

INCOME-TAX REFERENCE

1952
Oct. 6

Before Mr. M. C. Chagla, Chief Justice, and Mr. Justice Tendolkar.

J. K. TRUST, APPELLANT v. THE COMMISSIONER OF INCOME-TAX,
EXCESS PROFITS TAX, BOMBAY CITY, RESPONDENT.*

Indian Income-tax Act (XI of 1922), s. 4 (3) (i),—Trusts of charitable trust—Trustees as such appointed managing agents of mills—Managing agency commission earned by the trustees—Such commission when earned to be applied to charitable objects specified in trust-deed—Whether such commission is exempt under s. 4 (3) (i)—“any income derived from property held under trust”: true interpretation of it—Whether benefits under a contract constitutes “property”.

Trustees of a charitable trust, who were empowered by the Trust Deed to carry on business of managing agents of any company with the help of the Trust funds and to apply the income earned in such business to charitable objects specified in the Trust Deed, were appointed managing agents of certain Mills and as such managing agents they earned commission. On the question whether such commission was exempt from taxation under s. 4 (3) (i) of the Indian Income-tax Act, 1922,

Held, that s. 4 (3) (i) of the Act confers exemption only upon income which is derived from property which is settled upon a charitable trust and not upon any income which is itself settled upon a charitable trust. Unless the property from which the income is derived is made the subject of a charitable trust, the making of a trust with regard to mere income would not entitle the assessee to claim exemption from taxation under the section.

Held, therefore, that as there was no trust of the managing agency itself or of the managing agency business from which the commission was derived, the commission earned by the trustees as managing agents was not income derived from property held under trust or other legal obligation wholly for religious or charitable purposes and therefore was not exempt from taxation under s. 4 (3) (i) of the Act.

Quaere, whether a benefit under a contract constitutes property within the meaning of the section.

All-India Spinner's Association v. Commissioner of Income-tax, Bombay⁽¹⁾, *Commissioner of Income-tax, Bombay v. Currimbhoy Ebrahim and Sons Ltd.*⁽²⁾, *Commissioner of Income-tax, Bihār and Orissa v. Raja Bahadur Kamakhya Narayan Singh and others*⁽³⁾ and *Charitable Gadodia Swadeshi Stores v. Commissioner of Income-tax, Punjab*⁽⁴⁾

Sir Padampat Singhania, Lala Kailaspat Singhania and Lala Lakshmiapat Singhania created a trust in respect of a sum of Rs. 1,00,000 by a Deed of Trust dated June 15, 1945. According to the terms of the Trust Deed the said sum or the income thereof was to be applied for all or any of the charitable

* Income Tax Reference No. 1 of 1952.

⁽¹⁾ (1944) 12 I. T. R. 482.

⁽²⁾ (1935) 3 I. T. R. 395.

⁽³⁾ (1948) 16 I. T. R. 325 at p. 328.

⁽⁴⁾ (1944) 12 I. T. R. 385.

objects specified therein. The Settlers along with Lala Ramdeo Poder and Sir Chunilal V. Mehta were appointed trustees of the Trust Fund. Clause 3 of the Deed of Trust provided as follows: "The Trustees may with the help of the Trust Fund for and on behalf and for the benefit of the Trust carry on such business including the taking up and conducting the Managing Agency or Selling Agency of any Company in such name or names as they in their absolute discretion may think fit and proper.....and utilise the profits derived therefrom for all or any of the objects aforesaid.....". Clause 4 empowered the Trustees to invest the Trust Fund, *inter alia*, in deposits or loans with or to any Company on such terms as to repayment or interest as they may think proper.

By an agreement dated August 3, 1945 between the Rayon Woolen Mills of the one part and the Trustees of the other part, the trustees were appointed Managing agents of the Mills. Under the agreement, the trustees as such Managing Agents were entitled to receive commission at the rate and in the manner specified in the agreement. Clause 7 of the agreement provided as follows: "During the continuance of this agreement the Managing Agents shall maintain with the Company a deposit of Rs. 1,00,000 in cash by way of security for due fulfillment of their obligations as specified herein and shall be entitled to charge interest at 3½ per cent per annum on the amount of such deposit in addition to their remuneration."

In pursuance of the terms of the Managing Agency agreement, the Trustees deposited Rs. 1,00,000 with the Mills and received interest on the amount at the rate of 3½ per cent per annum. The amount of interest earned on this fund was, it was conceded by the Income-tax Department, exempt under s. 4 (3) (i) of the Act.

The Trustees as the Managing Agents of the Mills earned certain amounts as commission which they were bound to use for the purpose of the Trust. They therefore, contended before the Income-tax authorities that the income earned by them from the Managing Agency business was also exempt from taxation under s. 4 (3) (i). The Income-tax Appellate Tribunal was of opinion that the income was not so exempt for, according to the Tribunal, the income as soon as it was earned became subject to taxation and no body could create a trust of his future income for charitable purposes in order to claim exemption under s. 4 (3) (i).

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At the instance of the Trustees the Tribunal referred the following question to the High Court:—

(1) Whether on the facts of the case the commission earned by the Managing Agents for managing the Raymond Woollen Mills was income earned by the Managing agents for services rendered and not income derived from property held under Trust or other legal obligation and therefore not exempt under s. 4 (3) (i) of the Income-tax Act?

(2) Whether on the facts of the case the business carried on by the Trustees falls to be considered under s. 4 (3) (i) or 4 (3) (ia) of the Income-tax Act?

The Reference was heard.

Sir J. B. Kanga with *R. J. Kolah* and *D. H. Dwarkadas*, for the appellants.

Sir N. P. Engineer with *G. N. Joshi*, for the respondent.

CHAGLA C. J. A very interesting question arises in this reference as to the true interpretation of s. 4 (3) (i) of the Income Tax Act. The assessee is the trustee of what is known as the J. K. Trust and the Trust was created by Sir Padampat Singhania, Lala Kailashpat Singhania and Lala Lakshmiapat Singhania for a sum of Rs. 1,00,000, and it is admitted by the Department that the Trust was for charitable purposes. It is also not disputed that as far as the sum of Rs. 1,00,000 is concerned it is property which is held for charitable purposes within the meaning of s. 4 (3) (i) of the Act. The Trustees of this Trust were appointed the managing agents of Raymond Woollen Mills Ltd. and as such managing agents they have earned commission, and the question is whether the commission earned by the Trustees is exempt from taxation.

Now, under clause 3 of the trust deed, the Trustees are empowered with the help of the trust fund for and on behalf of and for the benefit of the Trust to carry on such business including the taking up and conducting the managing agency or selling agency of any company, and the Trustees availing themselves of the power conferred upon them under the trust deed have acted as the managing agents of the Raymond Woollen Mills. Under the managing agency agreement the Trustees have deposited a sum of Rs. 1,00,000 which constituted the trust fund and under the agreement the Trustees received interest at the rate of 3½ per cent per annum, and the Income

Tax Department does not dispute the fact that as far as the interest earned on this fund is concerned it is exempt under s. 4 (3) (i) of the Act. With regard to the commission earned by the Trustees, in order that exemption can be claimed we must be satisfied that the managing agency commission constitutes an income derived from property held under trust or other legal obligation. The only property which is held under trust or other legal obligation is the sum of Rs. 1,00,000 which is settled on trust, and really on the facts of this case the very narrow question that arises for our determination is whether the managing agency commission constitutes income derived from the sum of Rs. 1,00,000 settled upon trust. Sir Jamshedji has argued that there is an obligation upon the Trustees to apply every anna of the commission earned by them as managing agents. Undoubtedly clause 3 of the trust deed impresses the commission earned by the Trustees with the same trust as the sum of Rs. 1,00,000 which was settled upon trust and there can be no doubt that there is an obligation upon the trustees who have been appointed as managing agents, as the trustees of the J. K. Trust to apply the whole of the commission earned by them to the charitable objects of the trust. But it is hardly necessary to emphasise the fact that s. 4 (3) (i) does not confer any exemption upon income which is settled upon a charitable trust. The exemption is only conferred upon income which is derived from property which is settled upon the charitable trust. Therefore in order that the exemption can be successfully claimed, the most important ingredient that has got to be satisfied is that there must be some property which is settled upon trust, that the property is settled upon a charitable trust, and that there is income which is derived from that property and with regard to that income a claim is made that it is exempt from taxation. It is not sufficient for a person to make a trust of his future income to claim exemption under s. 4 (3) (i). Unless the property from which that income is derived is also made the subject of a trust, the mere making of a trust with regard to the income will not be sufficient to claim exemption under s. 4 (3) (i).

In this case the only property which has been settled on trust is the sum of Rs. 1,00,000 and Sir Jamshedji is right that if with the help of this trust fund any business is carried on then the income or profit derived from that business would be free from taxation. But in order that that position can arise, the trust fund must be invested in a business, that business must yield

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profits, and then it could be said that the profits were derived from the business which was settled upon trust because the trust funds were invested in that business. When we look at the facts of this case and the two documents, which are before us, it is clear that the managing agency commission was neither derived from the trust fund nor was the trust fund invested in the managing agency business. Turning to the first aspect of the case, it is clear that the managing agency commission is derived from the services rendered by the trustees as managing agents. It is a remuneration paid to them for the work they did as managing agents. It has nothing whatever to do with the trust fund of Rs. 1,00,000. The remuneration earned by them has no connection with the trust fund. All that the trust fund yields is the interest of $3\frac{1}{2}$ per cent per annum. But it is by reason of their personal labour and by reason of the services rendered by them that the trustees earned the commission as managing agents. Therefore when the managing agency commission comes to their hands it comes to them not as income derived from property settled upon trust, but it comes to them as managing agents, who have rendered services to the company. As soon as the income comes to their hands, tax is attracted to it and when the income is in their hands the Trustees cannot say that we have received this income from property which is held on trust. It is only after the income comes to their hands and tax is attracted to it that an obligation arises upon them to use that income for purposes of the trust. Therefore there is a trust of income earned by the trustees as managing agents. There is no trust of the managing agency itself or the managing agency business from which the commission is derived.

Turning to the second aspect of the matter, can it be said that the trustees have invested the sum of Rs. 1,00,000 in the managing agency business? It may be conceded for the sake of argument that the managing agency is a business. When we turn to the managing agency agreement it confers various obligations upon the managing agents and one of the most important obligation is that they have to advance to the company loans up to Rs. 10,00,000 at any time and if they are not in a position to advance these loans themselves they have to guarantee such loans if others advance them. As far as the trust fund is concerned, the sum of Rs. 1,00,000 is earmarked as a deposit under clause 7 of the managing agency agreement. It must remain with the company by way of security for the

due fulfillment of the obligations of the managing agents. Therefore it is clear that if the managing agents have to advance loans or have to guarantee loans, the advance of loans cannot be made out of the trust fund nor can any guarantee be discharged from the trust fund because there are no trust funds beyond the sum of Rs. 1,00,000 which is kept as a deposit with the company. Therefore the only purpose that the trust fund has played in this managing agency business is that it has served as a deposit for the discharge of the obligations of the managing agents. With regard to the rest, no part of the trust fund has played any part whatsoever in the business which the trustees have carried on as managing agents of the company. There seems to be no connection whatsoever between the commission earned by the managing agents and the keeping in deposit of the sum of Rs. 1,00,000. It is difficult to see how it could possibly be stated on the facts of this case that the sum of Rs. 1,00,000 which constitutes the trust fund is invested in the managing agency business.

Reliance has been placed by Sir Jamshedji on a decision of the Privy Council in *All India Spinners' Association v. Commissioner of Income Tax, Bombay*⁽¹⁾. In that case two questions arose for the decision of the Privy Council. One was whether there was a trust or other legal obligation under which the property from which the income was derived was held, and the second was whether it was a trust or legal obligation for the relief of the poor or for any other object of general public utility. The High Court of Bombay had taken the view that it was not a charitable trust within the meaning of the Income Tax Act. That finding was not accepted by their Lordships of the Privy Council. On the other question whether the property was held upon trust within the meaning of the Act, their Lordships of the Privy Council pointed out that by cl. 3 of the trust deed it was expressly provided that the funds and assets of the association were to vest in the trustees to be held for the purposes of the association, and their Lordships further held that the property of the association consisted of the organization and the undertaking as well as the fluctuating stock of yarn and cloth. Therefore the income for which the All India Spinners' Association was claiming exemption was the income derived from the whole organization and undertaking of the association, which organization and undertaking included the stock of yarn and cloth.

⁽¹⁾ (1944) 12 I. T. R. 402.

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Then reliance has been placed on another Privy Council decision in *Commissioner of Income Tax v. Currimbhoy Ebrahim & Sons*,⁽¹⁾ and in that case the Privy Council was considering the meaning to be given to the expression "property". They were construing the word "property" as used in s. 42 (1) of the Act and the opinion their Lordships gave was that the word property as it occurs in sub-s. (1) of s. 42 could be given so special a colour but was used as an ordinary English word to be taken in its usual signification subject to the context provided by the rest of the sub-section, and this expression of opinion of the Privy Council is relied upon by Sir Jamshedji for urging that the expression property used in s. 4 (3) (i) is used in its widest signification. The Privy Council has emphasised the fact that there is no definition given of the expression "property" in the Act, and "property" must be construed in its plain natural meaning subject to the context in which that expression occurs. Sir Jamshedji has advanced a very interesting argument that "property" in the sense used in s. 4 (3) (i) is used in the sense in which it includes all proprietary rights, both rights in rem and rights *in personum*, and according to Sir Jamshedji even if the commission earned by the managing agents was as a result of a contract and the commission constituted a benefit under the contract, the benefit under the contract would be property within the meaning of s. 4 (3) (i). In our opinion it is unnecessary to decide this question because, as we have already pointed out, the only property which is held on trust in this case is the sum of Rs. 1,00,000 in respect of which the trust has been constituted. It is unnecessary to launch upon an inquiry as to whether benefits under a contract would or would not constitute property because as far as this case is concerned there is no benefit under any contract which has been held under trust. It is either the sum of Rs. 1,00,000 with which we are concerned or any business started with the assistance of that sum of Rs. 1,00,000, and, as already pointed out, in this particular case the managing agency commission is derived neither from the sum of Rs. 1,00,000 nor from any business which has been started with the assistance of that sum of Rs. 1,00,000.

Reference might also be usefully made to the definition of the expression "derived" given by the Privy Council in *Commissioner of Income-tax, Bihar and Orissa v. Kamakhaya Narayan Singh*⁽²⁾. It is true that their Lordships were there considering

⁽¹⁾ (1935) 3 I. T. R. 355.

⁽²⁾ (1948) 16 I. T. R. 325 at p. 228.

the question of agricultural income, but the interpretation placed upon the expression "derived" by their Lordships is not without assistance for interpreting the same expression in s. 4 (3) (i). The expression used in this section is "any income derived from property held under trust", and to put upon it the interpretation put by the Privy Council, the property must be the effective source from which the income arises. It is not sufficient that the property should be indirectly responsible for the income. The income must directly and substantially arise from the property held under trust, and on the facts of the case before us it is impossible to contend that the managing agency commission effectively and substantially arose from the sum of Rs. 1,00,000 which was settled on trust.

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A question has also been submitted to us by the Tribunal whether on the facts of the case the business carried on by the trustees falls to be considered under s. 4 (3) (i) or s. 4 (3) (ia) of the Indian Income Tax Act. The interpretation of s. 4 (3) (ia) is not free from doubt or difficulty. One interpretation has been put upon it by the Lahore High Court in *Gadodia Swadeshi Stores v. Commissioner of Income-tax, Punjab*.⁽¹⁾ In our opinion it is unnecessary to consider what is the true construction to be placed upon s. 4 (3) (ia) because it is common ground that even if s. 4 (3) (ia) applied neither of the two conditions laid down in sub-clause (a) or (b) has been complied with by the assessee. Therefore if the assessee is entitled to exemption at all, it can only be on his case falling under s. 4 (3) (i). Therefore we do not think it necessary to construe s. 4 (3) (ia) for the purposes of this reference. It may be said that the result we have come to is rather unfortunate because in a case where the trust is admittedly a charitable trust and where the commission earned by the trustees is admittedly applied to charitable purposes, the income cannot be held to be exempt from tax. But perhaps it is necessary to point out that the Income Tax Act unfortunately does not permit an assessee to give his income in charity and to claim exemption by reason of that generous impulse except under s. 15B of the Act. It is only in very restricted cases that an income is exempted from tax under s. 4 (3) (i) or s. 4 (3) (ia).

⁽¹⁾ (1944) 12 I. T. R. 385.

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In the result the answer to question (1) is that the commis-
 sion earned by the assessee is not exempt under s. 4 (3) (i).
 Question (2) is unnecessary. Assessee to pay the costs.

Attorneys for applicant: *Kanga & Co.*
 Attorneys for respondent: *N. K. Petigara.*

Answer accordingly.
 P. M. P.

APPEAL FROM TESTAMENTARY AND INTESTATE
 JURISDICTION.

Before Mr. M. C. Chagla, Chief Justice, and Mr. Justice Tendolkar.

HIRJIBHOY RUSTOMJI PATEL, APPELLANT (ORIGINAL PETITIONER) v.
 THE STATE OF BOMBAY, RESPONDENT.*

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*Indian Succession Act (XXXIX of 1925), ss. 219, 259—Estate of deceased
 not fully administered—Letters of administration de bonis non—
 Counsel appearing as amicus curiae—Whether entitled to costs—
 Practice.*

On the death *intestate* of a Parsi, R., leaving behind him M. (his mother) and H. (his brother), M. took out letters of administration to R.'s estate as his sole heir, but she died before R.'s estate was fully administered. H. thereupon applied for letters of administration *de bonis non* to R.'s estate. The trial Court having held that H., the petitioner, should have applied for representation to the estate of M. in whom the estate of R., though unadministered, vested as his sole heir and not for letters of administration *de bonis non* to the estate of R., H. appealed.

Held, that as the estate of R. had remained unadministered, the Petitioner who could have taken out the original grant was entitled to the grant of letters of administration *de bonis non* to his estate under s. 259 of Indian Succession Act.

Counsel appearing before the Court as *amicus curiae* does not appear as a matter of right and hence is not entitled to costs.

Adarji Mancherji Dalal, In re,⁽¹⁾ disapproved.

Facts material to this report are fully set out in the judgment.

Sir J. B. Kanga with *P. P. Khambatta*, for the appellant.

M. P. Amin, Advocate General, (*amicus curiae*) for the respondent.

* Appeal No. 115 of 1952: T. & I. J. Petition No. 307 of 1952.

⁽¹⁾ (1930) 55 Bom. 795 s. c. 33 Bom. L. R. 576.