
(1967) 12 KL CK 0012

In the High Court Of Kerala

Case No : Income-tax Referred Cases No's. 19 of 1966 and 89 of 1967

P. Gangadharan Pillai

APPELLANT

Vs

Controller of Estate Duty, Ernakulam

RESPONDENT

Date of Decision : 01-12-1967

Acts Referred:

Estate Duty Act, 1953 — Section 10, 3, 64, 9

Citation : (1968) 70 ITR 640

Hon'ble Judges : Isaac, J

Bench : Single Bench

Judgement

Isaac, J.—These two reference arise out of an order passed by the Central Board of Revenue on April 16, 1960, in Estate Duty Appeal No. KL 28; and they relate to the assessment of estate duty under the Estate Duty Act, 1953 (hereinafter referred to as the Act) on the property passing on the death of one Sri Parameswaran Pillai of Quilon, who died on May 13, 1956. The applicant in these references is one of the accountable persons. He delivered to the Assistant Controller of Estate Duty, Ernakulam, a statement of account of all the properties in respect of which the estate duty is payable, showing a total value of Rs. 2,04,861. After scrutiny of the statement, and giving the accountable persons due opportunity of being heard in the matter, the Assistant Controller determined the principal value of the estate at Rs. 9,16,321, and the estate duty payable thereon at Rs. 1,33,560.

2. The controversy before the Assistant Controller related only to the following matters :

(i) The deceased, Parameswaran Pillai, had purchased a land more than two years prior to his death in the name of his wife. He had also constructed a house in the said land, wherein he was living with his wife, and children till he died. It was contended that the above land and building belonged absolutely to the wife of the deceased as a gift, which was made more than two years prior to his death, and that the value of this property should be, therefore, be treated as

part of the property passing on the death of the deceased.

(ii) Sri Parameswaran Pillai was carrying on a business in cashew and tobacco. On December 29, 1954, which is within two years of his death, he executed a deed of settlement in respect of certain immovable properties, and the assets and liabilities of the above business together with its goodwill in favour of his sons. According to the applicant, the business was then running at a loss and the value of its assets was a negative figure. It was only after the donees had invested their own moneys, expended their skill and effort in running the business and ploughing back the accrued profits into the business, that the business flourished, and the balance-sheet of the subsequent year showed a positive value for the assets. It was, therefore, contended that these assets should not be valued, as they stood at the time of the death, but only as they stood on the date of the settlement. In other words, the additions brought to the business by the donees should be excluded from the valuation; and

(iii) the business of the deceased had no goodwill, as it was being run at a loss; and there was no scope for assessing any value for its alleged goodwill.

3. The Assistant Controller rejected all the above contentions. The applicant, therefore, filed an appeal before the Central Board of Revenue, who was then the appellate authority, and pressed the same contentions before it. The Central Board upheld the order of the Assistant Controller, except with regard to the value of the goodwill of the business. It held that the value of the goodwill of the cashew business was nil, as against Rs. 1,25,955 fixed by the Assistant Controller. As regards the value of the goodwill of the tobacco business, the sum of Rs. 69,831 fixed by the Assistant Controller was reduced to Rs. 50,000. Being dissatisfied with the order of the Central Board, the applicant moved u/s 64 of the Act by an application dated 6th June, 1960, to refer the following questions of law said to arise out of the said order for decision by this court :

1. Whether, on the facts and in the circumstances of the case, the Central Board of Direct Taxes was right in holding that the bona fide possession and enjoyment of the property gifted was not immediately assumed by the donee and thenceforward retained to the entire exclusion of the donor ?

2. Whether, on the facts and circumstances of the case, the Central Board of Direct Taxes was justified in including the profits of the business carried on exclusively by the donees with their own monies and the augmented value of the assets, the augmentation being due to the exercise of the skill and efforts of the donees, in the value of the assets said to pass on the death of Sri Parameswaran Pillai ?

3. Whether the Central Board of Direct Taxes was justified in taking into consideration also the profits of business conducted exclusively by the appellants in computing the value of the goodwill of the business which was gifted long ago before the death of Sri Parameswaran Pillai ?

4. Whether, on the facts and circumstances of the case, the method of computation adopted by the Central Board to Direct Taxes for computing the value of the goodwill is justified in law ?

5. Whether, in any view of the matter, the Central Board of Direct Taxes should not have taken the profits from the two main items of business together in computing the profits for ascertaining the goodwill ?

4. The Central Board of Direct Taxes, New Delhi, considered the application; and it held by its order dated December 16, 1965, that only the following three questions of law arose out of its order for decision by the High Court :

1. Whether, on the facts and in the circumstances of the case, the house property at Q. M. C. No. 200 in Thamarakulam Ward, Quilon, standing in the name of the wife of the deceased was correctly included in the estate of the deceased as property deemed to pass on his death u/s 10 of the Act ?

2. Whether, on the facts and in the circumstances of the case, for the purpose of inclusion in the estate, the properties covered by the settlement dated December 29, 1954 (including the goodwill) should have been valued as on the date of death as has been done by the Board or as on the date of the settlement as was contended by the applicant ?

3. Whether, on the facts and in the circumstance of the case, for the purpose of including in the estate the property covered by the settlement dated December 29, 1954, the profits of the business subsequent to the date of the settlement which had been ploughed back into the business was properly taken into account by the Board ?

5. Accordingly, the above three questions were referred to this court by the Central Board by its letter dated February 7, 1966, u/s 64(1) of the Act, as it stood prior to the Estate Duty (Amendment) Act, 1958, along with statement of the case. This reference is I. T. R. No. 19 of 1966.

6. The applicant did not agree to the statement of the case; and he also claimed that more questions of law arose out of the order of the Central Board for reference. Hence, he filed O. P. No. 2087 of 1966 in this court u/s 64(3) of the Act to direct the Central Board to refer the following four questions of law arose out of the order of the Central Board to refer the following four questions of law also, for the opinion of this court :

(1) Whether, on the facts and circumstances of the case, the Central Board was justified in including the profits of the business carried on exclusively by the donees with their own monies and the augmented value of the assets, the augmentation being due to the exercise of the skill and efforts of the donees, in the value of the assets said to pass on the death of Sri Parameswaran Pillai.

(2) Whether the Central Board was justified in taking into consideration also the profits of business conducted exclusively by the appellant in computing the value

of the goodwill of the business which was gifted long ago before the death of Sri Parameswaran Pillai.

(3) Whether, on the facts and circumstances of the case, the method of computation adopted by the Central Board of Direct Taxes for computing the value of the goodwill is justified in law.

(4) Whether, in any view of the matter, the Central Board of Direct Taxes should not have taken the profits from the two main items of business together in computing the profits for ascertaining the goodwill.

7. The above O. P. was allowed. Accordingly, the Central Board, by its letter dated October 23, 1967, referred these four questions also to this court, along with a statement of the case. This reference is I. T. R. No. 89 of 1967. We shall now proceed to give our decision on the questions referred in these two references.

8. Question No. 1 in I. T. R. No. 19 of 1966 : It is not disputed that the property consisting of the land and the house therein, which is the subject-matter of this question, became the property of the wife of Sri Parameswaran Pillai more than two years before his death, pursuant to the gift made by him. It is also admitted that the deceased was living with his wife and children in the said property can be deemed to be property passing on the death of Sri Parameswaran Pillai, depends on the application of section 10 of the Act. This section reads as follows :

Gifts whenever made where donor not entirely excluded. -Property taken under any gift, whenever made, shall be deemed to pass on the donors death to the extent that bona fide possession and enjoyment of it was not immediately assumed by the donee and thenceforward retained to the entire exclusion of the donor or of any benefit to him by contract or otherwise :

Provided that the property shall not be deemed to pass by reason only that it was not, as from the date of the gift, exclusively retained as aforesaid, if, by means of the surrender of the reserved benefit or otherwise, it is subsequently enjoyed to the entire exclusion of the donor or of any benefit to him for at least two years before the death.

9. The Supreme Court had occasion to construe the above section in a recent decision in *George Da Costa v. Controller of Estate Duty*. The question in that case was whether a house gifted by a deceased person to his sons four years prior to this death can be deemed to be property passing on his death, if he continued to live with his sons in the said house after the gift. The court answered the question in the affirmative; and in doing so, it said :

The crux of the section lies in two parts : (1) the donee must bona fide have assumed possession and enjoyment of the property, which is the subject-matter of the gift, to the exclusion of the donor, immediately upon the gift, and (2) the donee must have retained such possession and enjoyment of the property to the entire exclusion of the donor or of any benefit to him, by contract or otherwise.

As a matter of construction we are of opinion that both these conditions are cumulative. Unless each of these conditions is satisfied, the property would be liable to estate duty u/s 10 of the Act.

10. The court further observed :

As a matter of construction we hold that the words by contract or otherwise, in the second limb of the section will not control the words, to the entire exclusion of the donor in the first limb. In other words, in order to attract the section, it is not necessary that the possession of the donor of the gift must be referable to some contractual or other arrangement enforceable in law or in equity. Even if the donor is content to rely upon the mere final affection of his sons with a view to enable him to continue to reside in the house, it cannot be said that he was entirely excluded from possession and enjoyment within the meaning of the first limb of the section, and, therefore, the property will be deemed to have passed on the death of the donor and will be subject to levy of estate duty.

11. In the light of this decision, question No. 1 in I. T. R. No. 19 has to be answered in the affirmative; and that is should be so fairly conceded by the learned counsel for the applicant. We may, in this context, note that section 10 of the Act has been amended by section 69 of the Finance Act, 1965, by adding the following proviso to section 10 :

Provided further that a house or part thereof taken under any gift made to the spouse, son daughter, brother or sister, shall not be deemed to pass on the donor's death by reason only of the residence therein on the donor except where a right of residence therein is reserved or secured directly or indirectly to the donor under the relevant disposition or under any collateral disposition;;

12. As a result of this amendment, the property of a spouse, son, daughter, brother or sister obtained by gift shall not be deemed to be property passing on the death of the donor on account of the mere fact that the donor resided therein along with the donee.

13. Question No. 2 in I. T. R. No. 19 of 1966 :- The applicants learned counsel submitted that his client had never contended that the properties covered by the deed of settlement, and which should be deemed to pass on the death of the deceased u/s 10 of the Act, should be valued as on the date of the deed of settlement. He submitted that there was no dispute that the principal value of the property shall be estimated to be the price which, in the opinion of the Controller, it should fetch if sold in the open market at the time of the death of the deceased, and that the above question did not arise out of the order of the Central Board. We are inclined to agree with the learned counsel; and hence we decline to answer this question.

14. Question No. 3 in I. T. R. No. 19 of 1966 and question No. 1 I. T. R. No. 89 of 1967 :- We shall deal with these two questions together, as we feel that they relate to the same subject-matter, and they are also substantially the same. The

subject-matter is the value of the property covered by the deed of settlement dated December 29, 1954. There is no dispute that, as the deed was executed within two years of the death of Sri Parameswaran Pillai, the property shall be deemed to pass to the donees on the donor's death. There is also no dispute, as we pointed out earlier, that its value has to be determined as on the date of death of the donor. The applicant's case throughout has been that what the donees brought in or added to the property, which they got under the settlement, should not be treated as property passing on the death of the donor. That this was his case is clear from the following passage appearing in paragraph 7 of the order of the Central Board of Revenue, out of which there reference arise.

The appellants' advocate did not dispute the inclusion of the property in the estate. His only contention related to the valuation of the property. The learned advocate stated that as on the date of the settlement, the value of the assets covered by the settlement was only a negative figure and it was only after the donees had invested their own moneys, expended their skill and effort in running the business and ploughing back the accrued profits into the business, the business had flourished and the balance-sheet of the subsequent year showed a positive value for the assets. He contended that the Assistant Controller was not entitled to take into account the balance-sheet of the subsequent year, viz., 1956, as the basis of the valuation of the assets. According to him, the valuation of the property should be made on the basis of the position obtaining as on the date of the settlement, viz., the 29th December, 1954.

15. The order of the Central Board shows that it did not grasp the above contention; and it held that the value of the property should be the value as on the date of death. The point raised on the aforesaid two questions is the same; and both these questions seek an answer to the contention which the applicant raised before the Central Board, as stated in the passage quoted above from its order.

16. Question No. 3 in I. T. R. No. 19 assumes that the business made profits after the settlement of December 29, 1954, in favour of the donees. Question No. 1 in I. T. R. No. 89 assumes more things, namely, the donees carried on the business after the settlement exclusively with their own monies and argued that the value of the assets, the argumentation was due to the exercise of the skill and effort of the donees, and the donees thereby made profits. This is all the difference between the two questions. In the statement of the case submitted in I. T. R. No. 19, the Central Board stated, among other things :

Although it was urged in the grounds of appeal before the Board that only after the donees had invested their own moneys and expended their skill and effort in running the business and ploughed back the profits accrued in the business, the business flourished and the balance-sheet showed a net surplus, no material was placed before the Board to enable it to disagree from the finding of the Assistant Controller that even at the time of settlement, for the purpose of the settlement itself, the business was taken at a positive figure which could only be if goodwill

was attached to the business and such goodwill was not included in the assets in the balance-sheet. No specific material was also placed before the board in support of the contention that the goodwill of the business had increased between the date of settlement and the date of death of the deceased. There has, therefore, been no finding by the Board either to the effect that there was an augmentation of assets of the business between the date of settlement and the date of death of the deceased, or to the effect that, such augmentation, if any, was the result of any special efforts on the part of the donees and was not the result of other circumstances like better trade conditions.

17. The applicant objected before the Central Board to the inclusion of the above passage in the statement of the case, on the ground that what is stated therein was contrary to facts, and he also referred to the various items of materials, which he pleased before the Assistant Controller. But the Central Board paid no heed to the objection. On this Court, he filed C. M. P. No. 10766 of 1967, paying that the Central Board may be required to submit by him in the objection. We consider that this is unnecessary; and we, therefore, dismiss the above C. M. P.

18. We are constrained to observe that the passage extracted above from the statement of the case submitted by the Central Board is wrong and unwarranted. If no material was placed before the Board, as it now states, in support of the applicants contention that "the doneed had invested their own moneys and expended their skill and effort in running the business" etc., the Central Board should have held so. This would have concluded the matter. But this is not the basis on which the Board or the Assistant controller disposed of the above contention. Both these authorities assumed that the facts, on the basis of which the said contention was advanced, were correct, but the contention was not legally sustainable. The reference in I. T. R. No. 89 of 1967, was made as per order of this court in O. P. No. 2087 of 1967, after hearing the counsel for the revenue. Question No. 1 in this reference would not stand, if this court was not satisfied that it arises out of the order of the Central Board. The said question can arises only on the facts assumed therein. It is not, therefore, now open to the Central Board to say in the statement of the case that the applicant did not place any materials before it to establish the said facts. From the statement of the case, and the papers annexed thereto, it is evident that there was no dispute that the value of the assets covered by the settlement was only a negative figure, and that it was only after the donees had invested their own moneys, expended their skill and effort in running the business, it flourished, and its balance-sheet showed a positive value; but the Central Board did not consider any these facts relevant to the determination of the value of the property passed under the deed of settlement on the date of the death of the donor. A question of law raised by an assessee, but failed to be dealt with by the Tribunal is a question which arise out of the order of the Tribunal. See the decision of the Supreme Court in Commissioner of Income Tax v. Scindia Steam Navigation Co. Ltd. Hence we cannot entertain the objection now raised by the Central Board to the reference of the above question to this court.

19. The controversy involved in the above two questions is whether the property, which the donees got under the settlement, should be valued as it stood on the date of settlement, or as it stood on the date of death as a result of the augmentation made by the donees with their own moneys and ferts. This controversy realities mainly, if not wholly, to the valuation of the business. There is no dispute that the value should be determined as on the date of the death; but the dispute is which is the property to be valued. The learned counsel for the revenue contended that it is the business as a whole that was donated under the deed of settlement, that the business continued the same, and that it should be valued as it stood at the time of the death, irrespective of the fact, whether it was augmented by the donees or not. Counsel for both parties relied on section 9 of the Act in support of their respective contentions. The learned counsel for the revenue also invited our attention to section 3(3) of the Act. These sections read as follows :

3. (3) For the avoidance of doubt, it is hereby declared that references in this Act property passing on the death of a person shall be construed as including reference to property deemed to pass on the death of such person.

9. Gifts within a certain period before death. - (1) Property under a disposition made by the deceased purporting to operate as an immediate gift inter vivos whether by way of transfer, delivery, declaration of trust, settlement upon person in succession, or otherwise, which shall not have been bona fide made two years or more before the death of the deceased shall be deemed to pass on the death :

Provided that in the case of gift made for public charitable purposes the period shall be six months.

(2) The provisions of sub-section (1) shall not apply to -

(a) gifts made in consideration of marriage, subject to a maximum of rupees ten thousand in value;

(b) gifts which are proved to the satisfaction of the Controller to have been part of the normal expenditure of the deceased, subject to a maximum of rupees ten thousand in value.

20. We do not think the above provisions render any assistance to the contention of the counsel for the revenue. If A donated to B property P, and the donee added to it property Q during the lifetime of A what B has got at the time of the death of A is property P+Q though, what he got under the gift is only property P. If A died within two years of the gift, the property obtained by B thereunder shall be deemed, u/s 9 of the Act, to pass on the death of A, and not on the date of the gift. But we find no warranty for the contention, in the language of any of the above statutory provisions, that what would be deemed to pass is not only property P, but it would be P+Q. The contention on the face of it is extraordinary. The learned counsel, however, sought support for the above contention on the following passage appearing at page 90 of Greens Death Duties, third edition :

In general the property which is deemed to pass is the settled property as it stands at the death, notwithstanding that the investment may have been varied, and including any capital accretions.

21. The learned author has not referred to any authority in support of the above proposition. But he proceeds to say that there is some doubt whether this rule applies to a gift money, and refers to the decision of the Court of Appeal in *In re Payne : Poplett v. Attorney-General*. The provisions of the English statute on estate duty seem to be same as those contained in the Act in respect of this matter. But the English law on the subject has been authoritatively settled by the House of Lords in their decision in *Sneddon v. Lord Advocate*. The facts of that case were the following : On December 19, 1946, one W. G. Netherington executed a deed of trust, settling Pounds 5,000 for the benefit of his daughter. The trustees were given wide powers of investment. On December 21, 1946, they invested the amount in shares in Creamola (England) Ltd. The trustee died on February 5, 1948; and thus he did not live for a period of five years after the execution of the deed of trust and the payment of the amount. The value of the shares on the date of death of the trustee was agreed at Pounds 9,250. The question was whether the property deemed to pass on the death of the deceased was Pounds 5,000 or Pounds 9,250. The law Lords, by a majority of three against one, held that it was Pounds 5,000, which alone the deceased gave to his daughter. We shall quote the following passage appearing in the speech of Lord Morton of Henryton, which if we may say so with respect, highlights the reasoning for the majority decision :

No one doubts that the trustee made a disposition which comes within the section and that estate duty is payable upon certain property which is deemed to pass upon his death, but the question is : what is the property which is deemed to pass; is it the Pounds 5,000 or is it the trust fund constituted by the deed of trust, in its state of investment at the death of the trustee, i.e., the Creamola shares ? It is common ground that Pounds 9,250 was the value of the Creamola shares at the trustees death. Thus no question as to value or as to the proper method of valuation arises in the present case.

What, then, is the property which is deemed to pass ? The statute says it is the property taken under the disposition made by the truster. My Lords, I feel no doubt that the property taken under that disposition was the sum of Pounds 5,000. That was the only property which passed from the truster, and it was the only property taken by the trustees from the truster under his disposition. They took that property, of course, as trustees for the beneficiaries under the deed of trust. The truster never owned the Pounds 5,000 Creamola shares and therefore, these shares could not be taken under any disposition made by him. As soon as the trustees received the Pounds 5,000 it became in their hands a trust fund to be held on the trusts declared by the deed of trust, and it was, of course, proper for the trustees to invest that sum in some one or more of the numerous investments authorised by the trust deed. They invested it in the Cremola

shares, but they did not take these shares under the disposition made by the trustor; they took the shares because, in the exercise of their discretion, they decided to apply for them and because the company decided to allot them to the trustees.

22. Referring to the decision in *In re Payne : Populate v. Attorney-General*, His Lordship said that, in his view, it was wrongly decided. The two other law Lords, who agreed with his decision, also doubted the correctness of the decision in *In re Payne*. It has, therefore, to be said that the passage relied on by the learned counsel from *Greens Death Duties*, does not state the correct law on the subject.

23. In the light of the above pronouncement of the House of Lords, it is unnecessary to refer to more decisions of the English courts on this question. *Dymonds Death Duties*, fourteenth edition, at page 296, and *Halsburys Laws of England*, third edition, volume 15 at page 18, also refer to the above decision of the House of Lords as laying down the correct law. There is a learned and detailed discussion of this question at pages 295 to 299 in *Dymonds Death Duties*. Apparently, there is no decision of our Supreme Court, or any Indian High Court on this question. Our reading of the relevant provisions of the Act is in complete agreement with the decision of the House of Lords in *Sneddons case*. We, therefore hold that, as regards the property covered by the settlement dated December 29, 1954, the property deemed to pass on the death of deceased is only the property as it stood on the date of the settlement, and that only the value of the said property as on the date of the death, without taking into account the augmentations or additions made thereto by the donees with their own moneys and efforts, can be included in the principal value of the estate for the purpose of assessment under the Act. What would be that value is a matter for determination by the appropriate authority under the Act. Accordingly, we answer question No. 3 in I. T. R. No. 19 of 1966 and question No. in I. T. R. No. 89 of 1967 in favour of the applicant, and against the Controller of Estate Duty.

24. Question Nos. 2, 3 and 4 in I. T. R. No. 89 of 1967. -These three question relate to the valuation of the goodwill of the business, which deceased Sri Parameshwaran Pillai settled in favour of his sons along with other properties, as per deed of settlement dated December 29, 1954. The learned counsel for the applicant submitted at the hearing that the was not pressing these question. It is, therefore, unnecessary to consider them, and we decline to answer these three questions.

25. In the result, we answer question No. 1 in I. T. R. No. 19 of 1966 in the affirmative, and against the applicant; question No. 3 I. T. R. No. 19 of 1966 and question No. 1 in I. T. R. No. 89 of 1967 in the manner stated in paragraph 13 of this judgment, and in favour of the applicant. We decline to answer the remaining questions referred in these two cases, for the reasons herein above stated. In the circumstances of the case, we direct the parties to bear their own costs. A copy of this judgment under the seal of this court and the signature of the Registrar shall be sent to the Central Board of Direct Taxes, New Delhi, as

required by section 64(7) of the Act as it stood before its amendment by the Estate Duty (Amendment) Act, 1958.