

CHAPTER XIV

ESTATE DUTY

The levy of an estate duty in India was recommended by the Taxation Enquiry Committee of 1924-25, but constitutional and other difficulties stood in the way of the introduction of this form of taxation.

Position under Constitution of India The constitutional position is now clarified by the inclusion of items 87 and 88 in the Union List in the Seventh Schedule to the Constitution of India, under which estate duty in respect of property other than agricultural land and duties in respect of succession to property other than agricultural land come within the exclusive legislative jurisdiction of Parliament. At the same time, the net proceeds of the duty (except for that accruing in Part C States) do not form part of the Consolidated Fund of India, but are, under Article 269 of the Constitution, to be distributed among the States within which duty is leviable. Estate duty and succession duty on agricultural land are within the legal competence of State Legislatures (items 47 and 48 of the State List in the Seventh Schedule). Under Article 252 of the Constitution, however, Parliament can legislate on these subjects if the Legislatures of two or more States pass resolutions to that effect; after such legislation is enacted, it can be extended to other States by a resolution adopted by the Legislatures of those States.

2. Another difficulty had been caused by the peculiar features of the Hindu joint family system. In view of this, the succession duty form of the levy, which bases liability on the amounts inherited by various persons and their degree of relationship to the deceased person, was considered unsuitable for adoption in India. It was, therefore, decided to go in for estate duty, which bases liability on the total value of the estate left by the deceased. Special legal provisions have also had to be made to cover the levy of the duty on coparcenary interests under the Hindu law.

Estate Duty Act, 1953 : main provisions 3. The Estate Duty Act was passed in 1953, and imposes a duty on property passing or deemed to pass on the death of a person, on or after the 15th October 1953. Property deemed to pass on death includes property which the deceased at the time of his death was competent to dispose of, and property in which the deceased or any other person had an interest ceasing on the former's death. Certain exceptions have been provided to this general rule. If the deceased was domiciled in India at the time of his death, the duty is leviable on all immovable property situated in India, and on all movable property (situated in India or outside) which passes on his death. If the deceased was domiciled outside India, the duty is leviable on all immovable property situated in India, all movable property situated in India and movable property situated outside India if it is settled property and the settler was domiciled in India at the time the settlement took effect. The *situs* of movable property of various kinds is determined by rules framed under the Act.

4. All property passing on the death of a person, subject to certain minor exceptions, is to be aggregated to form one estate. Agricultural land situated in eleven Part A and Part B States, whose Legislatures have agreed to central legislation, will form part of the estate subject to duty. Agricultural land situated in other Part A and Part B States is not subject to duty, but its value is to be taken into account for determining the rate of duty leviable on other property.

5. An important provision is that, on the death of a member of a Hindu coparcenary aged over eighteen years or less than eighteen years and with none of his lineal ancestors as a member of the coparcenary, who belongs to the Mitakshara, Marumakkatayam or Aliyasantana school, the share of the family property to which he would have been entitled if partition had taken place just before his death will be treated as property passing on his death. Different limits of exemption are prescribed for portions of the estate consisting of coparcenary property and of the rest of the deceased's estate.

6. The value of an estate is the market value of the properties comprising it, as at the time of death. From the value so determined, certain exclusions and abatements are permissible. Deductions are also permissible, subject to certain limitations, on account of reasonable funeral expenses and for debts and encumbrances.

7. The Act contains various provisions to counteract attempts at legal avoidance. One set of provisions is that gifts made 'in contemplation of death' (*donatio mortis causa*) as defined in the Indian Succession Act, are to be treated as passing on death. Gifts *inter vivos* for public charitable purposes made within a period of six months before the death, and gifts for other purposes made within two years before death takes place, are also to be treated as passing on death. Such gifts, however, will be exempt from duty up to a maximum of Rs. 2,500 in the case of gifts for charitable purposes and of Rs. 1,500 in the case of other gifts.

8. Another important set of provisions is to the effect that, where the deceased had transferred any property to a controlled company and had derived any benefits from it, a part of the assets of the company will be deemed to be property passing on his death, in the same proportion as the benefits derived by him on the last three accounting years of the company bear to the income of the company in those years. A controlled company is defined as one in which the public are not substantially interested and which has at any relevant time been under the control of not more than five persons, or which is not the subsidiary of a public company.

9. The first Rs. 50,000 of property consisting of a coparcenary interest in joint Hindu families of the Mitakshara etc., schools, and the first Rs. 1,00,000 of other chargeable property is exempt from charge. The balance is chargeable at progressive rates under the 'slab system' which rise from five per cent. on the slab from Rs. 50,000 to one lakh for joint family property, and seven and a half per cent. on the first Rs. 50,000 above Rs. one lakh in all cases, to 40 per cent. on the excess over Rs. 50 lakhs.

10. The administration of the estate duty has been vested in the Central Board of Revenue and in the officers of the Income-tax

Department. Assessments are to be made by the departmental officers, and all appeals lie to the Central Board of Revenue. At this stage, questions involving valuation of assets of various kinds are to be referred to Valuers chosen from a panel appointed by the Central Board of Revenue. References on questions of law can be made to the High Courts and the Supreme Court.

11. In view of the short experience of the working of estate duty, witnesses have generally refrained from suggesting any significant changes either in its structure or in the rates. They have, however, raised some points of principle in response to our questionnaire which we discuss below.

12. It has been suggested to us that the exemption limit is too high, particularly as compared to other countries where estate duty is levied, and also in relation to the *per capita* national income in this country. We are given to understand that the exemption limit has been fixed deliberately at the relatively high figure of Rs. one lakh for the present, in order to ensure that the volume of assessment and collection work that will require to be handled in connection with this new tax in the first few years of its introduction will not be much more than the relatively small staff, which has only very recently been recruited, and is still in the process of training, can effectively cope with. This strikes us as a good enough reason for hastening slowly in this matter, though we would suggest that the feasibility of reducing the exemption limit should be kept in mind by Government and all possible efforts made to increase the strength of the staff and to improve its quality, as early as practicable.

13. We also appreciate the relevance of the argument put forward by the Central Board of Revenue that in case the exemption limit is reduced very drastically—say, to Rs. 25,000 or some such figure—the cost of collection will become disproportionately high. Another point deserves notice. An amendment was introduced during the second reading of the Bill in the Parliament for the exclusion of residential houses in computing the principal value of the estate, but this was opposed by Government on the ground that the exemption limit was high enough to include the value of a residential house. If the exemption limit is now lowered appreciably, the question of excluding certain items like this will also have to be considered. We believe that, on the whole, it would be advisable to put off such changes till after more experience has been gained of the working of the new tax.

14. On all these grounds, we are of opinion that the exemption limit may be left for the present at Rs. one lakh. It may be of interest to note, in this connection, that the exemption limit in the United Kingdom has been increased steadily, over a period of years, from £2,000 to £3,000 in 1954-55.

15. Certain interests have suggested that investments in new industrial undertakings should be excluded from the principal value of the estate of a deceased, the concession being confined to investments in certain industrial units selected by Government. The justification for this suggestion is that the exemption of such shares from estate duty would act as an incentive for investment in new industries and would also incidentally prevent their being unloaded on the

market to the detriment of the industry concerned, for the purposes of payment of estate duty. We are alive to the question of incentives to productive efforts and we have already dealt with this question in its relevant context in relation to the structure of income-tax. We think it is not necessary at this stage to use estate duty as an instrument for the purposes of affording incentives to risk capital.

16. Section 84(1) of the Estate Duty Act has been criticised by certain foreign interests. It imposes a liability on the company in respect of the estate of a person who was not domiciled in India, but who possessed at the time of his death shares in a company which was not incorporated in India but which was resident in India for two out of the last three completed income-tax assessments. In view of the difficulty of recovering estate duty in such cases from the persons concerned, it has been provided in section 84 that the tax should be recovered from the company itself at a fixed rate which is *nil* if the value of the shares does not exceed Rs. 5,000 and seven and a half per cent. if it exceeds that figure. It is stated that the provision is inequitable inasmuch as it imposes a vicarious liability on the company and it will adversely affect the inflow of foreign capital into India.

17. The provision has been justified on the ground that it is not inequitable to place a charge on the company if its profits are largely derived from this country. In its ultimate effect, the charge will be borne by the whole body of the shareholders who are the beneficiaries of the profits made by the company. We agree with this view. The charge placed on the value of such shares is small and would not be a great burden on the current or accumulated profits of a company.

18. For the same reason, we consider that the effect of the estate duty on the inflow of foreign capital is exaggerated. More drastic provisions of this nature exist in other underdeveloped countries, e.g., Ceylon.

19. We would, however, draw attention to the proposal that we have made in Chapter II regarding the deletion from the law of the test for determining the 'residence' of companies based on their income arising in India. In view of the change recommended, the criterion used for the charge under section 84(1) of the Estate Duty Act will have to be reviewed.

20. The introduction of a tax on gifts has also been suggested by some witnesses as a means of preventing the evasion of death duties and incidentally also of income-tax. The present provisions regarding the taxation of gifts may be recounted briefly. All gifts *inter vivos* made within two years of the death of a person are chargeable to estate duty. Gifts for public charitable purposes are taxable if they are made within six months of the death of a person. In both cases, an exemption has been provided upto a maximum limit under section 33 of the Estate Duty Act. Gifts made otherwise than under the above conditions are not chargeable to estate duty. The suggestion now made is that a small charge should be placed on such gifts as and when they are made. The analogy for this purpose is provided by the gift tax in vogue in many countries, including the U.S.A.

21. A gift tax is theoretically an attractive proposition, but it requires considerable experience of the operation of estate duty before it can be introduced. One of the pre-requisites for operating successfully a tax of this nature would be to introduce the submission by income-tax assesseees of a statement of assets and liabilities. As more experience is gained of this type of work, the feasibility of introducing a gift tax can be considered. Moreover, the rates of death duty are at present low. The value of a gift tax as a second line of defence for estate duty is greater if the rates of the latter are steeply progressive. We are, therefore, not in favour of introducing the gift tax at this stage.

22. Another demand that has been placed before us is that an **Appellate Tribunal** independent Appellate Tribunal should be set up to hear appeals against the decisions of the Estate Duty Controller. According to this view, appeals should not lie to the Central Board of Revenue but to an independent body. Those who have put forward this claim point out that under the Income-tax Act the judicial and executive functions of the Commissioners have been bifurcated and an independent Tribunal has been provided for. A similar arrangement can be made for estate duty administration also, it is argued. Government's point of view has been that, during the initial years of the working of the Act, the executive should have adequate powers and that, later on, if the need for a Tribunal is felt, its establishment could be considered. Some witnesses are of the view that if provision is made for an appeal to the Tribunal instead of to the Central Board of Revenue, it would encourage disputes arising out of points of fact to be taken up to the Tribunal, from the very commencement of the Act, and that this will lead to lack of uniformity in interpretation. As the Estate Duty Act is a highly technical and complicated piece of legislation, we see considerable advantages in retaining the appellate powers with the Central Board of Revenue for the time being.

23. The question as to how the duty should be collected has also been raised, and it has been suggested that **Payment of duty** immovable property and shares and securities should be accepted in payment of dues. This, it is argued, would remove possible cases of hardship when the estate left by the deceased has inadequate liquid resources. Government can also collect the dues easily. It is further stated that, in the U.K., immovable property is accepted for payment and that a similar course should be adopted in India also.

24. The official point of view is that Government need money for development and that if company shares of fluctuating value or fixed assets not capable of easy disposal were given to them, it would only add to their worries. Although under the U.K. Act payment of duty in the form of immovable property is permitted, the provision is resorted to only in exceptional cases.

25. Section 70 of the Estate Duty Act empowers the Controller to allow payment to be postponed for such period, to such extent and on payment of interest at a rate not exceeding four per cent. or any higher interest yielded by the property as he may think fit. It is also provided that estate duty in respect of immovable property may, at the option of the person accountable, be paid in eight equal yearly

instalments or sixteen equal half-yearly instalments with interest at the rate of four per cent. per annum or higher. The Finance Minister has given an assurance that, in actual working, cases of hardship would be very sympathetically dealt with, and we have no doubt that this assurance will be carried out in practice.

26. It remains for us now to consider whether any change should be effected in the scheme of the estate duty and the rates at which it is levied. We have already pointed out that the Indian estate duty makes no distinction between acquired and inherited property, nor does it draw any distinction on the basis of the consanguinity of the inheritor. There is also no provision for the levy of succession duties. Moreover, the minimum value of property exempted from the duty is much higher than in other countries, while the rates of duty charged on the estates liable to tax are uniformly lower than in most of the other countries. Thus, the exemption limit is Rs. one lakh in India as against £3,000 in the U.K., Rs. 20,000 in Ceylon, and the equivalent of Rs. 30,000 in Australia. As regards rates, at Rs. one lakh level, the Indian rate would be nil, while it is 3 per cent. in the U.K., 2.6 per cent. in Australia, 1.3 per cent. in Canada, 7.3 per cent. in Sweden, and 29.3 per cent. in Japan. At Rs. ten lakhs level, the Indian rate works out at 15.25 per cent. as against 40 per cent. in the U.K., 16.9 per cent. in U.S.A., 20.6 per cent. in Australia, 14.2 per cent. in Canada, 32.7 per cent. in Sweden, and 56.8 per cent. in Japan. Indian rates are lower than foreign rates for almost every bracket. And the rate on the highest slab is 40 per cent. in India as against a 'step' rate of 80 per cent. in the U.K. Moreover, many of the recommendations we have made for the continued promotion of capital formation such as non-taxation of bonus shares, development rebate, tax holiday under section 15C of the Income-tax Act, etc., may lead, as a consequence, to the growth of savings and investments among individual tax-payers or the accumulation of undistributed profits and the issue of bonus shares in the private corporate sector and should, therefore, call for suitable action through the tax system to check the widening of inequalities in wealth. There seems to be, from this point of view, a case for recommending changes both in the system and in the rates of the estate duty with a view to making it a more effective instrument for lessening both the range and the magnitude of inequality of wealth in the country.

27. Three main objections are advanced against this view, *viz.*,

- (1) it will act as a disincentive to saving and therefore to investment and capital formation;
- (2) as the difficulties of collection increase with increasing rates, the danger of business units being broken up with consequent adverse effects on efficiency will also increase, a contingency particularly undesirable in a country in such urgent need of economic development as India;
- (3) as estate duty has just been introduced, the administration has hardly had the time to acquire experience of, or work out, suitable ways of dealing with the various problems it gives rise to in respect of both assessment and collection.

28. We are not impressed by the first argument. Although, taken by itself, the estate duty might have a certain effect on savings, this effect should be smaller than that of a tax on personal incomes yielding the same revenue. In fact, foreign experience has shown that death duties have had hardly any adverse effect on the volume of personal savings, for the reason, among others, that where savings are not involuntary in the sense of being a residual element they are the result of motives which are not adversely affected by taxation of the estate after death. We do not, therefore, accept as valid the contention that any increase in the rates of estate duties in India will have adverse effects on the volume of savings and investment.

29. Estate duty has an important role in the Indian fiscal system not only from the standpoint of revenue but also as an instrument for reducing inequalities in wealth; and we are certain that it will have to undergo changes in the direction of making it more progressive than it is at the moment. The point is whether the present time is opportune for this purpose. We are impressed by the fact that the duty has come into force only recently and the administration is not yet acquainted with the types of problems that are likely to arise in its administration. We would, therefore, recommend that, as more experience is gained, the rates should be reviewed for the purposes of increasing them. The only change that we would recommend for very early consideration is that the period before death during which gifts *inter vivos* become liable to estate duty should be increased from two years as prescribed at present to five years. This would bring the Indian legislation into line with that of some other countries, and also close more effectively than at present one of the admitted loopholes in the operation of estate duty, especially since our law does not provide for a separate gift tax.