

(2002) 08 MAD CK 0010

In the Madras High Court

Case No : T. C. No's. 1189 and 1190 of 1991 19 August 2002

INDIRA PHADKE (DECD.)

APPELLANT

Vs

TYPEWRITER and OFFICE APPLIANCES INDIA (P) LTD.

RESPONDENT

Date of Decision : 19-08-2002

Acts Referred:

Citation : (2002) 258 ITR 524

Hon'ble Judges : R. Jayasimha Babu, J;K.P. Sivasubramaniam, J

Bench : Full Bench

Advocate : C.V. Rajan, T. Ravikumar,, for the appearing parties;

Judgement

R. Jayasimha Babu, J.

This matter arises under the Estate Duty Act. The question referred for consideration at the instance of the assessee is, "whether, on the facts and circumstances of the case, the Appellate Tribunal was right in holding that there has been transfer attracting application of section 17 of the Estate Duty Act, 1953 ?

The deceased G.A. Phadke died on 26-5-1973. He was the managing director of Typewriter and Office Appliances India Private Limited which was a controlled company. While assessing his estate to duty under the Estate Duty Act, the assessing authority invoked section 17 of the Act and added a part of the value of the company to his estate by treating the remuneration of the deceased, the dividend received by him for three years, and other benefits received by him, such as commission and perquisites for three years, as benefits accruing to the deceased in that period, the accrual of which benefits resulted in the assets of the company determined in accordance with the other portions of section 17 being includible in

his estate.

That view of the assessing authority was upheld in appeal by the appellate authority as also by the Tribunal.

There is no finding by any of the authorities in these proceedings that the deceased Phadke had transferred any property to the company at any

point of time. In order to support the assessment made, what was relied upon was the Rules framed under the Estate Duty Act, more particularly,

a definition of "disposition" in rule 2(6) and the contents of rules 4 and 5 of the Estate Duty (Controlled Companies) Rules, 1953. Rule 4 deems

that a transfer of property for the purposes of section 17 is made if the property comes to be included in the resources of the company by the

effect of a disposition made by the person or with his consent or any associated operations of which such a disposition formed one. "Disposition" is

defined in rule 2(6), inter alia as including "any trust, covenant, agreement or arrangement, whether made by a single operation or by associated

operations". Rule 5 deems the income mentioned in sub-clauses (1)(a), (b) and (c) as the benefits accruing to the deceased from the company.

They include any periodical payment made to the deceased out of resources or at the instance of the company.

Rule 5 which deals with the benefits accruing to the deceased can be invoked only when and after it is found that there is transfer of property by

the deceased to the controlled company. Absent such a transfer, the mere accrual of the benefits to the deceased will not attract application of

section 17. Though section 17 does not define "transfer" an expanded meaning has been ascribed to that term by rule 4 which equates "disposition

with "transfer" and this disposition in turn is defined in broad terms by rule 2(6) of the Estate Duty (Controlled Companies) Rules. Nevertheless a

pre-condition for attracting section 17 is a transfer. As there is no transfer of property to the controlled company more particularly, of benefits due

to the deceased from the company no part of the value of assets of that company can be included in the estate of the deceased.

To ascertain the true scope of section 17, it is instructive to peruse the explanatory notes attached to the Estate Duty Bill, 1952 (Bill No. 92 of

1952). Section 17 of the Act is clause 17 of that Bill. That clause in the Bill which later became the section in that Act is based upon section 42 of

the U.K. Finance Act, 1940, and section 36 of the U.K. Finance Act, 1944. The necessity for the provisions contained in sub-sections (1), (2)

and (3) of section 17 are illustrated in the example given in the Notes on Clauses appended to the Estate Duty Bill, and which example reads thus :

A is the owner of an estate worth Rs. 12 lakhs including a residential house, and of stocks and shares worth Rs. 8 lakhs. He forms a company

with a nominal capital of Rs. 20 lakhs divided into 50,000 five per cent preference shares and 1,50,000 ordinary shares, all of Rs. 10 each. He

sells the estate and the securities to the company in consideration for the shares of which 50,000 ordinary shares are allotted to him and the rest to

his wife and children. As part of the arrangement, he is appointed governing director for life at a salary of Rs. 50,000 per year and the residential

house, whose annual value is Rs. 5,000, is let to him as governing director at a rent of Rs. 1,000 per year. On A's death more than two years

later, estate duty would, but for the provisions of this section, be payable only in respect of the 50,000 shares which he retained. There was no gift

to the company for the company gave full consideration. The only gift was a gift of the shares to his wife and children and that gift was not the

subject to any reservation. But, according to this provision, the estate duty payable would be not on the market value of 50,000 ordinary shares

but on such proportion of the assets of the company, as the aggregate amount of benefits accruing to the deceased for the three years ending with

his death bear to the income of the company for the same three years. Thus, if the income of the company for the last three years were Rs. 3 lakhs,

and the dividend declared on ordinary shares is Rs. 90,000, then the benefits enjoyed by the deceased are:

Rs.

Salary as governing director 1,50,000

Residential house less rent paid 12,000

Dividend 30,000

1,92,000

The assets which would be deemed to pass on his death would be of the value of

192

of 20 lakhs

or of Rs. 12,80,000 and not of Rs. 5 lakhs only.

The object of section 17 was to prevent evasion of duty by individuals owning valuable property divesting themselves of such properties and

transferring it to a company which was controlled by such persons, or their nominees and even thereafter continued to retain control over the

property so transferred, and enjoy the benefits therefrom. The section clearly was not intended to treat the fruit of labour of any individual who by

floating the company and contributing his skill and labour as a director or as other officer of the company received remuneration for the services

rendered by him to such company, as exigible to estate duty. Mere delay in drawal of the remuneration would not have the effect of his transferring

to the company the undrawn salary thereby attracting the mischief of section 17.

Here all that is stated by the assessing authority is that the deceased had become the managing director of a controlled company and had drawn

remuneration, perquisites and benefits therefrom. That by itself will not attract section 17 of the Estate Duty Act. Moreover, the accountable

person had in the return treated the balance of the credit amount of the deceased which represented undrawn remuneration and value of the

perquisites due to him, as forming part of his estate and thus being exigible to levy of estate duty. There can be no doubt that monies owing and

due to the assessee from the company of which he had been the managing director would form part of the estate, and the accountable person had

rightly included the balance in their current account, in the estate duty return.

The liability for the payment of estate duty in the circumstances was limited to the amount in so far as that amount was due to the deceased from

the company and there was no scope for invoking section 17 of the Act.

Learned counsel for the revenue sought to support the order of the Tribunal by placing reliance on the decision of this court in the case of

Controller of Estate Duty, Madras Vs. Lakshmi Saraswathi Textiles (Arni) (P) Ltd. and Another, . The court there was concerned with a case

where the deceased had deposited a substantial sum of monies with a controlled company and had been drawing interest therefrom. It was held by

the court that the deposit so made by the deceased with the company resulted in a transfer of the monies to the company, as the monies after such

deposit became part of the resources of the company. The court, on those facts, held that section 17 had been rightly invoked.

Here, it is not the case of the assessing authority that the deceased had deposited any of his monies with the company. All that the deceased had

done was to form a company; build up its net worth by contributing his own skill and labour for which he received remuneration from the company.

The delay on the part of the deceased in drawing the remuneration and other perquisites to which he was entitled, cannot, in the circumstances, be

regarded as a transfer by him of the undrawn salary and benefits to the company which would render a part of the assets of the company includible

in his estate. In fact, the deceased had drawn most of the monies which had become due to him by way of remuneration and value of perquisites,

prior to his death. The amount that was found due from his current account in the company was only Rs. 28,277.

The order of the Tribunal, therefore, cannot be sustained. The question referred to us is answered in favour of the assessee and against the

revenue. The assessee shall be entitled to costs in the sum of Rs. 1,500.

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