A.V. REDDY TRUST AND ORS.

v.

COMMISSIONER OF WEALTH TAX

OCTOBER 8, 1999

[D.P. WADHWA AND M.B. SHAH, JJ.]

Wealth Tax Act, 1957—S.21(1), (2) and (4)—Trust—Wealth Tax—Levy of—Mode of Assessment—Determination of—Trusts created for the benefit of grand children and daughter—Settlor constituted as sole trustee—Trust deed creating contigent interest on beneficiaries in the corpus of Trust fund—Interest of beneficiaries indeterminate and unknown—Held, tax to be assessed on the beneficial interest of the trustee in representative capacity—Assessment not on the entire value of trust fund in the status of an individual—High Court justified in holding that the provisions of S.21(4) and not S.21(1) or (2) were applicable.

One 'A' created four trusts for the benefit of his three grand children and daughter and constituted himself as the sole trustee. The terms and conditions of the trust deed stipulated certain contingencies on fulfilment of which the beneficiaries' interest would come into existence. Settlor's wealth tax returns showing the entire value of assets of the trust was rejected by the wealth tax officer and assessments were made under S.16(3) of the Wealth Tax Act, 1957. On appeal, the Appellate Assistant Commissioner and Income Tax Appellate Tribunal held that only the value of the interest of the beneficiary in the Trust could be included in the net wealth and not the value of the corpus of the Trust itself. However, on reference the High Court held that the assessment was to be made under S.21(4) of the Act and the trustee was to be assessed on the entire value of the Trust fund in the status of an individual. Hence the present appeal.

On behalf of the appellants it was contended that wealth tax assessment was required to be made under the provisions of S.21(1) or 21(4) of the Act and the assessment was not to be made on the basis of the corpus of the trust fund but was to be made on the basis of the beneficiaries' interest.

Partly allowing the appeals, the Court

HELD : 1.1. High Court was justified in holding that the appellant trust is to be assessed to wealth tax under S.21(4) of the Wealth Tax Act, 1957. [588-E]

1.2. It is apparent from the terms and conditions of the trust deed that rights of the beneficiaries to get the corpus of the trust fund come into existence at the future date when the condition regarding the survival is fulfilled. The High Court, therefore, rightly arrived at the conclusion that interest of beneficiary is indeterminate or unknown and is contingent and, therefore, S.21(4) of the Act would be applicable. Consequently, the contention of the appellant that the trust should be assessed under S.21(1) of the Act cannot be accepted. [585-B-C]

2. High Court erred in holding that the trustee will have to be assessed on the entire value of the trust fund in the status of individual. Once it is held that assessment is to be made under S.21(4) of the Act, there is no question of assessing the wealth tax on the entire value of the trust fund. Under sub- section (1) or (4) of S.21 of the Act, it is beneficial interests which are taxable in the hands of the trustee in a representative capacity and the liability of the trustee cannot be greater than the aggregate liability of the beneficiaries and no part of corpus of the trust property can be assessed in the hands of the trustees under S.3 of the Act. [587-A; B; E; F]

Commissioner of Wealth Tax **v.** *Trustees of Nizam's Family Trust*, **(1977) 108 ITR 555, relied on.**

CIVIL APPELLATE JURISDICTION : Civil Appeal Nos. 6077-6080 of 1990.

From the Judgment and Order dated 3.12.87 of the Andhra Pradesh High Court in R.C. No. 37-40 of 1983.

K. Ram Kumar for the Appellants.

K.N. Shukla, G. Venkatesh Rao, Shankar Divate, S.K. Dwivedi for the Respondent.

The Judgment of the Court was delivered by

SHAH, J. These appeals are filed against the Common Judgment and Order dated 8th December, 1987 passed by the High Court of Andhra

A Pradesh in Referred Case Nos. 37-40 of 1983 in reference made to the High Court under Section 27 of the Wealth Tax Act, 1957. The Income-Tax Appellate Tribunal referred the following question for decision in all the four cases :-

B "Whether on the facts and in the circumstances of the case, the Tribunal was justified in holding that only the value of the interest of the beneficiary in the Trust could be included in the net Wealth and not the value of the corpus of the Trust itself."

The facts in brief are that one Sri A.V. Reddy of Kadiam in East C Godavari District created four trusts for the benefit of his three grand children and daughter. One trust was created for the benefit of his grandson Dexter Anand Sear (eldest son of his daughter, Margaret) and the relevant Trust Deed was executed on 14th March, 1972. Another Trust Deed was created on 3rd October, 1970 for the benefit of the Settlor's D grand-son, Harish Reddy. Third Trust Deed was created on 2nd October, 1970 for the benefit of the Settlor's grand-son. B.V. Satish Reddy and fourth Trust Deed was created on 6th July, 1971 for Settlor's second daughter Mrs. Lalitha Anderson. The trust deeds were similar; the author of the trust constituted himself as the sole trustee; he had the discretion to apply whole or any portion of the income for the beneficiary and accumu- E late the residue by investing; the Trust funds were to be transferred and made over to the beneficiary of the trust after completion of the age of 45 years in the case of his daughters and 25 years in the case of his grandsons; if the object of the trust cannot be fulfilled the trust property was to be applied for the children of the beneficiary or other children. The trusts F created by the Settlor are on uniform pattern, namely, at the time of settling the trust, a sum of Rs. 1,116 was settled with the provision to augment the trusts fund from time to time by further contributions. The Settlor appointed himself as the sole trustee during his lifetime. The trustee A.V. Reddy filed the Wealth-Tax returns for the four trusts showing the entire value of assets held by the trust for the purpose of Wealth Tax assessment. G On 27 March, 1980, the Wealth Tax Officer made assessments under Section 16(3) of the Wealth Tax Act.

Against those orders, assessee preferred the appeals before the Appellate Assistant Commissioner. In those appeals, the method of valua- H tion of the wealth tax was disputed; additional ground was raised by

contending that in view of Section 21 which applied to all trusts only interest of the beneficiary should be assessed to wealth tax and not the entire corpus of the trust fund. By order dated 29th November, 1980, the appeals were allowed. The appellate authorities directed the Wealth Tax Officer to assess the beneficial interest according to Section 21(1) or 21(2) of the Wealth Tax Act. Against that order, Wealth Tax Officer preferred appeals before the Income Tax Appellate Tribunal, Hyderabad (hereinafter referred to as "the Tribunal"). The Tribunal arrived at the conclusion that the corpus of the trust was to be transferred to the beneficiary on completing the stipulated age and the intention of the Settlor was to vest the corpus in the beneficiary only on reaching the stipulated age. The Tribunal, therefore, held that there was only a contingent interest in the corpus of the trust till the beneficiary attained the stipulated age and what could be included in the hands of the assessee would be the interest of beneficiaries in the terms of the trustee and not the corpus of the trust fund itself. The appeals were, therefore, dismissed with clarification with which we are not concerned.

A B C D

The High Court after considering the various contentions and the decision relied upon by the Counsel for the parties and the terms of the trust deed arrived at the conclusion that the fund is held by the trustee on behalf of and for the benefit of the beneficiary or the beneficiaries whose interest may come to surface at a future date depending upon the happening of the events provided in the trust deed; on the valuation dates under consideration, it was not possible to say that the trustee held the fund of the trust on behalf of or for the benefit of known beneficiaries and much less could it be said that the shares of the persons on whose behalf the trust fund is held were determinate and known. Hence, the wealth tax assessment is to be made under Section 21(4) of the Act; the trustee will have to be assessed on the entire value of the trust fund in the status of an individual. Thereafter, the Court upheld the assessment made by the Wealth Tax Officer subject to any relief in the quantum granted either by the Appellate Assistant Commissioner or by the Income-Tax Appellate Tribunal. That finding of the High Court is challenged in these appeals by special leave.

E F G

The learned Counsel for the appellants submitted that in these cases, wealth tax assessment is required to be made under Section 21(1) or 21(2). He further submitted that presuming that the High Court has rightly

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A arrived at the conclusion that assessment is to be made under Section 21(4) of the Act, yet it committed error in giving final direction contrary to the ratio laid down by this Court in the case of *Commissioner of Wealth Tax* v. *Trustees of Nizam's Family Trust,* (1977) 108 ITR 555. He submitted that once it is held that the trust was valid, the wealth tax assessment is required to be made under the provisions of Section 21(1) or 21(4) of the Wealth B Tax Act and, in such cases, the assessment is not to be made on the basis of the corpus of the trust fund but is to be made on the basis of the beneficiaries interest as discussed by this Court in detail in *Nizam's Family* Trust case.

C In our view, there is much substance in the contention raised by the learned Counsel for the appellant because after arriving at the conclusion to the effect that wealth tax assessment is required to be made under Section 21(4) of the Wealth Tax Act, the Court erroneously held that it is to be assessed on the entire value of the trust fund in the status of an individual and the said directions are contrary to the ratio laid down in D *Nizam's Family Trust* case (supra).

Regarding the contention of the learned counsel for the appellant that assessment is required to be made under Section 21(1) or 21(2), we would refer to the relevant terms of the Trust Deed on which the High E Court has relied upon. They are as under :-

> "18. The Trustee for the time being may at his discretion apply the whole or any portion of the income of the Trust Fund for the maintenance education or advancement in life of the Beneficiary and shall accumulate all the residue by investing the same in the F aforesaid manner.
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> 20. On the Beneficiary completing the age of 25 years the trustee shall transfer and make over to be beneficiary all the trust funds and on so transferring this Trust deed shall stand cancelled and G be of no effect.
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> 21. If the object for which the Trust has been created fails and cannot be fulfilled, the Trustee for the time being shall be at liberty to apply the trust property to the benefit of the other sons, H daughters of my last daughter Mrs. Margaret Anne Reddy Sear in

the proportion of one share for a son and half- share for a daughter." A

On the basis of the aforesaid terms and conditions, it is apparent that rights of the beneficiaries to get the corpus of the trust fund come into existence at the future date when the condition regarding the survival is fulfilled. The High Court, therefore, rightly arrived at the conclusion that interest of beneficiary is indeterminate or unknown and is contingent and, therefore, held that Section 21(4) would be applicable. In this view of the matter, there is no substance in the contention of the learned Counsel for the appellant that the trust should be assessed under Section 21(1) of the Wealth Tax Act. B C

Once it is held that assessment is to be made under Section 21(4), there is no question of assessing the wealth tax on the entire value of the trust fund. In such a situation, in the case of *Nizam's Family Trust* case (supra), this Court has laid down that two assessments are required to be made on the trustee; one in respect of actual valuation of the life interest of beneficiary under sub-Section (1) of Section 21 and the other in respect of actual valuation of the totality of the beneficial interest in remainder as if it belonged to one individual under sub-Section (4) of Section 21. Under sub-Section (1) or (4) of Section 21, it is beneficial interests which are taxable in the hands of the trustee in a representative capacity and the liability of the trustee cannot be greater than the aggregate liability of the beneficiaries and no part of corpus of the trust property can be assessed in the hands of the trustees under Section 3. D E

This aspect is considered in detail in the aforesaid decision. The Court first reproduced the relevant part of Section 21, as it stood at that time, as under : F

"21. *Assessment when assets are held by courts of wards, administrators-general, etc.* (1) Subject to the provisions of sub-Section (1A), *in the case of assets chargeable to tax under this Act, which are held* by a court of wards or an administrator-general or an official trustee or any receiver or manager or any other person, by whatever name called, appointed under any order of a court to manage property on behalf of another, or *any trustee appointed under a trust declared by a duly executed instrument in writing,* G H

whether testamentary or otherwise (including a trustee under a valid deed of wakf), the *wealth-tax shall be levied upon and recoverable* from the court of wards, administrator-general, official trustee, receiver, manager or trustee, as the case may be, *in the like manner and to the same extent as it would be leviable upon and recoverable* from the person on whose behalf (or for whose benefit) *the assets are held*, and the provisions of this Act shall apply accordingly.

(2) Nothing contained in sub-section (1) shall prevent either the direct assessment of the person on whose behalf (or for whose benefit) the assets above referred to are held, or the recovery from such person of the tax payable in respect of such assets.....

(3) .....

(4) Notwithstanding anything contained in the foregoing provisions of this section, where the shares of the persons on whose behalf or for whose benefit any such assets are held are indeterminate or unknown, the wealth-tax shall be levied upon and recovered from the court of wards, administrator-general, official trustee, receiver, manager or other person aforesaid, as the case may be, in the like manner and to the same extent as it would be leviable upon and recoverable from an individual who is a citizen of India and resident in India for the purposes of this Act, and :

(a) at the rates specified in Part I of the Schedule I; or

(b) at the rate of three per cent,

whichever course would be more beneficial to the revenue."

After considering the various contentions raised by the parties and exhaustively dealing with the provisions of the Wealth Tax Act, Court, *inter alia*, held thus :-

(a) Charging Section 3 of the Wealth Tax Act is made expressly subject to Section 21 and it must yield to that section insofar as the later makes a special provision for assessment of a trustee of a trust. Section 21 is mandatory in its terms.

(b) Once it is established that a trustee of a trust can be assessed only in accordance with the provisions of section 21 and under these provisions, it is only the beneficial interests which are taxed in the hands of the trustee, it must follow as a necessary corollary that no part of the value of the corpus in excess of the aggregate value of the beneficial interest can be brought to tax in the assessment of the trustee.

(c) Under the scheme of Section 21, the revenue has two modes of assessment available for assessing the interest of a beneficiary in the trust properties; it may either assess such interest in the hands of the trustee in a representative capacity under sub-section (1) or assess it directly in the hands of the beneficiary by including it in the net wealth of the beneficiary. What is important to note is that in either case what is taxed is the interest of the beneficiary in the trust properties and not the corpus of the trust properties. So also where beneficiaries are more than one, and their shares are indeterminate or unknown, the trustees would be assessable in respect of their total beneficial interest in the trust properties.

(d) Under sub-sections (1) and (4) of Section 21 it is the beneficial interests which are taxable in the hands of the trustee in a representative capacity and the liability of the trustee cannot be greater than the aggregate liability of the beneficiaries, no part of the corpus of the trust properties can be assessed in the hands of the trustee under Section 3 and any such assessment would be contrary to the plain mandatory provisions of Section 21.

(e) For making it clear as to how the wealth tax is to be computed, the Court gave an illustration for assessment under sub-Section (1) and (4) of Section 21. In a case where property is held on trust for giving income for life to A and on his death, to such of the children of A as the trustee might think fit. The Court held that section 21, sub-section (4), would be clearly attracted in such a case so far as the reversionary interest is concerned, because, on the relevant valuation date, the remaindermen and their shares would be indeterminate and

unknown. But here also two assessments would have to be made on the trustee - one in respect of the actuarial valuation of the life interest of A under sub-section (1) of Section 21 and the other in respect of the actuarial valuation of the totality of the beneficial interest in the remainder as if it belonged to one individual under sub-section (4) of Section 21. The difference between the value of the corpus of the trust property and the aggregate of the actuarial valuations of the life interest of A and the remainderman's interest would not be assessable in the hands of the trustee because, as pointed out above, the trustee can be taxed only in respect of the beneficial interests and there being no other beneficiary apart from A and such of the children of A as the trustee might think fit, the balance of the value of the corpus cannot be brought to tax in the hands of the trustee under sub-section (1) or (4) of Section 21.

(f) The correct interpretation of sub-section (4) of Section 21 must, therefore, be that even where the beneficiaries of the remainder are indeterminate or unknown, the trustee can be assessed to wealth-tax in respect of the totality of the beneficial interest in the remainder, treating the beneficiaries fictionally as an individual."

In view of the aforesaid discussion, we agree with the findings given by the High Court that in the case of appellant trust beneficial interest is to be assessed to wealth tax in the hands of the trustee under Section 21(4) of the Act. However, the direction given by the High Court that "trustee will have to be assessed on the entire value of the trust fund in the status of individual" is contrary to the direction given in *Nizam's* case.

In the result, the question is answered partly in favour of the assessee and against the Revenue. The appeals are is allowed with costs.

S.V.K. Appeal allowed.