be the preferable course if the trust itself is assessed to tax at the maximum rate applicable to an individual. The Revenue is not bothered about the remedies available to the beneficiary : he may not consider them worth his while. What the Revenue is concerned with is the tax on the benefit that the author or trustee has managed to scrape away. A charitable or religious trust is taxed on such income under section 13(1)(c) of the Income-tax Act. In a private trust, it may be equitable to make the trust or the person in whose favour a benefit has been misapplied, pay tax on it at 10 per cent more than the maximum rate. The misapplication tantamounts to tax "avoision",[17] falling in the grey area between tax avoidance and evasion, and merits a deterrent levy, over and above the maximum rate of tax. A penalty as such may not be supported by the courts which insist on *mens rea*[18] being established where evasion is alleged by the Revenue; and this leaves the legislature with no option but to charge additional tax in such a case.

Any payment by a close company by way of advance or loan to a shareholder who has a substantial interest in the company is deemed to be a dividend.[19] There is need for a similar provision for the treatment of the resources of a private trust which the beneficiaries or their nominees are allowed to exploit, directly or deviously, through contracts, covenants, or other financial arrangements. As stressed earlier, even if the trust is made to pay tax on its full income, the income received or receivable by the beneficiaries will still have to be worked out to arrive at the rate of tax chargeable against the rest of their income. The value of the benefit enjoyed by any one on the sly, without sanction in the trust deed, may have to be indicated in the order of assessment in the case of the trust to facilitate appropriate tax procedings against the interloper, without prejudice to its being taken into account, simultaneously, as a part of the income of the trust.

(iii) Trusts in favour of natural children, premarital transfers of assets between a couple and settlements made in favour of persons not legally wedded

The provision in the tax laws for the removal of the undesi-

rable distinctions in the matter of aggregation of income and assets of minor children, etc., may have to be comprehensive in its scope : the income from assets transferred by a taxpayer, either directly or through a trust, to a minor child or any member of the opposite sex, without adequate consideration, may be required to be included in his or her own total income for income tax purposes even if the transfer has been subjected to the gift tax. The value of the transferred property may be aggregated likewise with the transferor's wealth for wealth tax purposes.

The term "children" has been defined to include illegitimate children in section 27(7) of the Estate Duty Act, though, unaccountably, those who live together without a valid contract of marriage or those whose relationship is not approved in law are not covered by the expression "relatives" in that section, while dealing with dispositions in favour of relatives as gifts for estate duty purposes. The object is not to visit the sins of the parents on the children or subject any category of taxpayers to a discriminatory liability, but ensure that the concerned parent who has made a settlement or other arrangement in the nature of trust does not get away with a tax benefit to which he will not be entitled if he strictly abides by his personal law. Gift tax is payable in any case, without reference to the relationship or the legitimacy of the donee, whenever property is transferred to him or her, in trust. What may escape are the income and wealth taxes and the estate duty unless the revenue laws are suitably amended. In effect, the proposed provision may entail income tax and wealth tax liability, in respect of gifted property, for the donor during his life-time without affecting the donees adversely in any manner. It will also obviate the need for any embarrassing and fruitless enquiry about the relationship between the transferor and the transferee, while protecting the Revenue from income-splitting tactics.

Pre- and post-marriage financial arrangements will get uniform tax treatment if income from transferred assets is taxed to the transferor, without reference to the period or motive of the transfer or the relationship between the transferor and transferee, during his life-time.

(iv) Estate duty liability in respect of property held in discretionary trusts

In the absence of a capital transfer tax as in the UK, estate duty may have to be raised on the death of persons qualified to receive any benefits from a discretionary trust with reference to the same proportion of the trust assets that the benefits actually received by the deceased during a prescribed period before his death bore to the total income of the trust during that period. Additionally, as in the case of the wealth tax, the Revenue may also be given the option to levy the estate duty at a fixed rate on the death of any person eligible for apportionment of a benefit in the trust: the rate may be the maximum prescribed in the Act, divided by the number of persons entitled to consideration by the trustees while exercising their discretion.

(v) Release of life-interest less than two years before death

Release of life-interest in favour of persons entitled to the remainder has been held to be a disposition of the nature of a settlement within the meaning of s. 21(1)(a) of the Finance Act, 1936, in the UK[20]. Since it is reasonable to subject all such acceleration to the estate duty, when it is effected by the deceased less than two years before his death, amendment to the Estate Duty Act on the lines of the provisions made in ss. 2(xxiv)(c) and 4(1)(e) of the Gift-tax Act seems to be required.

Need to vest Revenue with general power to ignore financial arrangements designed to avoid tax

Besides amendments to remove the deficiency in law set out above, a provision on the lines of section 64 of the Income-tax Act (41 of 1974) of Mauritius may be useful in tackling some of the cases in which the revenue has grounds for concluding that the apparent is not the real state of affairs. An "arrangement" can be ignored for income tax purposes in Mauritius, having regard to—

(*a*) whether it might reasonably be expected to have been entered into and implemented in that particular way if tax avoidance had not been its purpose or one of its purposes ;

(*b*) whether the rights and obligations arising under it might reasonably be expected to have been created under an arrangement not having tax avoidance as its purpose or one of its purposes;

(*c*) the extent to which the emphasis in it is substantial on income factors;

(*d*) the overall effect on the practical carrying on of an existing business or other income-earning activity to which it relates;

(*e*) the dependence on the taxpayer of the earning or accruing of income under it;

(*f*) the extent of control over the earning and disposition of income under it in practice, exercised by the taxpayer;

(*g*) any advantage or disadvantage accruing to the taxpayer from it;

(*h*) the income tax and other implications of other courses of action open to the taxpayer at the time he entered into it; and

(*i*) any other relevant considerations.

Where an arrangement is voided, the net income of a taxpayer who is a party to it is required to be adjusted as the Commissioner considers appropriate, so as to counteract the tax advantage obtained by the taxpayer, having regard *inter alia*, to the income that, in his opinion, would in all likelihood, have been derived by the taxpayer had the arrangement not been entered into. The Commissioner is competent to make any consequential adjustments that may be necessary in the income of any third party involved in the arrangement. For the purpose of these provisions, the Mauritius Act defines an "arrangement" to mean an agreement, plan or understanding, whether enforceable or unenforceable, and includes any step or transaction by which it is carried into effect. Since most modern trusts are mere business arrangements neatly tied up through instruments drafted with an eye to the settlor's tax liabilities, there can be no reasonable objection to arming the Revenue with the powers to unravel the skeïn.[21]

The only objection to such a provision in India may be that it is of a sweeping character, vesting the executive with excessive powers. But the objection may not be sustainable if the Commissioner's order is made appealable, like other orders passed by him, e.g., under section 263 of the Indian Income-tax Act, which permits him to revise the orders of the Income Tax Officer which are prejudicial to the Revenue. There is certainly a risk of the proceedings getting bogged down in protracted litigation but it will be an improvement on the existing situation in which tax avoidance has been raised to the level of a virtue. The alternative is to clutter the revenue Acts with countless *ad hoc* amendments, catching up every exercise of individual ingenuity, like plucking each weed with forceps in a garden.

Statutory registration of private trusts and provisions for ensuring flow of information

Since the marginal rate of tax applicable to the rest of the income or wealth of a beneficiary cannot be correctly computed without considering his share of the income or wealth of the trust in which he has an interest, it is evident that it is essential to have a true copy of the instrument of trust in the income and wealth tax records of every beneficiary and also to get its implications examined thoroughly in the tax assessment of the trust.

There should be a statutory obligation for the registration of all private trusts including private religious trusts, *debuttar* estates, *waqf*s and other pious or quasi-charitable endowments, with the designated authority in trust circles which should be constituted as a distinct jurisdiction in the direct taxes establishment in every State.[22] The formation of separate jurisdiction for private trusts will not merely be conducive to uniformity in the tax treatment of the trusts but also facilitate the collection and compilation of the necessary intelligence and statistical data about them. Concentration of the trusts in the hands of a few tax officials may make it possible to tackle them effectively. An idea of the scale of tax avoidance and the revenue entailed can be gathered and measures for preventing the leakage of revenue can be taken only if full and dependable information is systematically supplied to the concerned agencies.

The responsibility should be cast on the authors of the

non-testamentary trusts, and the trustees in regard to testamentary trusts, to have the assets valued and the trusts registered with the notified income tax authorities. All trusts holding properties in India with non-residents as beneficiaries, should be required to withhold the income tax and wealth tax at the appropriate rates each year and file statements of the taxes so deducted before the income tax authorities unless the trusts are themselves assessed to the income and wealth taxes.

In Sri Lanka, the Inland Revenue Act requires that every trust shall, on or before the 30th day respectively of July, October and January of a year of assessment and on or before the 30th day of April immediately succeeding the year of assessment, give the beneficiary concerned, a notice stating the amount of income or wealth earned or held by the trust for his benefit. It is desirable to incorporate a similar provision in the Income-tax Act in India, supplemented with the requirement that every trustee should also endorse a copy of his letter to the beneficiaries to the concerned revenue authorities, for more often than not, it is the Revenue which is in the dark about a trust, not the beneficiaries, especially if the trust is created for avoidance of tax. If the Revenue is posted with prompt information about all trusts that are set up, *inter vivos* or through wills, there can be no difficulty in keeping track of them and taking appropriate action in the cases of the beneficiaries as well as the trust.

Sections 443 and 453 of CTA 1970 in the UK vest the Inspectors with powers to require any party to a settlement to furnish them with the particulars necessary for the purposes of the tax legislation on settlements. Domestic and foreign settlements, banks and even solicitors are compelled to comply with the requisition.[23] Such a provision will be very useful in India, where some of the banks decline to furnish even statistical data of a general nature,[24] taking cover behind "privilege".

Since trust accounting and accounting for income tax purposes may be at variance, every trust will have to be asked to file income as well as wealth returns, furnishing details of all transactions with beneficiaries, settlor and trustees and persons related to or connected with them. A statement reconciling trust income with income returned for income tax purposes will also be required, besides particulars of all other trusts with

which either the trustees or beneficiaries are concerned either as beneficiaries or as trustees or as authors. The powers, if any, exercised by the beneficiaries of the trust with reference to the terms of the trust, e.g., powers of appointment and disposal of life interest, should also be specified in the form of return. The trust is in a better position to monitor action and comply with the assessment proceedings than the individual beneficiaries.

The filing of a photo-copy or a true copy of the trust deed and annual audited accounts, with a certificate of allocation of the different beneficiaries' respective shares in the trust's income and wealth, should be made compulsory for the trustees. The beneficiaries should also be required to declare in their own individual assessments (a) the exact amounts actually received by them from various trusts and the other benefits enjoyed by them in any trust, (b) the amounts apportioned to them by the trustees/auditors as their entitlement in the trust's income/wealth, but not received by them, and (c) their interests in other trusts, from which they have derived no tangible or intangible benefits.

A deterrent penalty ranging from 10 per cent to 50 per cent of the tax payable by the trust should be levied on the beneficiaries and trustees jointly and severally, if there is no compliance with the above requirements, including registration with the notified authorities. Where an individual trustee or beneficiary is guilty of deliberate default or delay, the penalty may be a fixed amount for every day of default, with the prospect of prosecution and a prison sentence, in the event of conviction, if penalty is of no avail in securing compliance. The responsibility for cooperation with the Revenue should be collective in the case of a trust since the settlor, the trustee and the beneficiary have in most cases, a common purpose, *viz.*, promoting the beneficiary's interests in the trust. They cannot therefore, disclaim their obligation on any technical pretexts.

NOTES

1. See Chapter 3. As long as a trust exists the beneficiaries' right to the assets held in trust and the income derived from them depends on the terms of the trust instrument. The trustees are in possession of the assets and in control of the income and are accountable accor-

dingly for the income and wealth taxes. To the extent that the beneficiaries are given a vested interest in the assets and a right to a part of the income or the whole income, the trustees' tax liability is required to be determined with reference to the aggregate liability of the beneficiaries. The trustees bear the income tax on the balance of the income, if any, to which the beneficiaries may not be entitled in the accounting or income year and the wealth tax on the difference between the market value of the wealth, in trust and the aggregate value of the beneficiaries' interests in the wealth at the close of the year. It is possible that the beneficiaries of a particular trust may have a specific share in all the income that accrues to or arises in a trust but this is not a requirement of either the Indian Trusts Act or the Income-tax and Wealth-tax Acts. In this connection, see Arundhati Balkrishna v CIT (1976) 102 ITR 356 (Guj); Reid's Trustees v IR 14 TC 512, 523; Aikin v Macdonald's Trustees 3 TC 306; IR v Dewar 16 TC 84, 94 (HL); Hotz Trust v CIT (1930) 5 ITC 8, 16; IR v Blackwell Minors' Trustees (1924) 10 TC 235.

2. See Chapter 5 on the incompleteness and vagueness of the statutory provisions regarding the tax treatment of trusts, Chapter 6 on the pronounced bias in favour of trusts as against other media for carrying on a business or holding investments and Chapter 7 on some of the methods of tax avoidance that have come to notice in the recent years.
3. A Hindu deity is an "artificial juridical person", caught by s. 2(3)(vii) of the Income-tax Act. Endowments to Him are accordingly within the ambit of the Act. There is no lack of tax-planning for these endowments, e.g., Pravinchandra C. Parekh, 1981, *Tax-Planning through Artificial Juridical Persons (Private Family Gods, Idols, Deities)*.
4. Thiagesar Dharma Vanikam v CIT (1963) 50 ITR 798, 807 (Mad).
5. Deccan Wine and General Stores v CIT (1977) 106 ITR 111 (AP); CIT v Harivadan Tribhuvan Das (1977) 106 ITR 494 (Guj); CIT v Indira Balakrishna (1960) 39 ITR 546 (SC); N.V. Shanmugam and Co. v CIT (1971) 81 ITR 310 (SC).
6. See n. 16, Chapter 3.
7. The American approach is similar, *vide* s. 641(b) of the Internal Revenue Code. Also see s. 104(2) of the Income-tax Act in Canada. The trustees of a trust in India are treated like an association of persons or a body of individuals, depending on the facts of the case, where they have to be assessed on the income or wealth of the trusts not immediately belonging or attributable to any particular beneficiary. See also Chapter 3.
8. Report of Committee chaired by J.E. Meade (1978), *The Structure and Reform of Direct Taxation*, The Institute of Fiscal Studies, London, George Allen and Unwin, p. 461.
9. A non-industrial domestic company in which the public are not

substantially interested has to pay income tax at 65 per cent of its total income and surcharge at 5 percent thereon for its assessment for 1984-85. The maximum rate applicable to income exceeding Rs. 1,00,000 in the case of an individual is income tax at 60 per cent plus surcharge at 12.5 per cent thereon.

10. The rate of tax has been taken at 60 per cent only for purposes of illustration. The rates actually applicable to a close company are higher—60 per cent tax plus 5 per cent surcharge thereon if it is industrial and 65 per cent tax plus 5 per cent surcharge thereon if it is non-industrial.

11. The Meade Committee has suggested that where income is distributed, the trust capital can be attributed to the beneficiaries in the same proportion as the share of income which each has received and the wealth tax payable (if any) can be calculated by treating the attributed amount as the top-slice of the beneficiary's wealth. According to the Committee, the tax should be payable by the trust and not the beneficiary; and this arrangement could apply both where the beneficiary has an interest in possession in the trust and where the income he receives is paid at the discretion of the trustees. [Report of Committee chaired by J.E. Meade (1978), *The Structure and Reform of Direct Taxation*, The Institute of Fiscal Studies, London, George Allen and Unwin, p. 409].

    This approach may not be satisfactory where the object of creating a trust is to split income and wealth in order to reduce tax liability. In a discretionary trust, for example, distribution of income can be so made as to benefit only those who have little or no wealth, apart from their interest in the trust, while those who have large wealth may be content if they are let alone without any payment, for the time being.

    The Meade Committee has pointed out that where some income or part of the income is accumulated, some relatively arbitrary charge on the slice of the trust capital corresponding to the fraction of income accumulated may be attributed to the settlor but the tax that is raised, realised from the trust. Provisions to give effect to these suggestions are not likely to simplify the existing law in India.

12. The residence of the majority of the trustees of a trust not engaged in a business will be the residence of a trust in Canada : Theobodean Family Trust v The Queen (1978) CTC 539 (FCTD), quoted at p. 568, James G. Carphin, *Constituting an inter vivos Trust*, 1981 Conference Report—Report of the Proceedings of the 33rd Tax Conference, Canadian Tax Foundation.

13. A & F Harvey Ltd., v CWT (1977) 107 ITR 326 (Mad).

14. S. 90 enables the Government of India to enter into agreement with the Government of any country outside India for the granting of relief in respect of income on which income tax has been paid in India as also in that country, and for avoidance of double taxation in both the

countries. A treaty between two countries prevails over the laws of both the countries so far as its terms are concerned. India has comprehensive agreements for double tax avoidance with Austria, Belgium, Denmark, Federal Republic of Germany, Finland, France, Greece, Japan, Malaysia, Norway, Singapore, Sri Lanka, Sweden, Tanzania, the United Arab Republic and the UK. India's agreement with Pakistan is no longer operative. There are agreements limited in scope to shipping or aircraft profits with several other countries, including the USA. None of the treaties specifically mentions tax treatment of trusts. However, the amount of tax attributable to the tax law of a particular country is that which is ultimately imposed on the taxpayer : O. A. P. Andiappan v CIT (1971) 82 ITR 876 (SC). If, therefore, a trust is taxed on the same income, say, in the UK as well as India, it will be able to claim appropriate relief in terms of the treaty between the two countries.

S. 91 grants unilateral relief to a resident assessee who has paid tax on his income in another country with which India has no tax treaty, subject to the condition that the income is not deemed to accrue in India under any provision of the Act. The relief is in the form of a deduction, from the tax payable in India, of a sum calculated on the doubly taxed income at the Indian rate of tax or the rate of tax in the foreign country, whichever is lower, or at the Indian rate of tax, if both the rates are equal.

15. Section 25(1) of the UK Finance Act of 1965 is reproduced below :

"(1) In relation to settled property, the trustees of the settlement shall for the purposes of this part of the Act be treated as being a single and continuing body of persons (distinct from the persons who may from time to time be trustees), and that body shall be treated as being resident and ordinarily resident in the United Kingdom unless the general adminsitration of the trusts is ordinarily carried on outside the United Kingdom and the trustees or a majority of them for the time being are not resident or ordinarily resident in the United Kingdom :

"Provided that a person carrying on business which consists of or includes the management of trusts, and acting as trustee of a trust in the course of that business, shall be treated in relation to that as not resident in the United Kingdom if the whole of the settled property consists of or derives from property provided by a person not at the time (or, in the case of a trust arising under a testamentary disposition or on an intestacy or partial intestacy, at his death) domiciled, resident or ordinarily resident in the United Kingdom."

The Tax Reform Act of 1976 has made the creation of a foreign trust unattractive in the USA. The income of a foreign trust with one or more US beneficiaries is taxed to its US grantor for his life (I RC 679). The US beneficiary has to pay tax at a higher rate on the

accumulated capital gains, if any, distributed to him, as though it has been converted into ordinary income, if it does not suffer tax in the hands of the grantor (IRC 643 and 667). The taxes due from a foreign accumulation trust under throw-back rules bear a non-deductible interest at 6 per cent per year, where the income of the trust has not been treated as the grantor's (IRC 667 and 668).

In Canada, a non-resident trust is subject to FAPI rules under which a Canadian taxpayer has to include his share in all "foreign accrual property income" (FAPI) of any "controlled foreign affiliate" in his income for tax purposes. A foreign trust is deemed to be a controlled foreign affiliate if a Canadian resident has a beneficial interest in it to the extent of at least 10 per cent. A non-resident trust which has a Canadian beneficiary or which has acquired property either from the beneficiary or any person related to him who had been resident in Canada for more than 5 years is treated as a resident of Canada if the distribution of its income or capital is subject to the discretion of the trustees.

The Foreign Tax Law in Germany (Aubensteuergesetz-AStG) has a special rule which attributes the income and assets of a non-resident family foundation established by a resident of the Federal Republic to the resident, vide, *Recourse to Tax Havens: Use and Abuse*, (1980). IFA, Proceedings of a Seminar held in Paris in 1980 during the 34th Congress of the International Fiscal Association, Kluwer.

16. In the UK, s. 451 of the Income and Corporation Taxes Act 1970 provides that where either the trustee of a settlement or a body corporate connected with the settlement pays any capital sum, makes a loan or repays a loan to the settlor or spouse, such amount should be treated as the income of the settlor to the extent that it falls within the amount of income available in the settlement upto the end of that or subsequent tax-years. See also IR v De Vigier (H/L 1964) 42 TC 25; McCrone v IR (1967) 44 TC 142; in re. Pott's Executors 32 TC 211; Bates v IR (H/L 1966) 44 TC 225.

17. The word, which has been in circulation for the last few years, reflects the gradual blurring of the distinction between "legal avoidance" and evasion.

18. Anantharam Veerasingaiah & Co. v CIT (1980) 123 ITR 457 (SC); CIT v Anwar Ali (1970) 76 ITR 696 (SC).

19. S. 2(22)(e) of the Income-tax Act.

20. IR v Buchanan (1958) 34 ITR 173 (CA); (1958) 37 TC 365; CWT v Smt Ansuya Sarabhai (1982) 133 ITR 108 (Guj); Palanivelu v Ouseph (1973) 1 MLJ 264 (Mad); CGT v Mrs Jar Merivis Lubimoff (1978) 114 ITR 90 (Bom).

21. IR v Leiner (1964) 41 TC 589; IR v Wachtel (1971) 46 TC 543; IR v Mills (1974) 49 TC 367; Crossland v Hawkins (1961) 39 TC 493; IR v Plummer (1979) 3 All ER 775; Arundhati Balkrishna v CIT (1976) 102 ITR 356 (Guj).

22. In the UK, the corporate trustees and banks file returns of income for the trusts that they administer. Non-professional trustees file returns in the area where they reside.

23. In the UK, every trustee is obliged to return full details of the trust income, including (a) gross income received during the year, (b) annual charges paid, (c) expenses incurred in administering the trust and (d) the distribution of income among the beneficiaries.

24. See n. 11, Chapter 9.

9

Extent of Use of Private Trusts

SINCE private trusts have not so far been required to be registered with any statutory authority in India and the Income Tax Department does not also have separate circles or jurisdictions for them or officers exclusively dealing with them, it is not possible to find out the number of private trusts in the country or even make a reasonable estimate of the number based on a proper sample. However, the Comptroller and Auditor General reports that according to provisional figures furnished by the Ministry of Finance, there were 13,288 private trust assessees in the books of the revenue authorities during 1981-82 (Table 9.1).

The Inland Revenue estimated the total number of trusts in the UK at 4,00,000 in 1975, composed of 3,10,000 trusts with interests in possession and 90,000 discretionary trusts (Table 9.2). The total value of assets, *viz.*, £ 16.8 billion, constitutes about 6 per cent of total personal wealth; and most of it is handled by trust companies and banks[2].

Though no data are available to arrive at the precise extent to which trusts have been employed to checkmate the Revenue or the exact value of the services rendered by them to the individuals or families resorting to them and the community at large, there are several indications of the part played by them and the broad dimensions of their assets and income:

(i) It would appear that trusts are popular among the tax-

TABLE 9.1

Numbers of trust assessees in the books of the Income Tax Department

	As on March 31, 1981	As on March 31, 1982
Public Charitable trusts	29,737	30,467
Discretionary trusts	2,486	2,786
Specific trusts (where beneficiaries' shares are determinate and known)	8,464	10,502
TOTAL	40,687	43,755

Source: Comptroller and Auditor General of India 1981-82, Union Government (Civil) Revenue Receipts, Vol. II—Direct Taxes, p. 7.

payers in the higher income brackets, though assessees with small income also make use of trusts. This is obvious from the Comptroller and Auditor General's annual reports to the Parliament and the published rulings of the courts (Appendices I and II). The cases which were taken to the Courts or have been subjected to scrutiny by the Comptroller and Auditor General involve large investments, the beneficiaries of the trusts being close relatives of the settlors. A reading of the court judgments and audit reports leaves one with the impression that the dominant motive in the creation of trusts is provision for the settlor's family at the least cost in terms of taxes.

(ii) The Public Accounts Committee of the Parliament has brought out the fact that the wealth disclosed by some of the persons controlling the large industrial houses in 1977-78 was much less than what they had shown in 1957-58. The value of the wealth admitted in 1957-58 should have appreciated substantially, even if there was no physical addition to it. The anomaly becomes glaring in the context of the pronounced overall growth in the assets of a group as a whole. This feature, illustrated by the Public Accounts Committee with

TABLE 9.2

PRIVATE TRUSTS IN THE UK

(a) Trusts with interests in possession

Sizes of trusts £ 000	Numbers	Wealth £ m
0—10	1,40,000	500
10—20	47,000	600
20—40	47,000	1200
40–80	43,000	2300
80—100	11,000	1000
Over 100	22,000	2700
	3,10,000	8300
(b) Discretionary Trusts		
0—50	73,500	1300
50—500	14,000	2500
Over 500	2,500	4700
	90,000	8500

Source: Inland Revenue (Appeal) (1980), *Capital Transfer Tax and Settled Property—A Consultative Document*, reproduced from Thomas, G. W. (1981), *Taxation and Trust*, p. 21, London, Sweet & Maxwell.

reference to a few of the large industrial houses, will be evident from Tables 9.3 and 9.4.

In the view of the Public Accounts Committee, the creation of private trusts and transfer of assets to them is one of the reasons for this "disquieting feature". The Public Accounts Committee refers, in this connection, to a study recently conducted by the special cell of the Directorate of Inspection (Investigation) in the Income Tax Department, which revealed how the device of private trusts has enabled the Sarabhai group

TABLE 9.3

Growth of assets of some large industrial houses

Names of the Industrial Houses	Value of assets 1972 (Rs. crore)	Assets 1977 (Rs. crore)	Percentage increase over 1972
Tata	641.93	1009.28	66.6
Birla	589.42	1070.20	81.6
Mafatlal	183.74	285.63	55.4
J. K. Singhania	121.45	167.31	120.1
Modi	58.05	125.26	115.78
Sarabhai	88.44	136.92	62.3
Goenka	18.01	52.26	190.17

Note : The above data do not take into account the market value of the assets. They reflect the book-figures.

Source : Government of India, Public Accounts Committee (1981-82), *101st Report on Wealth Tax*, Seventh Lok Sabha, p. 7, para 1.26.

to avoid the wealth tax on a large scale. The family had about 400 private trusts before March 1972. About 1200 trusts were created thereafter in order to frustrate the aggregation provisions of the Income-tax Act. The ultimate beneficiaries in all the trusts were 25 individuals of the group; and each member of the family was made a beneficiary of a number of trusts and also a trustee in other trusts in which he was not a beneficiary. The Public Accounts Committee has pointed out that the book-value of the assets of the group increased from Rs. 88.44 crore in 1972 to Rs. 136.92 crore in 1977, that the market value of the assets was estimated at about Rs. 520 crore as against this book value and that the arrangements made by the group through trusts have enabled it to reduce its wealth-tax liabilities. The Committee is doubtful about the efficacy of the wealth tax in preventing the concentration of wealth in the context of tax avoidance efforts on such an extensive scale.

(iii) Control of companies running large industries is generally exercised through equities held in trusts. As

TABLE 9.4

Wealth shown by some of the members of some of the large industrial houses

(Rs. lakh)

Name of the person	Value of wealth disclosed in Assessment year 1957-58	Projected value of the wealth in 1977-78 at yield of 10 per cent	Wealth disclosed in Assessment year 1977-78
M.P. Birla	45.28	304.02	11.65(R)
B.M. Birla	58.67	394.70	16.85(R)
Smt. Rukmanidevi Birla	75.43	507.40	19.49(R)
J.R.D. Tata	12.21	82.14	12.58
N.H. Tata	1.98	13.32	16.00(R)
Y.N. Mafatlal	37.57	252.75	12.94 (76-77)
R.N. Mafatlal	35.53	239.03	17.81
Anand Sarabhai	15.12	101.72	2.65
Gautam Sarabhai	22.07	148.48	0.59
V.H. Dalmia	9.19	61.83	7.79
G.H. Singhania	7.36	40.51	25.10
K.N. Modi	2.00	13.45	0.67
R.P. Goenka	7.76	52.21	1.20

Source : Government of India, Public Accounts Committee (1981-82), *101st Report on Wealth Tax*, Seventh Lok Sabha, p. 8, para 1.27.

mentioned at page 8 in Chapter 1, all trusts, private and public, which have been created by an instrument in writing and which have invested more than Rs. 5 lakh in any company or which have investment in any company ranging between Rs. 1 lakh and Rs. 5 lakh, but constituting 25 per cent or more of its paid-up capital, come within the scope of Sections 153-B and 187-B of the Indian Companies Act, and a Public Trustee has been

appointed by the Government to exercise voting rights in respect of the trusts' shares, when necessary, in terms of these provisions. The Public Trustee was vested with the powers of intervention in respect of 34 private and 89 public trusts, i.e., 123 trusts in all, in 1981. The total investment of the private trusts amounted to about Rs. 3.45 crore in public limited companies and Rs. 1.04 crore in private limited companies as on December 31, 1981. The total of 123 trusts included 9 trusts of the Birla group, 6 of the Tata group and 2 of the Thapar group, all of them presumably public trusts. The Public Trustee has no information about trusts having less than 25 per cent control or Rs. 5 lakh investment in any one company.

(iv) The Research and Statistics Wing of the Department of Company Affairs which undertook a study of trusts associated with certain business groups in 1967-68, had to content itself with an examination of the data supplied for only 75 trusts, including 9 private trusts, 3 employee welfare trusts and 63 charitable trusts. The information available in respect of the private trusts is shown at Table 9.5. It would appear that over 200 trusts were requested to supply details of their working but most of them failed to respond to the request.[3] Even the meagre data given in Table 9.5 should serve to indicate the scale of trust investments.

(v) That the aggressive use of private trusts for reduction, deferment or avoidance of tax liability is not confined to the large industrial houses alone is evident from the various cases mentioned by the Comptroller and Auditor General in his annual reports to the Parliament, and also from the cases which have gone to the High Courts for rulings on questions of law, many of which involved a multiplicity of "settlements" in the same families. The following cases set out by the Comptroller and Auditor General in his Report on Revenue Receipts (Direct Taxes) for 1978-79 exemplify the size and nature of the problem :

(a) Ten members of an industrial group in Tamil Nadu

TABLE 9.5

Data of a few private trusts collected by the Research & Statistics Wing of the Department of Company Affairs

(Rupees in thousands)

Sl. No.	Name of Trust	Group with which associated, if known	Date of creation	Brief objects	Total assets at date available (with date)	Investments in joint stock companies on that date (excluding deposits with banks)
(1)	(2)	(3)	(4)	(5)	(6)	(7)
1.	Apostolos Raptakos Trust—I-207	No group	20.6.46	Benefit of the settlor, his relatives and others mentioned in the settlement	24,21 (31.3.68)	24,21
2.	Estate Lord Cable	Bird Heilgers	26.7.27	Benefits of two private individuals (non-residents) who receive annuities to the extent of the maximum income of the trust	1,90,91 (31.3.67)	1,51,38
3.	Gargi Trust	Mafatlal	19.10.53	For the benefit of a sister of the settlor and her issue and in certain events for the benefit of other sisters and their issues	10,76 (1967)	10,04

4.	Gokaldas Binani Trust	Binani	14.1.57	Benefit of the settlor's grand-son	10,16 (31.3.68)	8,03
5.	Hemant Kumar Bhagabhai Trust	Mafatlal	6.4.44	For the benefit of the son of the settlor, his issues and in certain events for the benefit of brothers, if any, and heir of the beneficiary	44,70 (1967)	19,00
6.	Hemnalini Trust	Mafatlal	19.10.53	For the benefit of the daughter of the settlor and her issues and in certain events for the benefit of other sisters	10,33 (1967)	10,04
7.	Indian Iron & Steel Trust	Martin Burn	18.12.57	To facilitate performance of the settlor's obligation in respect of an advance taken from National Bank of India for purchasing shares of Indian Iron & Steel Co. Ltd.	34,25 (31.12.67)	...
8.	Kamalnayan Bajaj Trust	Bajaj	26.12.56	Benefit of the children of the creator of the trust	4,75 (31.3.57)	4,71
9.	Rohini Trust	Mafatlal	19.10.53	For the benefit of a sister of the settlor and her issues and in certain events for the benefit of other sisters and their issues	10,43 (1967)	10,04

set up 77 family trusts upto the assessment year 1976-77. The trusts which were for a period of 18 years from the date on which they came into existence, could be foreclosed at the discretion of the trustees or if the income-beneficiaries in any of them were reduced to one. The audit estimate of the tax advantage sought through these trusts was Rs. 41.90 lakh in 1976-77 as against gift tax payment of only Rs. 23.23 lakh;

(b) A family in Gujarat created 136 private trusts after March 31, 1978, mostly through gifts of shares in companies under its control besides cash. The initial corpus of all the trusts together was about Rs. 82.51 lakh and the aggregate rose to Rs. 430.75 lakh as on March 31, 1976. There were 76 beneficiaries from the family and 95 outsiders in 87 of the trusts, the outsiders being only income-beneficiaries. Twenty-seven of the beneficiaries appeared in 3 to 9 trusts, and a few in 14 trusts;

(c) A group in Bombay constituted 128 trusts upto February 1977 through settlement of the unquoted shares of some of the controlled companies, besides cash, etc., amounting to over Rs. 2 crore for 51 beneficiaries. The present value of the properties held in the trusts has been estimated at about Rs. 6 crore. One of the beneficiaries figured in 20 of the trusts;

(d) A group in Tamil Nadu set up 15 trusts before February 1977 for the discharge of the debts owned by its members to a company controlled by them. The settlors were themselves the beneficiaries;

(e) A family engaged in the production, distribution and exhibition of cinematograph films and having a chain of cinema houses in Bombay set up 6 private discretionary trusts for its members, empowering the trustees to utilise the trust funds in any business, including production, distribution and exhibition of cinematograph films;

(f) Eight discretionary trusts held shares of substantial

value in three family companies of an industrial group. These shares were transferred by the trust to members of the group at a price much lower than the market value. According to the Comptroller and Auditor General, tax had been avoided by the trusts on "deemed gift" to the extent of nearly Rs. 23 lakh. When an attempt was made by the revenue authorities to charge tax on the capital gains, the Appellate Tribunal deleted the gains from the assessments on the ground that no "transfers" had occurred within the meaning of the term in the Income-tax Act; and

(g) In 15 cases subjected to audit check, it was found that properties valued at Rs. 86.64 lakh had been settled in trust by Hindu undivided families in favour of male and female relatives.

It is worth noting that the above cases have come up for consideration on a random scrutiny and that no audit of all private trusts liable to the income tax has so far been undertaken.

Apart from income-splitting, trusts have come in handy for reduction of wealth tax,[4] gift tax[5] and estate duty liability in many of the bigger cases. The Comptroller and Auditor General has pointed out that a minor child in one of the industrial groups in Tamil Nadu is alleged to have made gifts of 15,000 unquoted equity shares of a company controlled by its family, valued at Rs. 16,59,430 to 10 private trusts of the family between 1970 and 1974. The Comptroller and Auditor General also refers to a hotel business covered by a testamentary trust in favour of the testator's sons, which was subject to two annuities of Rs. 84,000 per annum to each of the two wives of the testator and a charitable trust. There has been a difference of opinion between the audit and revenue authorities on the question whether the annuities constitute a mere application of the trust's income or were a diversion of the income by an over-riding title before it reached the trust. A list furnishing broad details of the cases subjected to audit scrutiny during the last few years is given in Appendix I.

(vi) An analysis of the wealth tax assessees in India based

on the size of the wealth during the years 1970-71 to 1981-82 is given in Table 9.6. The Table shows unaccountable fluctuations in the numbers of assessees with wealth exceeding Rs. 10 lakh in certain years (e.g., 1972-73 and 1976-77). The figures do not also reflect the rises in the prices of precious metals, jewellery and real estates during the period covered by them. One explanation for the relatively low numbers of wealth tax assessees and also for the fall in the numbers of assessees with wealth exceeding Rs. 10 lakh in some of the years may be the resort to trusts by the concerned taxpayers for splitting their wealth and income.[6] This inference is also supported by the fact that gift tax and estate duty cases continue at about the same low level from 1975-76 to 1981-82 (Table 9.7).

TABLE 9.6

Analysis of wealth tax assessees, with reference to the size of their wealth

Year	Above Rs. 20 lakh	Between Rs. 10 and Rs. 20 lakh	Between Rs. 5 and Rs. 10 lakh	Below Rs. 5 lakh	Grand Total
1970-71	448	1445	6057	1,59,669	1,67,619
1971-72	449	1599	6105	1,90,172	1,98,325
1972-73	361	1340	5841	1,98,440	2,05,982
1973-74	385	1320	6085	2,08,459	2,16,249
1974-75	331	1575	6137	2,11,336	2,19,379
1975-76	296	1499	6359	2,22,370	2,30,524
1976-77	301	1353	6838	2,40,814	2,49,306
1977-78	408	1676	7487	2,73,293	2,82,864
1978-79	784	3776	12147	3,01,743	3,18,450
1979-80	N.A.	N.A.	N.A.	N.A.	3,46,291
1980-81	N.A.	N.A.	N.A.	N.A.	3,90,326

Note : N.A. : Not available.

Source : Government of India, Public Accounts Committee (1981-82), *101st Report on Wealth Tax*, Seventh Lok Sabha, para 2.23.

TABLE 9.7

Number af Assessees

Year	Income tax	Wealth tax	Gift tax	Estate duty
1975-76	37,96,258	2,30,524	1,00,901	40,095
1976-77	37,58,753	2,42,306	96,432	40,695
1977-78	39,55,244	2,82,864	91,160	39,879
1978-79	39,69,965	3,18,450	98,077	36,756
1979-80	41,75,615	3,46,291	87,069	35,179
1980-81	45,94,425	3,90,326	93,400	35,862

Source : Report of the Comptroller and Auditor General of India for the different years, Union Government (Civil), Revenue Receipts, Vol. II—Direct Taxes.

(vii) Since trusts have not so far been treated as taxable entities in the Income-tax Act, the trustees are assessed to tax on the income enjoyed by the beneficiaries in the same manner and to the extent as the beneficiaries, where the beneficiaries are not assessed directly on the income they derive from the trust. The income from them is not, perhaps, separately reported and statistically depicted in the Income Tax Department for this reason. Trust assessments are evidently included in the assessments of "individuals" or "associations of persons". The total numbers of income tax assessees increased from 33,88,259 on 31.3.73 to 45,94,455 on 31.3.81 and 46,60,865 on 31.3.82. The numbers of income tax assessees in selected ranges of income are given in Table 9.8. By reason of the deficiency in the classification of trusts for statistical purposes, even the Income Tax Department has no ready means, at present, of ascertaining how many trusts are included in which range of income and in which category of assessees—"individuals" or "others". There is, however, every reason to expect that trusts have been thriving like "firms" or partnership concerns. A partnership is constituted for conducting a business and not for holding investments. As pointed out in Chapter 6, a trust confers more advantages to the taxpayers than a company or a firm for carrying on a small or medium business, not being liable to the

TABLE 9.8

Classification of assessees as on March 31, 1981, in selected ranges of income

Status of assessees	Income range		
	Income upto Rs. 25,000	Income between Rs. 25,001 and Rs. 1,00,000	Income of Rs. 1,00,001 and above
Individuals	26,71,276	8,02,449	15,652
HUFs	1,73,986	59,002	1,495
Firms	4,01,046	3,16,202	36,470
Cos.	31,210	7,205	3,710
Others*	62,310	9,588	824
TOTAL	33,39,928	11,94,446	60,151

Source : Lok Sabha Unstarred Question No. 1007, dated 26.2.1982.
*Include "associations of persons", "bodies of individuals", cooperative societies and probably also charitable trusts and discretionary trusts. A break-up is not available.

income tax that even registered firms suffer or aggregation of income with the parent's or spouse's that a minor's beneficial interest in a partnership, or the partnership of a husband and wife, entails. It has the added attraction that it can confine itself to investments in shares or securities like an investment company without being required to run a business to justify its existence. The numbers of firms increased from 4,55,558 on 31.3.73 to 7,86,321 including 3,36,398 with income between Rs. 25,001 and Rs.1,00,000 and 38,004 with income exceeding Rs. 1,00,001 on 31.3.82.[7] It is probable that trusts also prospered even if they did not keep pace with the increase in the number of firms during this period, in view of their freedom from the disabilities to which the latter are exposed.

(viii) *Waqf-alal-Aulad,* or *waqf*s which are "partly" for family maintenance and partly for pious or charitable purposes, are not obliged to register themselves with the *waqf* Board, except in Uttar Pradesh and West Bengal. There were 4,990 "partly" charitable and 9,497 purely charitable *waqf*s in Uttar

Pradesh in October 1979. Similarly West Bengal had 886 private *waqfs* and 6,177 public *waqfs* in November 1979. The position in the other States is not known. The total number of public *waqfs* in the country, excluding Bombay, Gujarat and Jammu and Kashmir was 1,50,317 (Table 9.9). Bombay had 1247 public *waqfs* with assets valued at Rs. 20.09 crore in 1976. Even if the *waqf-alal-aulad* constituted only about 14 per cent of the public *waqfs* as in West Bengal and not over 50 per cent as in Uttar Pradesh, the number of *waqf-alal-aulad* in existence in the country as a whole at present can be reasonably estimated at over 20,000. Some of them may be small. Some may be deriv-

TABLE 9.9

Waqfs registered in different States in India

Name of Board	Total no. of *waqfs* registered
Andhra Pradesh Waqf Board	34,189
Assam Waqf Board	96
Bihar Sunni Waqf Board	1,500
Bihar Shia Waqf Board	—
Delhi Waqf Board	3,624 till 1965 (SIP)
Karnataka Waqf Board	7,805 till 1968 (SIP)
Kerala Waqf Board	3,626
Kutch Waqf Board	832
Madhya Pradesh Waqf Board	3,202
Marathawada Waqf Board	19,677 till 1969 (SIP)
Orissa Waqf Board	852 till 1964 (SIP)
Punjab Waqf Board	38,110
Rajasthan Waqf Board	16,959
UP Sunni Waqf Board	9,066
UP Shia Waqf Board	2,010
West Bengal Waqf Board	6,146
Lakshadweep Waqf Board	265 till 1965 (SIP)

*SIP—Survey in progress.

Source : Khalid Rashid (1978), *Waqf Administration in India*, New Delhi, Vikas Publishing House, p. 79.

ing income from sources like agriculture not liable to the central income tax levy. There is, however, no ground for believing that tax avoidance considerations weigh less in the creation of *waqfs* than in the execution of other private settlements.

There is no system of registration of *debuttar* estates and "private temples" or other private religious trusts in any State.

The Income Tax Department has not also so far tried to survey them, though experience has shown that some of the trusts, *waqfs* and Hindu endowments which are ostensibly religious or charitable turn out, on enquiries, to be really not public in character and, therefore, not entitled to tax exemption. In any case, the Income-tax and Wealth-tax Acts require systematic collection of information about sources of income, investment of corpus, application of income, etc., even in the genuinely public trusts, since they are liable to tax in certain circumstances.

(ix) In the UK, banks have been a fruitful source of information regarding trusts. The Association of Corporate Trusts in the UK reported in June 1980 that its members served 1,03,048 trust funds with resources valued at £ 4955 million, besides administering 13,974 estates of the value of £ 495 million.[8] Some of the banks in India too provide trusteeship services to their constituents. Data received from three of them are shown in Table 9.10.

Some of the banks denied that they rendered such trusteeship services, while it is difficult to get the necessary information from some of the others, e.g., the State Bank of India.[10] Some of the foreign banks have stated that they are not functioning as trustees for any trust in India, e.g., National and Grindlay's Bank. The Mercantile Bank of India has declined to supply any statistical information though it was pointed out to the Bank that it would not offend its confidentiality obligations to any of its constituents.[11] If banks can be statutorily compelled to furnish the necessary information, at least a part of the area, about which the public as well as the Government are in the dark, may be lighted up.

It is improbable that the numbers of trusts shown in (i) to (ix) above overlap to any significant extent. They relate to different types of cases, which are mutually exclusive. However, the data that are readily available and that do

TABLE 9.10

Details of trusteeship services provided by three banks

	31.3.79	31.3.80	31.3.81
Trust accounts (furnished by the Bank of India, Canara Bank and Central Bank)	2208	2153	2224*
Trust accounts of wills (-do-)	289	293	294*
Trust accounts under the Married Women's Property Act, 1874 (furnished by the Bank of India and Canara Bank)	4120	4150	4200**

*The trust investments administered by the Bank of India and the Canara Bank amounted to about Rs. 13 crore, altogether. The information is not available for the Central Bank.

**Value not available.

not carry any confidentiality-inhibition, are not adequate to frame a realistic estimate of the number of private trusts, *waqf-alal-aulad* and Hindu endowments in the country and the funds or property settled in them. Though one is, therefore, hesitant to hazard an estimate, it is clear that the number of such entities is not very small and that the wealth they hold is not inconsiderable. While genuine trusts set up to protect the interests of helpless infants or the mentally unsound or handicapped persons may not necessarily have a large investment, trusts designed primarily to reduce tax liability may be expected to have assets of value exceeding the threshold for wealth tax exemption. One may perhaps venture to presume that there may be over 50,000 trusts in the country not falling in the category of religious or charitable trusts or employees' welfare trusts, with assets ranging in value from Rs. 1 lakh to Rs. 5 lakh on an average, largely motivated by tax considerations. On this rough guess, the aggregate annual income from investments of the order of Rs. 500 crore may be about Rs. 50 crore, and it may go up to Rs. 250 crore if the total investment is around Rs. 2,500 crore, taking the return at about 10 per cent per annum. It is not possible to estimate the tax avoided on this income, for want of the essential data.

NOTES

1. C.& AG, 1981-82, p. 8. There seems to be some confusion in the matter since the total number of companies as on March 31, 1982, is shown as 46,355. If this number includes 30,467 charitable trusts and 2,786 discretionary trusts, the number of companies assessed to the income tax will be reduced to only 13,082. Since there were 836 Government companies and 57,674 companies in the private sector including 8,465 public companies in 1980-81, the number of companies borne on the tax registers could not be as small as 13,082 in 1981-82.
2. G.W. Thomas (1981), *Taxation and Trusts,* London, Sweet and Maxwell, p. 1.
3. Company News and Notes, Annual No. for 1970, p. 43.
4. The C & AG has reported under-assessment of wealth tax to the extent of Rs. 4,57,384 for the assessment year 1976-77 alone, resulting from the incorrect valuation of shares of private limited companies held by different firms in which 13 private trusts belonging to a "family group" were partners. The interest of the trusts in the partnership concerns was worked out on the basis of the book-value of the shares reflected in the relevant balance-sheet of the concerns and not their market value as the law requires, vide C & AG, 1981-82 p.173. This illustrates the methods adopted by the taxpayers and the revenue at stake.
5. The C & AG mentions two typical cases of avoidance of gift tax in his report for the year 1981-82, pp. 205-6. In the case of a Hindu undivided family there was under-charge of gift tax to the extent of Rs. 82,767, in the transfer of 75 unquoted shares of a private limited campany to two family trusts in the previous year for the assessment for 1974-75. In the other case relating to three private trusts belonging to a particular group, the aggregate gift tax that escaped assessment for 1974-75 and 1976-77 was Rs. 11,26,780. The tax was avoided when the trusts transferred unquoted equities of certain companies as their contribution to the capital of different firms in which they (i.e., trusts) become partners through the trustees.
6. In this connection, see Wheatcroft's observation, quoted at p. 83 ante and also the following extract from the evidence tendered by the US Treasury Department based on a study of estate duty returns showing net estates of $ 500,000 and over in 1945 : ". . . . the larger the amount of wealth transferred the longer is the average duration of trusts. Decedents who transferred property worth between $ 500,000 and $ 1,000,000 put less than 15% of their wealth into trusts for two generations or more whereas decedents who transferred property worth more than $ 3 million put more than 40 per cent of their wealth into trusts for this period. Thus the figures indicate that the wealthiest taxpayers make the most effective use of the tax

advantages of transferring property in trust." *Hearings before the Committee on Ways and Means on Revenue Revision* of 1950, p. 75, Vol. I (House of Representatives, 81st Congress, 2nd Session), quoted at page 358, J. Keith Butters, Lawrence E. Thompson and Lynn L. Bollinger, *Effects of Taxation—Investment by Individuals*, Harvard University, 1953.

7. Source: The reports of the C & AG to the Parliament, Union Government (Civil), Revenue Receipts, Vol. III, Direct Taxes, for the different years.
8. C.W. Thomas (1981), *Taxation and Trusts*, London, Sweet and Maxwell, p. 1.
9. The Bank of India and the Canara Bank also exercised voting power on behalf of the trusts with which they were concerned in 134 companies.
10. There was response only from six banks, though 28 banks were addressed for the necessary information.
11. Mercantile Bank's letter, dated March 9, 1982.

10

Concluding Observations

THE trust was conjured up by equity to supplement the common law in the UK. It was based on the principle of natural justice that the reality of a situation should be recognised in law and that those for whom the hidebound courts provided no remedy could turn to the Lord Chancellor for succour. It is an irony that the trust has evolved as a device to outwit the Chancellor of the Exchequer in the UK. The height of irony is that it has come to be treated in India as a *purdah* which cannot be lifted for getting at the truth : once a settlement is made the Revenue cannot, according to a judicial pronouncement, go behind its motives.[1] The suggestion in Chapter 8 is that since a family trust functions almost like a close company, there should be near-parity in their tax treatment.

The question that requires consideration in this context is whether such a treatment will have an adverse effect on the economy : the issue is not merely the use of a trust as a contrivance for dodging tax but its role in the economy. There are no data to show that private trusts have made any significant contribution to the growth of trade and industry in this country. Well-heeled private trusts with a lot of money may be a measure of a person's wealth but they have a negative effect on saving and risk taking. An outright gift puts a person on his mettle while a trust lulls his initiative and makes him dependent on the estate.[2] Investments held in trust lack mobility; and trustees are generally conservative and non-innovative[3]. Either the settlor does not want the investments in the companies of his group to be changed or the trustees do not consider

it safe. If the aim of a trust is a certain, steady and secure return on the capital provided by the settlor, a trustee will not dare to expose the capital to the hazards of a business. His legal competence to undertake a business is also open to doubt, unless he is given the necessary authority in the trust deed. A trustee in a pubic trust may have accepted the ·trusteeship out of a sense of civic responsibility or hankering for the prestige and privilege that go with it, but the trustee of a private trust can only be a relative or a family friend or an employee or a person appointed by a court or the Official Trustee, the Court-of-wards or the Administrator-General or a bank or a company rendering trusteeship services. To expect any shrewd investment from a trustee is unrealistic because of his accountability in law for any decision he takes[4]. He usually plays safe even if he has the power to convert the assets or venture into business. The beneficiaries are prone to look on him with dislike and suspicion if the trust is genuine and as a fellow-conspirator if it is sham.

If the beneficiaries of a trust are dependent on the settlor's bounty, it is improbable that the income that they derive from the trust will be saved. It may just meet their consumption requirements. If it is a mere apparatus for tax reduction, it is likely that the tax saved will be utilised in further investment; but the State cannot be a party to a taxpayer's consolidating his personal wealth out of its funds or at its expense.

Implications of near-parity with a close company

The Court decisions bearing on private trusts during the last thirty years, which are over 150 in number, and the annual reports of the Comptroller and Auditor General to the Parliament, make it clear that the investments in private trusts and also the income from them are not negligible. The Revenue should not obviously tinker with the law, making periphrastic changes, every time a court delivers an adverse judgment or a new tax fiddle comes to light. However, since every loophole and every adverse judgment would, in effect, be an indictment of the administration and the legislature, it is essential that the law should be rationalized and properly drafted : anticipation of abuses is as essential as reform. Irrespective of whether the tax avoided is inconsequential or considerable, the adminis-

tration should not be allowed to get stalled over issues which might not have been raised at all if the law had been clearer and more comprehensive. It is also essential that the law should be so framed that those who are in a position to hire the best legal advice do not succeed in shifting their share of the tax burden to the less fortunate. The income tax and the wealth tax should not be reduced to taxes on lack of ingenuity or lack of desire to avoid them.

A private trust has a limited social purpose in the present-day conditions. No benefit to the community can be urged as a justification for it, with reference to the pecuniary advantages enjoyed by the relatively few taxpayers in the high income brackets. The neutrality of the direct taxes in family arrangements may ensure that extraneous tax avoidance considerations do not influence the taxpayer's choice of a medium for his investment or business or professional activities; and this neutrality can be achieved through the legislative measures spelt out in Chapter 8, which can be summarised as follows :

(a) Trusts may be declared taxable entities like Hindu undivided families and firms;

(b) all private trusts may be required to be registered with the tax authorities and assessed to the income tax at the maximum marginal rate applicable to individuals, i.e., at rates slightly lower than those charged in respect of close companies, with imputation to the beneficiaries of the tax paid by them in proportion to the benefits actually enjoyed, where the trusts are specific and are not also engaged in business or professional activity; alternatively, if the beneficiaries are not proposed to be given such a tax credit, their proportionate income in a trust may be aggregated with the rest of their income only for determining the tax rate applicable to the other income;

(c) the wealth tax may be charged at 3 per cent or the appropriate marginal rate where it is beneficial to the revenue[5]: a trust may be granted tax exemption only where it is established that none of its beneficiaries will have taxable wealth in the relevant assessment year;

(d) the existing lacunae in all the direct taxes laws may be removed and a provision also made enabling the administration to supersede tax avoidance arrangements, subject to the taxpayer's right of appeal; and

(e) genuine trusts for specified classes of beneficiaries—e.g., the mentally unsound, the physically disabled, those deprived of parental care in infancy, widows without help and those rendered infirm and dependent in old age—may be taxed at the marginal rates appropriate to their beneficiaries' income and wealth, or even lower, concessional rates.

Legislation on the above lines may be the end of the road for phoney trusts[6]. Discouragement of family trusts created primarily for tax avoidance is unlikely to leave an economic, social or moral vacuum.

NOTES

1. K.T. Doctor, v. CIT (1980) 124 ITR 501 (Guj).
2. Though the Musalman Waqf Validating Act, 1930, superseded the Privy Council Judgment in Abu Fata Mohamed Ishak v Russomoy Dhur Chowdhury (1894) 22 IA 76, there is a section of opinion among Muslims in India that its social consequences have been disastrous for Muslims and that indefinite settlements tend not merely to fragment estates but also create a demoralised class of pensioners, vide Daniel Latife, General Secretary of the Muslim Progressive Group, "Law of Family Waqfs : Need for a reconsideration", *Islamic Law of Modern India*, New Delhi, The Indian Law Institute, 1972, pp 228-30. Also S. Khalid Rashid, "Administration of Waqfs in India", *ibid*., pp. 237-38.
3. The Canadian experience is similar; Robin W. Boadway and Harry M. Kitchen (1979), *Canadian Tax Policy*, Canadian Tax Foundation, p. 80 : "While data of the use of trust are not available in Quebec, they are primarily used by the wealthy and as such allow these individuals to exempt large amount of their wealth from taxation. Further criticism centres on the suggestions that substantial sums of property become tied up in trusts with a consequent lack of flexibility in investment activity. In addition, trust investments are generally concentrated in more conservative, less risk ventures."
4. Learoyd v Whitely (1887) 12 App. Cas. 727, 733; Re. Cooper's Settlement (1961)3 All ER 636; Re. Kolb's Will Trusts (1961) 3 All ER

811; Re. Clark's Will Trusts (1961)3 All ER 1133; Shaw v Cates (1909) 1 Ch. 389; Re. Solomon (1912) 1 Ch. 261; Re. Walker v Walker 62 IT 449; Re. Harari's Settlement Trusts (1949) 1 All ER 430.

5. See Harry Rudick (1950), "What Alternative to the Estate and Gift Taxes", *Californian Law Review*, Vol. 38, pp. 169-75. It was suggested by Rudwick that there should be an annual accession tax on trusts, based on the benefits derived by the income beneficiary, and the remaindermen's tax liability determined on the termination of the trusts with reference to the value of the corpus. The tax on the life tenant would compensate the delay in the settlement of the liability on the capital. The aim would be to make assets transferred on trust pay about the same amount of tax as assets transferred outright. The purpose can, perhaps, be achieved also by harmonising the income tax, wealth tax, gift tax and estate duty levies. Such refinement in harmonisation may, however, be an exercise in futility as long as trustsare used as mere tax avoidance devices.

6. The English experience in regard to discretionary and accumulation trusts has been succinctly expressed in Prof. G. S. A. Wheatcroft's observation quoted at p. 83 ante; and the reaction of the Revenue is reflected in the recent amendments to the Capital Transfer Tax provisions in that country. See also C.T. Sandford, 1977, *Taxing Personal Wealth*, London, George Allen and Unwin.

Appendix I

Information available about trusts on which C & AG has reported to Parliament

1970-71

Page 77, Para 73(i)

The life interest of the beneficiaries in *four* trusts was valued at Rs *130.81* lakh. This had escaped assessment for the years 1957-58 to 1965-66.

1971-72

Page 63, Para 41(iii)

There was wealth tax escapement to the extent of Rs *64.14* lakh in the assessments of the beneficiaries of a trust for 1965-66 to 1968-69. Their one-twelfth share in the trust had not been subjected to the wealth tax.

Page 72, Para 49(v)

A registered firm transferred Rs *1,47,900* to a trust for the benefit of the partners' children.

1973-74

Page 136, Para 52(B)(iii)

Wealth tax amounting to Rs *10,534* escaped assessment in the cases of *four* discretionary trusts.

Page 137, Para 52(B) (iv)

There was a short levy of wealth tax in a trust for the assessment years 1967-68 to 1972-73.

Page 140, Para 54(ii)

Three trusts were created for the benefit of three minor

children with 15000 ordinary shares of the total value of Rs *1,50,000*.

Page 143, Para 54(iv)(a)

There was a short demand of wealth tax in a trust with three beneficiaries. Wealth to the extent of Rs *1,70,000* escaped assessment for the years 1965-66 to 1971-72.

Page 144, Para 54(iv)(1)

Rs *1,50,000* invested by a company in a trust escaped the wealth tax assessment for the years 1965-66 to 1973-74.

Page 151

Exemptions in excess of Rs *1,50,000* had been wrongly given in the assessment of a trust for the years 1969-70 to 1972-73.

Page 171

Property of the value of Rs *1,25,280* escaped estate duty assessment, having been transferred to a trust not long before the death of the deceased. This fact was not noticed by the revenue authorities.

1974-75

Page 191, Para 70(i)

A trust created in 1928 held a property which was valued at Rs *1.03 crore* in 1963-64. The value was shown at Rs *8 lakh* on the ground that the trust deed stipulated that the settlor's grandson by the first son could purchase it for the sum of Rs *8 lakh* if he so desired.

1975-76

Pages 138 & 139, Para 60(c)

A Hindu undivided family sold a property to a trust in which its *karta* was trustee for Rs 3,75,000 though its market value was Rs *5,53,665*.

Page 203, Para 92(ii)

Exemption of Rs *1,50,000* in respect of shares and securities

held by a private family trust in which the assessee was a beneficiary was allowed in the beneficiary's assessment.

Page 208, Para 93(iii)

A trust running a cinema theatre was not assessed to the wealth tax on the value of its property.

Page 229

Settlements through several trusts made by one of the tax-payers amounted to Rs 3,37,40,540.

1977-78

Page 122, Para 62(i)

Two cross trusts for the benefit of minor children were created resulting in under-assessment of income tax of Rs *55,474* in the assessment for 1976-77.

Pages 122-123, Para 62(ii)

A lady created *three* trusts in 1957 for the benefit of her three sons. Each of the trusts was liable to the wealth tax.

Page 123, Para 62(iii)

A private discretionary trust was created for the benefit of male members of the family of the settlor after they attained the age of 50. The corpus was Rs *1,07,546* in April 1970.

Page 124, Para 62(iv)

Three private family trusts were created, each with corpus exceeding the maximum amount not liable to the wealth tax.

Page 124, Para 62(v)

A private family trust was created in 1967 with assets on which gift tax amounting to Rs *3,67,750* had escaped assessment.

1978-79

Page 101, Para 51(i)

An individual created *77* trusts through 97 separate deeds executed on a single day, *viz.*, February 8, 1973 with an initial

contribution of small cash. The trusts received Rs *18,75,150* as "donations" in the form of shares of seven private companies in the following three years.

Page 120, Para 59.7(i)

A big industrial group in Tamil Nadu created *77* private family trusts upto the assessment year 1976-77. According to audit, tax advantage secured was Rs *41.90 lakh* upto the assessment year 1976-77.

Page 120, Para 59.7(ii)

A family in Gujarat set up *136* private trusts upto March 31, 1978, mostly by gifts of share in companies of the group and cash in some cases. The aggregate value of the initial corpus was Rs *82.51 lakh*. The book value of the corpus as on March 31, 1976 was Rs *430,75 lakh* as per the balance-sheets of the trusts. In 87 of these trusts created upto February 1977, there were 74 beneficiaries from out of the members of the family and 95 from outside the family. The outsiders were only income beneficiaries, the corpus being settled upon the family members. Twenty-seven beneficiaries appeared in three to nine trusts. A few appeared as beneficiaries in 14 trusts.

Page 121

An industrial group of Bombay set up *128* trusts upto February 1977 for the benefit of 51 members of the family in different permutations and combinations. The settlor of one trust was the beneficiary in another, and so on. Unquoted equity shares in companies of the group, worth Rs 2 crore were originally settled in these trusts. Their present value would be about Rs 6 crore. The maximum number of trusts in which the same person appeared as beneficiary was 20.

Page 121, Para 59.8(i)

There were *32* trusts set up by 23 settlors with corpus of the value of Rs *86.98 lakh*.

Page 122, Para 59.8(ii)

In 15 cases trusts with assets of the aggregate value of Rs *86.64 lakh* were set up by Hindu undivided families.

Page 122, Para 59.8(iii)

An industrial group in Tamil Nadu set up *15* trusts for the discharge of the debts owned by the settlors of the trusts to a company owned by the family. The assets were of the value of Rs *33.67 lakh.*

Page 123, Para 59.8(iv)

A minor child in an industrial group of Tamil Nadu is supposed to have transferred 1,50,000 unquoted shares in a company constituted by the family to *ten* private family trusts. The shares were of the value of Rs *16,59,430.*

Page 123, Para 59.8(v)

A trust was created by an individual with certain equity shares for the benefit of his wife and the children of his grandson, the grandson had no child when the trust was set up.

Page 124, Para 59.8(vi)

A private discretionary trust was constituted by an individual in March 1973 by transfer of Rs 1000 and 960 unquoted equity shares.

Page 124, Para 59.8 (vii)

A big family group engaged in the production, distribution and exhibition of cinematograph films in Bombay created *six* private discretionary trusts for the members of the family. The object was to avoid the aggregation provisions of section 64 of the Income-tax Act.

Page 125, Para 59.9(i)

Capital gains amounting to Rs 2,59,155 from transfer of land and buildings was assessed in the hands of the trustees and income from other properties in the hands of the individual beneficiary in 1972-73.

Page 126, Para 59.9(ii)

The ruler of an erstwhile State set up a trust with corpus of Rs *6 lakh* for the benefit of his wife. The income from the trust was not clubbed with the husband's income under section 64.

Page 126, Para 59.10(i)

A family in Calcutta created *five* private family trusts in April 1954, for the benefit of its personal deities. The value of the immovable property was Rs *39,64,500* in only two of the five trusts.

Page 128, Para 59.11(i)

A private family trust for regular worship of the settlor's deity and for helping the destitutes in the Agarwall community, which has been held to be assessable to tax as a private trust, had net wealth of *Rs 17,61,586* as far back as 1957-58.

Page 129, Para 59.11(ii)

A big industrial group transferred the shares of three family companies to *eight* private trusts at Rs 1800 and Rs 1404 per share while the fair market value of the shares was Rs 7730 and Rs 3650 per share. Deemed gift of Rs 23,10,928 on which gift tax of Rs 4,21,799 escaped assessment has been reported by the Audit.

1980-81

Page 175, Para 4.05(b)

Wealth which escaped assessment in six assessment years—Rs *78,56,586.*

Page 192, Para 4.10(iii)

Net wealth in 1967-68—Rs 19,66,895

Net wealth in 1974-75—Rs 13,39,390

(exclusive of urban immovable property valued at Rs 20,06,000)

Page 200, Para 4.11(e)

Short levy of wealth tax in two assessment years—Rs *1.06.393*

Page 211, Page 4.22(iv)

Property transferred to a private *waqf*—Rs *3,31,000* in April 1972.

Page 228, Para 4.28 (b)(ii)

Rs 3,51,000 (13,000 shares of a private ltd. co.) to one trust, and

Rs 1,89,000 (7000 shares of a private ltd. co.) to a second trust.

Page 229, Para 4.28(b)(v)

Rs 5.12,000 (400 shares of a private ltd. co.)

Page 170, Para 4.04(i)

Accumulation in trust funds—Rs 11,27,358. Wealth tax liability which escaped assessment for 1965-66 to 1974-75, was according to the C&AG, Rs *2,98,783*.

1981-82

Page 153, Para 3.15(ii)

Income from revocable transfer of assets to two private trusts escaped assessment for 1977-78 and 1978-79 in the cases of the two settlors. The short-levy of income tax was Rs 53,040.

Page 173, Para 4.05(i)

There was under-assessment of wealth tax of Rs 4,57,384 for 1976-77, because of the deliberate undervaluation of shares of private limited companies held by a group in thirteen private trusts.

Page 185, Para 4.10(vi)

A big industrial group held assets of the value of Rs 38,54,864 in one trust and assets of the value of Rs 49,50,840 in a second trust. There was short-levy of wealth tax to the extent of Rs 1,02,594 in the cases of some of the beneficiaries who were directly assessed on the value of their interest in the trusts and who declared the value at figures much lower than even those returned by some of the other beneficiaries.

Page 187, Para 4.12(i)

Five private family trusts were set up by an industrial family group "in favour of unborn sons and would-be wife of

members of the family (including minors) as per deed executed in 1973-74 by transfering to each trust as corpus 60,000 equity shares in a reputed company belonging to that family group".

Page 205, Para 4.23(i)(a)

A Hindu undivided family undervalued shares gifted by it to two family trusts by Rs 3,27,525, escaping gift tax of Rs 82,767 for the assessment year 1974-75.

Pages 205-206, Para 4.23(i)(b)

There was undervaluation of shares of private limited companies transferred to four private trusts belonging to a group, resulting in the "aggregate non-levy of gift-tax" to the extent of Rs 11,26,780. Shares were undervalued by Rs 15,94,209 in the case of one trust, Rs 14,72,873 in the second case and Rs 6,03,570 in the third in the assessment for 1974-75. The undervaluation was Rs 9,90,709 in the assessment for 1976-77 in the case of the fourth trust.

Pages 208-209, Para 4.23(iv)

Three private family trusts sold 3855 unquoted equity shares of a company at Rs 250 per share, in the previous year for the assessment for 1976-77, though the value of the shares had been declared by another shareholder of the company at Rs 544 per share as on March 31, 1975. That is to say, shares of the value of Rs 20,97,120 were shown as transferred for a consideration of Rs 9,63,750. According to the C&AG, the market value of the shares was actually higher. On rectification of the amount, additional tax of Rs 2,24,090 was raised by the revenue authorities.

Appendix II

Details of value of trust property/income in reported High Court/Supreme Court judgements in tax cases between 1970 and 1981

Citation in Income Tax Reports		Value of investments in Rs.	Annual income in Rs.	Assessment year/date of gift/date of death
1		2	3	4
(1970) 76 ITR 471	Ahmed G. Ariff v CWT	N.A. [Properties in Calcutta]	N.A.	1957-58 and 1968-59
(1970) 77 ITR 180 (AP)	CWT v Nawab Fareed Nawaz Jung and others (5 trusts)	2,96,700	7,103	1957-58 and 1958-59
(1970) 77 ITR 505 (AP)	CWT v Arundhati Balakrishna (3 trusts)			
	Trust I	5,50,325	N.A.	1958-59
	Trust II	N.A.	N.A.	1958-59
	Trust III	15,70,601	N.A.	1958-59

Contd.

Appendix II—*Contd.*

	1	2	3	4
(1970) 77 ITR 350 (SC)	CIT v Kokila Devi (Trust for benefit of deity)	3 houses (value not indicated)	N.A.	N.A.
(1971) 79 ITR 259 (Cal)	Chhaganlal Baid v CIT (Four trusts)	N.A.	54,000	1958-59 to 1960-61
(1971) 80 ITR 331 (All)	Chintamani Ghosh Trust v CWT	5,00,000	N.A.	1957-58 1958-59 1959-60
(1971) 82 ITR 699 (SC)	CWT Rajasthan v Her Highness Maharani Gayatri Devi of Jaipur	£3,00,000 ($3\frac{1}{2}$ per cent war loan)	£10,500	1959-60
(1972) 83 ITR 416 (SC)	Col. H.H. Harinder Singh v CIT	£1,80,000 (UK Government securities held in Grindlay's Bank. London)	N.A.	1957-58 to 1960-61
(1972) 84 ITR 150 (Cal)	Sri Sri Iswar Radha Govinda Jew v CIT	3,06,500	—	1951-52 to 1955-56
(1972) 84 ITR 7 (Cal)	Usha Kumar Banerjee v CED	16,51,314	—	17.4.1955
(1972) 86 ITR 153 (Guj)	CWT v Kum. Manna G. Sarabhai (4 Trusts)	N.A.	—	1958-59 assessment

(1973) 87 ITR 33 (AP)	CED v Trustees of HEH the Nizam's Family Pocket Money Trust	55,00,000	N.A.	N.A.
(1973) 88 ITR 417 (SC)	Purshottam N. Amarsey v CWT	N.A.	N.A.	N.A.
(1973) 88 ITR 47 (SC)	Gordhandas Govindram Family Charity Trust	11,00,000	N.A.	1957-58 1958-59
(1973) 90 ITR 158 (Bom)	CIT v Neville N. Wadia	N.A.	1.46,126	1959-60
(1973) 93 ITR 332 (All)	CWT v Smt. Rani Kaniz Abid	N.A. (Right to draw remuneration as Muttawalli valued at Rs. 61, 160)	5,500 (Remuneration as Muttawalli)	—
(1974) 94 ITR 361 (Cal)	CIT v Trust Estate of Tarun Kumar Roy	Several houses, *bustees* & landed properties in Calcutta	N.A.	1959-60 1960-61 1961-62
(1974) 94 ITR 144 (Mad)	CED v H.N. Markandan	N.A.	N.A.	1950
(1974) 95 ITR 476 (Bom)	CGT v Dr. R.B. Kamdin	N.A.	N.A.	1957
(1974) 95 ITR 460 (Ker)	CED v John D'Souza	7,14,000	N.A.	1962
(1974) 96 ITR 50 (Bom)	CIT v Gordhandas K. Vora	Immovable properties (Details N.A.)	N.A.	1957-58 1958-59
(1974) 96 ITR 185 (Guj)	CWT v Phirozesha Pestanji (2 Trusts)	9,22,000	N.A.	1963-64

Contd.

Appendix II—*Contd.*

	1	2	3	4
(1974) 97 ITR 246 (SC)	CIT Hyderabad v Nawab Mir Barkat Ali Khan Bahadur	30,00,000	1,00,000	1952-53 1953-54 1954-55
(1975) 98 ITR 287 (Bom)	CIT v Arvind Prasad N. Mafatlal	500 shares of Surat Cotton Spg. & Wvg. Co. Ltd.	N.A.	1960
(1975) 98 ITR 480 (All)	CGT v Maharaja Pateshwar Prasad Singh	20,31,500	N.A.	1957
(1975) 99 ITR 162 (Bom)	H.H. Maharani Shri Vijay Kunverba of Morvi and Others v CIT	N.A.	N.A.	1956-57 1957-58
(1955) 99 ITR 477 (AP)	N. Durgaiah v CGT	1,20.780	N.A.	1982
(1975) 100 ITR 699	M.S.M. Ratnaswami Nadar v CIT (Two settlements)	2,07,000	12,000	1956-57
(1975) 101 ITR 626	CWT v Smt. Arundhati Balkrishna Trust (Guj)	39,66,905 (shares and securities & cash)	N.A.	1960-61 1964-65
	Two more trusts of the same magnitude were involved—			
	CWT v Virmati Ramkrishna Trust	N.A.	N.A.	

	CWT v Padmavati Jaykrishna Trust	N.A.	N.A.	
(1975) 101 ITR 561 (Pat)	CIT v Smt. Indu Bala Sen Trust	50,000	N.A.	1961-62 1962-63
(1976) 102 ITR 356 (Guj)	Mrs. Arundhati Balkrishna v CIT (Income from Arundhati Balkrishna Trust)	N.A.	78,793	
(1976) 102 ITR 232 (Guj)	CWT v Arvind Narottam	19,25,655	N.A.	1964-65
1976) 102 ITR 248 (AP)	Addl. CIT v Trustees of H.E.H. The Nizam's Second Supplementary Family Trust (Conversion of 6000 preference shares of the Hindustan Motors Ltd. into 60,000 ordinary shares of that company and the capital gains on sale of 30,000 ordinary shares for Rs. 6,04,679)	N.A.	3,04,679	1963-64
(1976) 103 ITR 56 (Bom)	CWT (Central) v Kishanlal Bubna (2 Trusts)	75,610	N.A.	1962-63
(1977) 106 ITR 667 (Bom)	Sardaben Jayantilal Mulji & Others v CWT (2 trusts in favour of two minor daughters)	1,06,774 (Shares)	N.A.	1960-61
(1977) 106 ITR 203 (Bom)	Mrs. Monie Ardeshir Baria & Mrs. Piloo F Antia, Executrices of the	9,80,873	—	13.8.1958

Contd.

Appendix II—*Contd.*

	1	2	3	4
	estate of Ardashir D. Barie—Three separate trusts for the benefit of wife and two daughters. Amount to the credit of the trusts on 13.8.1958			
(1977) 107 ITR 426 (Bom)	CIT v Bhagwandas S. Malvi	N.A.	N.A.	1959-60
(1977) 107 ITR 45 (Bom)	K.M. Sheth v CIT	(500 shares of Chand-deo Sugar Mills Ltd. — value not indica-ted)	N.A.	1960-61
(1977) 107 ITR 661 (Mad)	CGT v Thiruvenkata Mudaliar	Two houses (value not indicated)	N.A.	1.3.1963
(1977) 109 ITR 798 (Bom)	CWT v Somaiya Trust	62,72,000	N.A.	Not specified
(1977) 109 ITR 602 (Bom)	Yogendra Prasad Mafatlal v CIT. Three trusts for three minor daughters—one with 310 shares of Mafatlal Gagalbhai and Co. (P) Ltd. and the other rwo with 75 shares each of the same company	N.A.	33,808	1962-63

(1977) 109 ITR 649 (Mad)	CED v Gourishankar Damani	About 70,000	N.A.	19.10.1966
(1977) 110 ITR 326 (Cal)	CIT v Sri Brojendra Nath Kundu	A house (value not indicated)	N.A.	Not specified
(1978) 112 ITR 652 (Guj)	CIT Gujarat v Smt. Kamalini Khatau (six discretionary trusts)	N.A.	18,000 (aggregate for all the six trusts)	
(1978) 112 ITR 725 (Cal)	CWT v B.N. Chowdhury (two trusts for minor children)	N.A.	N.A.	Probably 1955-56 (not clear)
(1978) 112 ITR 33 (Bom)	Keshaoji Morarji v CIT (two cross trusts)	6,95,000	N.A.	Probably 1955-56 (not clear)
(1978) 113 ITR 751 (Cal)	Khimji Keshavji Trust Estate v CWT	N.A.	N.A.	1965-66 1966-67
(1978) 113 ITR 185 (Com)	CIT v Trustees of Khimchand Amerchand Trust	7,60,000 (value of "Lamington Talkies")	N.A.	1960-61
(1978) 114 ITR 90 (Bom)	CCT v Mrs. Jer Mavis Lubinoff	18,66,457	N.A.	25.2.1958
(1978) 115 ITR 211 (Bom)	National & Grindlays Bank Ltd. v CWT (for a constituent)	1,14,43,836 Indian assets 1,03,26,160 Foreign assets	N.A.	1957-58

Contd.

Appendix II—*Contd.*

1		2	3	4
(1978) 115 ITR 232 (Ker)	CWT v H.H. Yeshwant Rao Ghorpade (value of 1520 shares of Sandur Manganese & Iron Ore Ltd.)	1,56,271	N.A.	1965-66
(1979) 116 ITR 344	CWT v Waqf K.B. Syed Ahmed Hussain Rizvi	N.A.	N,A.	1968-69
(1979) 116 ITR 360	CED v Sultan Alam Khan	House property (value not indicated)	—	—
(1979) 116 ITR 613	CIT v Gopaldas Agarwal	N.A.	N.A.	1956-57 to 1960-61
(1979) 116 ITR 219	Official Trustee of West Bengal v CIT West Bengal	N.A.	N.A.	1964-65 to 1967-68
(1979) 117 ITR 654 (Mad)	Hussain Sait v CED	4,55,000	N.A.	—
(1979) 117 ITR 190 (Bom)	Official Trustee of Bombay v CED	20,85,649	N.A.	1958
(1979) 117 ITR 221 (All)	K.C. Srivastava v CED	2,62,503	N.A.	1962
(1979) 117 ITR 446 (Cal)	G.B. Banerjee v CIT	House property (value N.A.)	(owner occupied)	1966-67

(1979) 120 ITR 329 (Mad)	CWT v Trustees of the Estate of V.R. Chetty (Mad)	House property (value N.A.)	N.A.	1967-68
(1979) 120 ITR 837 (All)	CIT v Smt. Shakuntala Banerjee	10,00,000	N.A.	1967-68
(1979) 120 ITR 271 (Mad)	CIT v Estate of V.L. Ethiraj	N.A.	25,004 8,17,870 36,354 26,107	1962-63 1963-64 1964-65 1966-67
(1980) 121 ITR 735 (SC)	CED v Usha Kumar	1,44,000	N.A.	1955
(1980) 122 ITR 62 (Bom)	CGT v Ebrahim Hafi Usuf Botawala	House properties (value N.A.)	N.A.	1964
(1980) 122 ITR 100 (All)	Haji Abdul Hamid v CIT	Biri business (value N.A.)	N.A.	1961-62
(1980) 122 ITR 499 (Guj)	Addl. CIT v M.K. Doshi	1,55,000	N.A.	1963-64 1964-65 1966-67
(1980) 124 ITR 501 (Guj)	K.T. Doctor v CIT	5,000	22,376	1972-73 1973-64
(1980) 124 ITR 98 (Mad)	CED v S.M. Kamaluddin Fakri	8,00,000	N.A.	1964
(1980) 126 ITR 489 (Cal)	Ayesha Khatoon & Others	N.A.	N.A.	—

Contd.

Appendix II—*Contd.*

	1	2	3	4
(1980) 126 ITR 233 (AP)	CWT v Trustees of Nizam's Miscellaneous Trust	4,83,00,000	N.A.	1957-58 to 1972-73
(1981) 128 ITR 689	CWT v Thiruvenkata Raddiar (Ker)	3,16,428	N.A.	1973-74 to 1975-76
(1981) 128 ITR 593	CED v Nirmal Kumar Roy	N.A.	N.A.	1962
(1981) 127 ITR 701	Kum. Pallavi S. Mayor v CIT (beneficiary in 18 trusts including 4 in which she was sole beneficiary)	N.A.	N.A.	
(1981) 130 ITR 479	CIT v Trustees of Miss Gargiben Trust (3 trusts, the sole beneficiaries being ladies of the Mafatlal family)	N.A.	92,788 92,790 92,680	Income of the sole beneficiary of each of the 3 trusts in 1966-67, besides capital gains of about Rs. 26,640 each, tax liability of which was disputed

(1981) 131 ITR 151 (Bom)	CWT v Kali D. Cawasji	N.A.	N.A.	—
(1981) 137 ITR 92 (Bom)	CWT v Tanil Ramdas (3 trusts)	Rs. 3,70,000 (Face value of 370 shares of a pvt. ltd. company)	—	31-3-1960 29-3-1961 & 28-3-1962

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Additional Notes

Ch. (Note):

1(1) For the extent to which the trust concept existed before the Code of 1882, the Statement of Objects and Reasons accompanying the legislation may also be seen. The draftsman of the Indian Trusts Act was Whitley Stokes who was Law Member of the Governor-General's Council at that time.

There has been little amending legislation since the Act came into force. The Law Commission has made the following observation in its Seventeenth Report, which was limited to private trusts (1961) : "The Trusts Act has proved to be a very successful piece of legislation. It has stood the test of time. Its provisions are remarkable alike for lucidity and conciseness. There have been practically very few difficulties in the interpretation of the Act. This is as much due to the skilled draftsmanship of Whitley Stokes as to the fact that the rules of the English law of trusts were well-developed by the time of the drafting of the Act." However, the English law on trusts has itself been undergoing changes. Recent English legislation includes the Trustee Act (1925), Variation of Trusts Act (1958), Administration of Estates Act (1925) and the Settled Land Act (1925). The following are some of the statutes other than the Indian Trusts Act which affect the law of trusts in India—The Indian Trustee Act, XXVII of 1866; The Specific Relief Act, XLVII of 1963; The Limitation Act, XI of 1980; The Limitation Act, XXXVI of 1963; the Official Trustee Act, II of 1913; the Official Trustees (Amendment) Act, XLVIII of 1964; the

Transfer of Property Act, IV of 1882 (sections 10 and 18); the Indian Succession Act, XXXIX of 1925 (sections 112-118); the Penal Code (sections 405-9); Trustees' and Mortgagees' Powers Act, XXVIII of 1866; Specific Relief Act, I of 1877 (which contains a definition of a trust in section 3, with illustrations appended to it).

1(9) For a case of "dedication" of property to an irrevocable trust without its actual divestiture, see Peerchand Phoolchand v CIT, Special Leave Petition No. 8608 of 1980, dismissed by the SC on 4/4/83 (1983) 142 ITR 3 (Statutes).

1(15) If the class of objects is conceptually uncertain, the trustee cannot exercise the power of selection. If the problem is evidential uncertainty, there may be difficulty in the exercise of the power but the power itself is not invalid. The difference between the two situations can be illustrated by contrasting "friends" with "first cousins". It may not be possible to find out all the friends of a settlor or testator but first cousins are ascertainable with less difficulty. See R.P. Austin, "Discretionary Trusts : Conceptual Uncertainty and Practical Sense", *The Sidney Law Review*, Vol. IX, no. 1, January 1980.

1(40) If a person has the discretion to operate an alleged trust as he likes he cannot be taken to be a trustee known to the law : Advocate General v Yusuf R.E. Ibrahim, AIR 1929 Bom 338; 84 IC 759.

1(45) Sec. 34 of the Indian Trusts Act resembles sec. 57 of the English Trustee Act, 1925. For the court's powers under section 34, see Official Trustee, West Bengal v Sachindra Nath Chatterjee AIR 1969 SC 823, which has followed the decision of the HL in Chapman v Chapman (1954) AC 429.

1(57) The fact that the trustee has claimed that the trust is a private trust will not disentitle the trustee

to the benefit of tax exemption if properties are clearly held under a trust for religious or charitable purposes : Velambal Ammal v Agl. ITO (1963) 47 ITR 558 (Mad).

1(58) A trust may ordinarily be taken to be private unless proved to be public. If somebody claims that his institution is private and the Charity Commissioner believes that it is public, it is for the latter to prove that it is public : Martand Pandharinath Harkari v Charity Commissioner 1963, Bom LR 274.

1(66), 1(70), 1(73) A society which is predominantly political in its objects will not be eligible for tax exemption in respect of any part of its income merely because some of its objects are charitable. For tax exemption, either all the objects of a society/trust should be charitable or an identifiable part of its income should be specifically applicable for charitable purposes : CIT v All India Hindu Mahasabha (1983) 140 ITR (Del).

1(69) In the UK, a trust for making spelling simpler cannot be classified as a trust which will be beneficial to the community : Trustees of Sir G. B. Hunter (1922) "C" Trust v IR (1929) 14 TC 427. A trust to enrol voluntary workers for carrying on essential public services in the event of strikes and public lock-outs exists for political action and not for charitable purposes : Trustees for the Roll of Voluntary Workers v IR (1941) 24 TC 320.

1(72) "Debuttar" is derived from the Sanskrit word "devatra". When the property dedicated to a deity is large, and the religious ceremonies to be performed are prescribed by the person who has made the endowment, the entire income from the property may not be exhausted. A portion of the beneficial interest cannot but vest in the heirs in such a case : Jadugopal v Pannalal AIT 1978 SC 1329.

1(89) Also Re. Ames' Settlement (1946) Ch. 217: (1946) 1 All ER 689. A marriage settlement confers

no right to the married couple, if the marriage is nullified.

1(91)) There is need in India for legislation similar to the UK Variation of Trusts Act, 1958, but see the penulitinate para of additional notes in 10(6) below.

1(92) When one of the two beneficiaries of a trust dies, the trust does not come to an end : Stott v Ratcliffe (1982) 126 SJ 310, summary in BTR c 49-50, 1982-83, no. 6.

3(1) For a discussion on the implications of a settlement as distinct from a trust, with reference to sec. 3 of the Stamp Act (2 of 1899), see the case of the Chief Controlling Revenue Authority, Board of Revenue, Madras v P.A. Muthukumar AIR 1979 Madras 5.

The difficulty experienced in the interpretation of uncertain words and phrases in taxation laws is demonstrated by IR v Plummer (1979) STC 793 (HL), mentioned at n. 63 (p. 57). The contention of the Revenue that the definition of a "settlement", which covered "any trust, covenant, agreement or arrangement", applied to all transactions that did not have a *bona fide* commercial reason, including transactions designed to avoid tax, was rejected by the HL in this case. An element of "bounty" has been held to be a necessary characteristic of a "settement". Also see, Bulmer v IR (1967) 44 TC; Copeman v Coleman (1939) 22 TC 594; Chamberlain v IR 25 TC 317.

3(7) If a trust deed provides for remuneration to the managing trustee, and the settlor himself becomes the managing trustee, that will not amount to a reservation of any interest and the trust property will not be deemed to pass on the settlor's death under sec. 12(1) of the Estate Duty Act, 1953 : CED, Vidarbha & Marathwada v Smt. Mangala (1983) 143 ITR 491 (Bom).

3(9,67)
6(5) The case of CIT v Nandiniben Narottamdas (1983) 140 ITR 16 (Guj) has been followed in

another case of a "donation" of share in a partnership to a trust and diversion of the income to the donor's daughters : Jyotsnaben Narottamdas v CIT (1983) 142 ITR 91.

3(26, 166, 167) Quantification of shares does not mean specification of shares in terms of rupees and paise. The provisions of sec. 164 will not be applicable if the aliquot shares of the beneficiaries are specified. The imposition of restrictions on the beneficiaries' withdrawal of amounts from the trust business or the vesting of the trustee with power to retain substantial cash will not justify a single assessement on the trustees under section 164 : CIT v K. Balakrishna Rao (1983) 143 ITR 651 (Mad).

3(36, 110) The Supreme Court dismissed SLP (Civil) number 9144 of 1982 filed in Gunvantal Jiwanlal Family Trust v CIT against the Gujarat High Court decision reported in (1982) 133 ITR 162 that the minor children having separate income cannot be held to be dependent upon the settlor of a trust for their maintenance and support within the meaning of clause (iii) of the proviso to section 164(1). The trustees would accordingly be liable to tax at the rate of 65 per cent in such circumstances : (1983) 140 ITR (Statutes) 5.

3(38) Once a trust is found to be for a public charitable or religious purpose, it will not be hit by the provisions regarding oral trusts in the Income-tax and Wealth-tax Acts, which are confined, in their scope, to private oral trusts. Where the origin of an endowment is obscure and no definite evidence is available to show whether it is for a public religious or charitable purpose, the court resolves the controversy about the character of that trust after taking into consideration the object and purposes for which the trust was created, the manner in which the property has been dealt with, contribution or participation of the public, etc.: P. K. Goswamy and Others v Mohd

Hanifa (deceased) by legal representatives, and others, AIR 1946 SC 1569.

3(57) A gift does not cease to be such if it is made through a trust. The trustee who has the legal ownership is not the real object of the bounty though it may be possible to regard him and the beneficiary together as donees : The Commissioner for Stamp Duties for New South Wales v Perpetual Trustee Co. (1948) 1 All ER 525, 530; Wheeler v Humphreys 1918 AC 506, 508, 509.

3(68) For an interesting discussion on once-for-all payment of capital to life beneficiary, see A.J. McClean, "Variation of Trusts in England and Canada", *Canadian Bar Review*, Vol. XLIIJ, No. 2, May 1969, pp. 181-261.

3(69) If a trust document is not stamped or is insufficiently stamped, the document may not be admissible in evidence till the requisite stamp duty is paid but the trust will not be invalidated : Poornachandra v Kalipada Roy, AIR 1942, Cal 386.

3(70) When an executor becomes a trustee is indicated in several other cases also : Estate of IAT Ward v CIT (1961) 43 ITR 219 (MP); Asit Kumar Ghose v Commr of Agl IT (1952) 22 ITR 177 (Cal); Jahangir Rustomji v Bai Kuku Bai (1903) ILR 27 Bom 281; Estate of V.R.R.M.S. Chockalingam Chettiar v CIT (1960) 40 ITR 429 (Mad); Suhasini Karuri and another v WTO (1962) 46 ITR 953 (Cal).

3(72) Initial donors are founders of a trust but subsequent donors do not automatically become donors or trustees even in regard to the property gifted by them : Gangaram v Dooboo Mania AIR 1936, Nagpur 223.

3(96) When the shares of the beneficiaries are indeterminate, the manager of a Court of Wards is liable to pay tax at the maximum rate notwithstanding pending litigation on government's claim of escheat : Manager, Court of Wards v CIT (1983) 140 ITR 78 (Pat).

3(135) In a gift, whether *hibba* or *sadaqaka*, the corpus of the property may itself be consumed, while in a *waqf* it is only the usufruct that is available for use : Nabi Hassan v Gajadhar Singh, AIR 1974 Patna 141.

3(140) The legal history of *waqf-alal-aulad* is given in the Supreme Court decision in Mohd. Ismail v Sabir Ali, AIR 1762 SC 1922. A Muslim is not precluded from creating a public religious or charitable trusts, which does not conform to the conventional form of *waqf* : Nawab Aziz Yar Jang v Director of Endowments, AIR 1963, SC 985.

Where no part of the income of a *waqf* can be distributed to any person other than the members of the family of the *waqif*, and poor Muslims come in only in the event of the entire line of the family becoming extinct, it will be a case of *waqf-alal-aulad* simpliciter : Tamil Nadu Waqf Board v M. Ibrahim Mutawalli and Others, AIR 1979 Madras 231.

3(146) Once a *waqf* comes into existence a breach of trust cannot revoke it : Waji-ud-in Ashraf Shah v Murtaza Asharaf Shah, AIR 1930 Oudh 120 IC 828.

3(172, 173) Exemption from duty under section 33(1)(n) will not be available if the deceased has not retained the right to exclusive use of the house he occupies : Miss A.N. Khan v First Assistant Controller of Estate Duty (1983) 140 ITR 293.

3(177) The Madras High Court has held that there can be private *Mutts* : Sathappayar v Periaswamy (1890) AIR 14 Mad 1. There are also *Mutts* in which property is given to the head of a *Mutt* for his personal benefit : Madapam Madipudi Koti Veerayya v Board of Commissioners, AIR 1938 Mad 810; 179 IC 275.

3(178) Where a trust had been created for the maintenance and education of the settlor's children and powers were reserved to the trustee to execute supplementary

documents to strengthen the trust, supplementary deeds granting benefits to the settlor were beyond the powers of the settlor and the trustee. The original deed was operative and no part of the settled property could be taken to pass on the settlor's death : Manindranth Mukherjee v A C E D (1983) 140 ITR 476 (Cal).

4(19) The existence of a valid power of accumulation would prevent the beneficiary's having an interest in possession, since the trustees would take time to decide whether the income that had already arisen should be accumulated and the beneficiary's entitlement to the income would depend on the decision : Pearson v IR (1980) 2 WLR 872 (HL); (1980) 2 All ER 479.

4(39) The English law of trusts was introduced into Cyprus when it came under British administration in 1880. Nigeria, Ghana, Malaysia and Singapore have also followed the English law : G.W. Keaton and L.A. Sheridan, *The Comparative Law of Trusts in Commonwealth and Irish Republic*, 1976, Barry Rose.

5(11) The Asprey Committee has pointed out the need for a statutory provision to ensure that where an amount is received by a beneficiary at any time, it enters into the calculation of the personal entitlement of the beneficiary for purposes of allocating the net income of the trust to him (Taxation Review Committee, Australia, *Final Report*, 1975, para 15.5).

5(12) See sec. 677(a) of the US Code. If the grantor of a trust had been willing to maintain the periodical premium out of his own funds before he created the trust, the trust would simply be an irrevocable commitment of the income from the same ultimate source to the same purpose. If the trust income was used to meet the grantor's legal support obligations—the medical bills of the children of the grantor, for example—it could only be treated as his

income. It involved no substantial change in his economic position and was merely a reallocation of income within the family group : Burnet v Walls 281 US 376 (1930).

6(1) For a discussion on the use of a trust as an alternative to and not a duplication of a corporation, see Yves Caron, "The Trust in Quebec", *McGill Law Journal*, 1980, Vol. XXV, no. 4.

7(21) See also CIT v Wadilal Chunilal (1963) 47 ITR 305 (Bom).

7(22) Where a workshop was settled on trust for the benefit of Aurobindo Ashram of Pondicherry, which was exempt from tax as a charitable institution, it was held that the workshop was entitled to only the limited tax exemption available on actual donations to the Ashram under section 80G : it was not a branch of the Ashram but a different entity with different objects : CIT v Workshop Trust (1983) 142 ITR 26 (Mad).

7(79) In the UK, section 15 of the Family Law Reform Act, 1969 provides that in a disposition made on or after the 1st July, 1970 any reference to a child of any person shall be taken to include an illegitimate child: see P.M. Bromley, *Family Law*, 1977, Butterworth's, London, 5th ed., p. 577. Sec. 100 of the Indian Succession Act 1925 states that "in the absence of any intimation to the contrary in a will the word 'child', the word 'son', the word 'daughter' or any word which expresses relationship is to be understood as denoting only a legitimate relative, or, where there is no such legitimate relative a person who has acquired, at the date of the will, the reputation of being such relative".

8(15) The US Foreign Investment in Real Property Tax Act of 1980 subjects to US income tax a foreign person's entire income from dispositions of his interests, direct or indirect, in US real property. See Arthur A. Feder and Lee S. Parker, *United States*

Legislation—Taxing Gains of Foreign Persons for Dispositions of Direct and Indirect Interests in US Real Property, BTR 1981, pp. 83-103, and 176-90.

The Tax Reform Act of 1976 also sought to curb the use of foreign trusts as a tax-planning device in the USA. Earlier, it had been possible to have income accumulated in a foreign trust and enjoy the advantage of a tax deferral. When the income was actually distributed, the income tax had to be worked out as the sum of the taxes that would have been hypothetically payable if the income had been received during the different years during which it had been earned by the trust. Code section 668 charged a special tax at 6 per cent of the income tax leviable on the income distributed, multiplied by the number of years during which the income had been accumulated, subject to the total demand not exceeding the amount of income distributable to the concerned beneficiary.

Code section 679 requires the US settlor to pay tax on the income from property transferred to a foreign trust that has a US beneficiary under the grantor trust rules (secs. 671-679). These rules ignore the existence of the trust and tax the grantor if he has a reversionary interest taking effect within ten years, or if the trust is revocable or if he has reserved certain powers.

But even these provisions are not invulnerable: see Egerton W. Duncan, "Use of Foreign Trusts by Non-resident Aliens", p. 113-19, *The International Tax Journal*, Vol. 9, No. 2, December 1982. For an indication of the optimum tax position that can be secured under both the US and the Canadian death tax regimes and the importance of drafting multiple trusts for wills of US citizens resident in Canada, see Hugh B. Lambe, "Will Planning for U.S. Citizens resident in Canada", *Canadian Tax Journal*, Vol. 30, No. 3, May-June 1982, pp. 335-359.

For the Canadian tax consequences of administering a trust resident in Canada that has resident and non-resident beneficiaries, see Gordon Cooper, "Canadian Resident inter vivos Trusts with Non-resident Beneficiaries", *Canadian Tax Journal*, Vol. 30, No. 3, May-June 1982, pp. 422-438.

For a case of apportionment of accumulated gains in a descretionary trust with non-resident trustees, see Leedale v Lewis, Simon's Intelligence, Oct. 22, 1982, reported in BTR, C 71-72, 82-83.

For the complexities of the residence of trusts, see Richard A. Green, "The Residence of Trusts for Tax Purposes" *Canadian Tax Journal*, May-June 1983, pp. 217-35.

8(22) In the UK, trusts were dealt with in over 700 separate local offices. The work was concentrated in 55 selected Tax Districts in 1982-83. The Chief Inspector's office in the UK has two branches, one dealing exclusively with charities and the other advising on trusts and deeds.

The *inter vivos* trust has been effectively used for tax reduction in Canada. For some of the questions of law that have come up in this connection, see Marshall A. Cohen, *Income Taxation of Inter Vivos Trusts*, 1964, Canadian Tax Foundation.

10(6) As for the US experience, David Westfall sums up the position as follows : "In few other areas is a lawyer's work as tax-dominated as it is in the creation if irrevocable *inter vivos* trusts . . . The conclusion is inescapable that irrevocable *inter vivos* trusts usually are created primarily to save taxes and in forms dictated by tax considerations. They are part of a nation wide adventure in tax avoidance." (Westfall, "Trust Grantors and Section 674: Adventure in Income-tax Avoidance", *Columbia Law Review*, 326 (1960), reproduced at page 471, *Readings in Federal Taxation*, edited by Frank E.A.

Sander and David Westfall, Foundation Press, New York).

In his message on the Revision of the Tax Laws, in 1950, President Truman attributed the low yield of federal estate and gift taxes in the USA to "excessive exemptions, unduly low effective rates of most estates and the fact that the law as written favours large estates for small ones and leaves substantial amounts of wealth completely beyond the reach of the tax laws." (HR Doc. No. 451, 81st Congress, 2nd Sess, 6-7, 1950, quoted at page 591 of *Readings in Federal Taxation*). The contribution of trusts to development of this situation was, perhaps, not negligible.

Pechman points out that the trust device had been frequently used by the wealthy to transfer property to the later generation. In the 1940s and 1950s more than three of every five millionaires transferred at least some of their property in trust. Transfers on trust accounted for at least one-third of non-charitable transfers by millionaires in this period. While those with smaller estates gave much more of their property outright, trusts were used primarily by the rich. (Joseph A. Pechman, 1977, *Federal Tax Policy*, 3rd ed., Studies of Government Finance, Brookings Institution). According to Rembar, the main contemporary motive of trusts is "the ancient one of thwarting the overlord, now resident in Washington : trusts are a prominent tax avoidance device". (Charles Rembar, *The Law of the Land—The Evolution of Our Legal System*, Simon & Schuster, New York, p. 298). The official version, reproduced at n. 6, p. 190, corroborates these findings.

As for the redistributory effect of the estate duty levy in the UK, the Royal Commission on the Distribution of Income and Wealth (Cmnd 6171, published in 1975) pointed out that in 1960, 63.1 per cent of the total wealth of England and Wales was owned by 10 per cent of the population. Despite the fact

that the estate duty ranged upto 80 per cent, the Commission found in 1973 that 10 per cent of the population still owned 50.9 per cent of the wealth of the country. Trusts and settlements are the convenient strategies employed for so arranging one's affairs that the least duty is paid under the law on one's death. See n. 51 p. 149.

According to Riddall, the majority of applications to the court for variation of trusts in the UK under the Variation of Trusts Act, 1958 have been made with a view to reducing the tax which would become due if the trusts remained unaltered: J. G. Riddall, *The Law of Trust,* 1982, 2nd ed., Butterworths, p. 250.

The Law Reform Committee, on whose report the Variation of Trusts Act 1958 was based, saw no objection to such tax-induced variations (*Sixth Report*, 1957, Cmnd 310, para 16). Courts have not, however, been unanimous on the propriety or otherwise of a variation on this ground : see Tinker's Settlement (1960) 1 WLR 1011, 1013 (not in public interest). Variations were sanctioned in several cases on the ground that they were of advantage to the beneficiaries : Re. Holinden's Settlement Trusts (1966) 1 Ch 511, on appeal (1968) AC 685; Re. Holt's Settlement (1969) Ch 100; Re. Drewe's Settlement (1966) 2 All ER 844, (1966) 1 WLR 1518; Re. Clitheroe's Settlement Trusts (1959), 3 All ER 789 (1959), 1 WLR 1159. Lord Denning did not consider that it would be for the benefit of children to be uprooted from England and transported to Jersey simply to avoid tax : Re. Weston's Settlements (1969) 1 Ch 223 (1968) 1 All ER 338. Migration to Canada, swayed by the same purpose, was, however, approved by the court in the case of Seale's Marriage Settlement (1961) Ch 574 (1961) 3 All ER 135.

The Indian experience has, by and large, been similar. It is a trite saying that laws are like cobwebs, where the small flies are caught and the great break

through. Courts are constrained to proceed on the basis of the letter of the law; and if this results in leakage of revenue, it is for the legislature to amend the law suitably, vide Lord Wilberforce's emphasis on the decisive importance of the legal form (p. 137).

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