

Decoding Family Settlements & Arrangements

Mar 14, 2023



Sachin Vasudeva

SCV & Co. LLP



Nehal Kumar

SCV & Co. LLP

Disputes amongst families is not uncommon and India has been witness to many such disputes and altercations between families. Starting from the Mahabharat to present times there have been a spate of family feuds which in some cases have been very bitter and acrimonious. A family arrangement is one of the oldest alternative dispute resolution mechanisms which is known to mankind. 'History' is a great teacher. Lord Krishna in the Mahabharat also proposed a family arrangement when 'He' presented a peace proposal before King Dhritrashtra as he could foresee the consequences if the arrangement that was proposed was not accepted. Any one of us today can don the mantle of Lord Krishna and be a trusted party to warring families. However, in order to do that we must first understand what does a family settlement mean and what are its tax implications. In this two part article the nuances of family settlements and arrangements and the tax consequences are being discussed.

The entire law on family arrangements is judge made law and therefore reference is made to important decisions in this article to explain the ingredients of a family arrangement.

Concept of a family arrangement

1. In **Maturi Pullaiah v Maturi Narasimham, AIR 1966 SC 1836**, the Hon'ble Apex Court explained that '*a family arrangement is an agreement between members of the same family, intended to be generally and reasonably for the benefit of the family either by compromising doubtful or disputed rights or by preserving the family property or the peace and security of the family by avoiding litigation or by saving its honour. The agreement may be implied from a long course of dealing, but it is more usual to embody or to effectuate the agreement in a deed to which the term 'family arrangement' is applied.*' The Court relying on the commentary in Halsbury's Law of England further enunciated certain principles which should be borne in mind in appreciating the scope of such family arrangement:

1. Family arrangements are governed by principles which are not applicable to dealings between strangers. The Court, when deciding the rights of parties under family arrangements or claims to upset such arrangements, considers what in the broadest view of the matter is most for the interest of families, and has regard to considerations which, in dealing with transactions between persons not members of the same family, would not be taken into account.
2. Matters which would be fatal to the validity of similar transactions between strangers are not objections to the binding effect of family arrangements.

2. In **Sahu Madho Das v Mukand Ram AIR 1955 SC 481** , the Court observed that *"It is well settled that a compromise or family arrangement is based on the assumption that there is an antecedent title of some sort in the parties and the agreement acknowledges and defines what that title is, each party relinquishing all claims to property other than that falling to his share and recognising the right of the others, as they had previously asserted it, to the portions allotted to them respectively. But, in our opinion, the principle can be carried further and so strongly do the Courts lean in favour of family arrangements that bring about harmony in a family and do justice to its various members and avoid, in anticipation, further disputes which might ruin them all, that we have no hesitation in taking the next step (fraud apart) and upholding an arrangement under which one set of members abandons all claims to all title and interest in all the properties in dispute and acknowledges that the sole and absolute title to all the properties resides in only one of their number (provided he or she had claimed the whole and made such an assertion of title) and are content to take such properties as are assigned to their shares as gifts pure and simple from him or her, or as a conveyance for consideration when consideration is present."*

3. In **Tek Bahadur Bhujil v. Debi Singh Bhujil, AIR 1966 SC 292** the Apex Court held that *"It is well settled that a compromise or family arrangement is based on the assumption that there is an antecedent title of some sort in the parties and the agreement acknowledges and defines what that title is, each party relinquishing all claims to property other than that falling to his share and recognizing the right of the others, as they had previously asserted it, to the portions allotted to them respectively. That explains why no conveyance is required in these cases to pass the title from the one in whom it resides to the person receiving it under the family arrangement. It is assumed that the title claimed by the person receiving the property under the arrangement had always resided in him or her so far as the property falling to his or her share is concerned and therefore no conveyance is necessary."*

The Court further held that *"these observations do not mean that some title must exist as a fact in the persons entering into a family arrangement. They simply mean that it is to be assumed that the parties to the arrangement had an antecedent title of some sort and that the agreement clinches and defines what that title is. Similar assumption can be made in the present case even on the basis that the property was purchased with the moneys of the mother. How they got some antecedent title in the property is not for us to determine. The plaintiff (respondent No. 1) alleged that the property belonged to the family. The appellant did not allege that it could not have belonged to the family as it was purchased with the moneys of the mother but claimed that it was his self-acquired property. In the circumstances, it can be assumed that the parties recognized the existence of such antecedent title to the parties to the property as was recognized by them under the family arrangement. It is not so much an actually existing right as a claim to such a right that matters."*

4. In **Kale and Ors v Deputy Director of Consolidation 1976 AIR SC 48 1**, the Court held that *"by virtue of a family settlement or arrangement members of a family descending from a common ancestor or a near relation seek to sink their differences and disputes, settle and resolve their conflicting claims or disputed titles once for all in order to buy peace of mind and bring about complete harmony and goodwill in the family. The family arrangements are governed by a special equity peculiar to themselves and would be enforced if honestly made."*

The Hon'ble Court also held that *for the purposes of a family arrangement, the term 'family' has to be understood in a wider sense so as to include within its fold not only close relations or legal heirs but even those persons who may have some sort of antecedent title, a semblance of a claim or even if they have a spes successionis so that future disputes are sealed for ever and the family instead of fighting claims inter-se and wasting money, time and energy on such fruitless or futile litigation is able to devote its attention on more constructive work in the larger interest of the country.*

The Court also noted that *the members who may be parties to the family arrangement must have some antecedent title, claim or interest even a possible claim in the property which is acknowledged by the parties to the settlement. Even if one of the parties to the settlement has no title but under the arrangement the other party relinquishes all its claims or titles in favour of such a person and acknowledges him to be the sole owner, then the antecedent title must be assumed and the family arrangement will be upheld, and the Courts will find no difficulty in giving assent to the same. Even if bona fide disputes, present or possible, which may not involve legal claims are settled by a bona fide family arrangement which is fair and equitable the family arrangement is final and binding on the parties*

to the settlement.”

5. In **Ram Charan Das v Girija Nandini Devi** [\[TS-5025-SC-1965-O\]](#), the Hon'ble Court while discussing the principles of a family arrangement held that “it will be, therefore, seen that, in the first place, there must be an agreement amongst the various members of the family intended to be generally and reasonably for the benefit of the family. Secondly, the agreement should be with the object either of compromising doubtful or disputed rights, or for preserving the family property, or the peace and security of the family by avoiding litigation or for saving its honour. Thirdly, being an agreement, there is consideration for the same, the consideration being the expectation that such an agreement or settlement will result in establishing or ensuring amity and good-will amongst the relations”

The principles enshrined above can be summarized as under:

1. A family arrangement is an agreement between members of the same family intended to be generally and reasonably for the benefit of the family either by compromising doubtful or disputed rights or by preserving the family property by avoiding litigation.
2. A compromise or arrangement is based on the assumption that there is an antecedent title of some sort in the parties
3. In a family arrangement there is neither an alienation of property nor an exchange of property. The differences of parties having competing titles are resolved through a compromise and therefore the arrangement might not require compulsory registration.
4. Family arrangements are governed by a special equity peculiar to themselves and will be enforced if honestly made.
5. The term 'family' has to be understood in a wider sense so as to include within its fold not only close relations or legal heirs but even those persons who may have some sort of antecedent title or a semblance of a claim.
6. Courts would make every attempt to sustain a family arrangement rather than to avoid it having regard to the broadest consideration of family peace and security.
7. A family arrangement may be oral.
8. It is not necessary that there must exist a dispute actual or possible in the future, in respect of each and every item of property and amongst all members arrayed one against the other. The settlement should be a bona fide one so as to resolve family disputes and rival claims by a fair and equitable division of allotment of properties between various members of the family.

Type of properties that can be covered

An analysis of the case laws gives an understanding that the properties that can be covered under a family arrangement are typically ancestral properties on which there are multiple claims to ownership. It may be noted though, that it is not a pre-requisite that a family arrangement should only cover ancestral properties.

Whether Registration is required

A very important issue in family arrangements is whether the document needs to be registered under the Registration Act or not. As explained hereinabove, the whole law on this subject is case-law made, therefore the answer to the said question is also found in decided cases.

In a family arrangement more often than not there are multiple claims to the properties involved and pursuant to the family arrangement the parties relinquish all claims to property other than that falling to their individual share and recognizing the right of the others, as they had previously asserted it, to the portions allotted to them respectively. On account of the said reason and in such cases, no registration is required. However, if a person has an absolute title to the property and the said property is transferred to another person then it would be a case of transfer requiring registration.

Another important aspect which needs to be borne in mind is that a family arrangement may be oral and therefore in such a case no registration would be required. Registration would still not be required if the arrangement is reduced to writing in a memoranda format wherein the arrangement that has already been orally made is put on a document to facilitate mutation of properties. On the contrary, if from the terms of the written document it can be discerned that the said document itself creates an interest in an

immovable property then the same would require compulsory registration under the Act.

Definition of a family

In **Krishna Bihari Lal v Gulabchand, AIR 1971 SC 1041** the Apex Court held that the word 'family' has a wider meaning. It cannot be confined to a group of persons who by law has the right of succession. Accordingly, in a family arrangement, the word family is to be seen in a wider context and would not get restricted to the immediate family. It would extend to first cousins as well.

Can Company be a part of the family arrangement

The Bombay High Court in the case of **B.A. Mohota Textile Traders (P.) Ltd v Dy CIT [TS-5420-HC-2017(BOMBAY)-O]** held that a company cannot be a part of the family arrangement as it denied lifting the corporate veil. The facts of

the case were that the assessee, was a private limited company. Over 80% of its share capital was owned by a family referred to as three groups A, B and C (for convenient purposes). The family also had joint interest in various other limited companies and partnership firms apart from family owned immovable properties owned jointly. As disputes arose between these 3 groups, with a view to settle the differences between them and to restore family peace and harmony the dispute was referred to a sole arbitrator by an agreement dated 15-1-1994. The arbitration award was rendered on 30-4-1994 in the form of a family settlement and the said award became decree of the Court dated 7-11-1994. As per the terms of the award amongst other things, the assessee-company was allotted to Group B and other companies in the group were allotted to Groups A and C. As a result of this settlement, members of Group B who acquired control of the assessee-company required the assessee-company to transfer shares hitherto held by it in the companies now allotted as a result of the arbitration award to members of other Groups A and C at a certain agreed consideration.

The question that arose before the HC was whether assessee-company was liable to capital gains tax as a result of transfer of shares done in pursuance of family arrangement/settlement. The High Court, observed, though there was no dispute that family arrangement/settlement would not amount to transfer - the fact which was not disputed by any of the three lower authorities, yet the family arrangement/settlement would bind only parties to the dispute and the assessee-company, being a stranger to such family arrangement/settlement, would be outside the ambit of such family arrangement/settlement.

A Company therefore does not fit in the definition of the family and would not be a part of the family settlement. It may however be noted that individuals holding shares in companies can be a part of the family settlement where they relinquish their rights in such shares.

Conclusion

A family arrangement is a very effective alternate dispute mechanism the validity of which has been recognised by the Hon'ble Apex Court multiple times. It is much faster than proceedings in a civil court and it is recommended that families take this route for settlement of their disputes.