PETITIONER:
P. MADHUSUDHAN REDDY (DEAD) BY LRS.

Vs.

RESPONDENT:
THE CONTROLLER OF ESTATE DUTY

DATE OF JUDGMENT: 20/07/1998

BENCH:
SUJATA V. MANOHAR, D.P. WADHWA

ACT:

HEADNOTE:

JUDGMENT:

J U D G M E N T

Mrs. Sujata V. Manohar, J.

These appeals arise out of the estate duty proceedings in respect of the estate of the deceased P. Madhusudhan Reddy. During his lifetime the deceased had taken out three life insurance policies of Rs. 50,000/- each. Two policies were from the phoenix Assurance Company, Bombay and one policy was taken from the Standard Life Insurance Company, Calcutta. During his lifetime the deceased had obtained loans on the security of his tow life insurance policies taken out from Phoenix Assurance Company, Bombay. It seems that the total loan amount was Rs. 78,400/- . the deceased had also, from time to time, repaid a part of the loan. The amount due in respect of the loans so taken at the time of the death of the deceased was Rs. 71,260/-.

During his lifetime on or about 29th of August, 1954 the deceased executed an assignment in respect of each of these three life insurance policies in favour of his grand children. the deeds of assignment have been registered on 27.9.1954. A notice of the assignment was given to the insurance company in accordance with the provisions of Section 38 of the Insurance Act, 1938 and the assignments were registered with the Insurance Companies.

The Deceased made a will dated 4.2.1959 in respect of all his properties. In his will, in the list of properties he mentioned, at item no. 30, as follows:-

> " There are three Policies of Life Insurance, as detailed below of Rs. 50,000/- each, which are already assigned in favour of my six grandsons and a grand daughter (i.e. the sons and daughter of my two sons). 1. The Standard Life Insurance Co., Fifty thousand. 2. The Phoenix Assurance Co., two policies of Fifty thousand each."

In the will, he also mentioned in the list of dues, payment of dues to insurance companies amounting to Rs. 71,250/-. Under his will he provided that after his death the amount of his three life insurance policies, that is to say, Rs.

1,50,000/- plus bonuses that will be received thereon, should be distributed equally among his surviving six grandsons and grand daughter in whose favour he had already assigned irrevocably and transferred the policies. He also provided that the dues of the insurance companies (inter alia) should be paid out of the general estate.

In the estate duty proceedings the Assistant controller of Estate Duty initially treated the three policies as a separate estate for the purpose of calculation of the rate of estate duty. In appeal, before the appellate Tribunal held that each of the three policies should be separately assessed to estate duty. However, after reopening the assessments the Assistant Controller of Estate Duty treated the three policies as a part of the main estate of the deceased and levied estate duty accordingly. In the several proceedings which took place dealing with the initial assessment as well as the reopening of the assessment, the Appellate tribunal ultimately held that the two insurance policies taken out from Phoenix Insurance Company formed a part of the general estate of the deceased while the third policy constituted a separate estate. The Appellate Tribunal, however, rectified its order as a mistake and ultimately held that all the three policies formed a part of the general estate of the deceased and could not be separately assessed.

In respect of these various proceedings, depending on the view then taken, three sets of questions were framed by the Tribunal and referred to the High court in three reference applications which arose from these proceedings. The three sets of questions are as follows:-

" Set No. 1.:

1. Whether on the facts and in the circumstances of the case, the Appellate Tribunal was justified in law in holding that there should be separate assessments in respect of each of the three insurance policy amounts assigned by the deceased in favour of his grand-children (At the instance of the Revenue).
2. Whether the loan amount of Rs. 78,400/- taken on the insurance policies by the deceased is liable to be deducted as a debt under section 44 of the Estate Duty Act from the General estate as distinct from the separate estate of the three insurance policies; and
3. Whether the estate duty payable is liable to be deducted while computing the net estate exigible to duty?

(At the instance of the accountable person).

Set No. 2:

1. Whether on the facts and in the circumstances of the case, the Tribunal has acted within its jurisdiction in allowing the department's appeal and revering its earlier order passed on 27.10.77.
2. Whether on the facts and in the circumstances of the case, the Tribunal was justified in holding

that the amount of Rs.1,39,284/- in respect of Standard Life Assurance co. policy was to be included in the main estate of the deceased under Section 34(3) of the Estate Duty Act.

3. Whether on the facts and circumstance of the case, the Tribunal was correct in law in holding that Section 34(3) of the Act was not applicable.

Set No. 3:

1. Whether on the facts and in the circumstances of the case, the Tribunal was correct in holding that the Assistant Controller could reopen the assessment under section 59(b) of the Estate Duty Act?

2. If the answer to the first question No. 1 is in the affirmative, whether the two insurance policies could be assessed as separate estates under Section 34(3) of the Act?"

The High Court by its impugned judgement (reported in 156 ITR 45) has upheld the ultimate finding of the Tribunal that the three insurance policies have to be considered as a part of the general estate of the deceased and they cannot be aggregated individually or collectively to form a separate estate or estates for the purposes of calculating the rate of estate duty. The three sets of questions were accordingly answered in favour of the revenue. The High Court also upheld the exercise of power in the present case by the Assistant Controller of Estate Duty in reopening the assessment and it also upheld the exercise of power by the Tribunal for rectifying the mistake.

The present appeals are filed from the above impugned judgment of the High Court. Before us, the question relating to the exercise of power by the Assistant Controller of Estate Duty for reopening the assessments as also the question relating to the power of the Tribunal exercised in the present case to rectify the mistake, have not been pressed.

In the first set of questions, question no. 3 has been correctly answered by the High Court against the assessee in view of two decisions of this Court, one in the case of p. Leelavathamma v. Controller of Estate Duty (188 ITR 803) and other in the case of Nawab Mir Barkat Ali Khan Bahadur v. Controller of Estate of Duty (222 ITR 612).

The remaining questions deal with two issues; 1) whether after the assignment of the three insurance policies by the deceased in favour of his grandchildren, it could be said that the deceased had any interest in the life insurance policies which passed on his death; and 2) if the three insurance policies are held to pass on the death of the deceased whether (i) each of the three insurance policies should be separately assessed to estate duty or (ii) the three insurance policies taken together should be separately assessed to estate duty of (iii) whether the three insurance policies have to be aggregated with the main estate of the deceased for the purposes of estate duty.

Under Section 2(15) of the Estate Duty Act, 1953, "property" includes any interest in property movable or immovable, and also includes, inter alia, any property converted from one species into another by any method. The

Explanations to Section 2(15) are not relevant for our purposes. Section 2(16) defines "property passing on death". It includes property passing either immediately on death or after an interval; and he phrase "on death" includes "at a period ascertainable only by reference to the death". Learned counsel for the appellants contended before us that in view of the assignments of the life insurance policies by the deceased during his lifetime to his grandchildren, it cannot be said that the deceased had any interest in the life insurance policies which could pass on his death. Hence under Section 34 of the Estate Duty Act, 1953, the life insurance policies cannot be treated as property passing on the death of the deceased.

He drew our attention to Section 38 of the insurance Act, 1938. Section 38(1) provides that a transfer or assignment of a policy of life insurance can be made only by an endorsement upon the policy or by a separate instrument in the manner provided there. In sub-section (2) it is provided that the transfer and assignment shall be complete and effectual upon the executions of such endorsement or instrument in the manner provided but shall not be operative as against an insurer and shall not confer upon the transferee or assignee or his legal representatives any right to sue for the amount of such policy until a notice in writing of the transfer or assignment and either the said endorsement or instrument itself or a certified copy thereof have been delivered to the insurer. Under sub-section (5), subject to the terms and conditions of the assignment, the insurer shall, from the date of the receipt of the notice referred to in sub-section (2) , recognise the transferee or assignee named in the notice as the only person entitled to benefit under the policy, such person shall be subject to all liabilities and equities to which the transferor or assignor was subject on the date of the transfer or assignment. Since the deceased had duly assigned the policies in accordance with the provisions of Section 38 and by complying with all its requirements, the assignee alone, it is contended, had an interest in these policies at the time of the death of the deceased. Hence no interest was left in the deceased in respect of these policies which passed on his death.

In considering this contention, one must bear in mind Section 14(1) of the Estate Duty Act, 1953. It provides as follows:

> " 14(1): Money received under a policy of insurance effected by any person on his life, where the policy is wholly kept up by him for the benefit of a donee, whether nominee or assignee, or a part of such money in proportion to the premiums paid, by him, where the policy is partially kept up by him for such benefit, shall be deemed to pass on the death of the assured.
>
> Explanation. - A policy of insurance on the life of a deceased person effected by virtue or in consequence of a settlement made by the deceased shall be treated as having been effected by the deceased."

The remaining part of Section 14 is not relevant for the present purpose. By virtue of Section 14(1) money under a

life insurance policy which is kept up by the donee for the benefit of his nominee or assignee is deemed to pass on the death of assured. This is a clear deeming provision whereby even after the assignment of his policy by the assured, if the assured keeps up the policy for the benefit of his assignee, the insurance policy will constitute a part of the estate of the deceased.

From the statements of Case which are before us in the three references, as also the facts found, the assignees have not contended that after the assignment of the policies in their favour, the assignees paid the premium or any part of the premium on the policies so assigned or the assignees kept the policies alive. The policies were entirely under the control of the deceased. The deceased had taken loans and repaid loans or parts thereof on these insurance policies. From the tenor of the will it is apparent that it was the deceased who had retained possession of the policies and had kept them up during his life time even after the assignment. The provisions of Section 14 are, therefore, directly attracted in the present case.

The contention of the appellants that the deceased did not have any interest in the insurance policies passing on his death must, therefore be rejected in the light of Section 14. Learned counsel for the appellants drew our attention to a decision of the Madras High Court in D. Mohanavelu Mudaliar and Anr. V. Indian Insurance and Banking Corporation Ltd., Salem and Anr. (AIR 1957 Mad. 115). The Madras High Court, however, was not concerned with the question whether on assignment of a life insurance policy by the insurer during his life time, the insurer had any interest left in the life insurance policy which could pass on his death under the provisions of the Estate Duty Act, 1953. The Court was concerned with the effect of assignment and whether a creditor of the insurer could attach the policy which was already assigned. The provision so of the Estate Duty Act are not considered in the judgment.

The appellants also drew our attention to two decisions of this Court dealing with accident policies. One is a decision in the case of M. CT. Muthiah and Anr. V. Controller of Estate Duty, Madras (161 ITR 768) and the other is the decision in the case of Bharat Kumar Manilal Dalal v. Controller of Estate Duty, Gujarat (164 ITR 231). In the former case, the deceased , prior to flying by air, took out a personal accident policy under which the insurance company agreed that if, any time during the currency of the policy, the deceased should sustain an accident resulting in any injury of injuries leading to death, the insurance company would pay to the assured or to his legal representatives in the case of his death, such sum as was specified. The deceased effected a nomination in favour of M. The deceased died following the crash of the airline in which he was travelling. On his death, the insurance company paid the nominee M a sum of Rs. 2 lakhs which was the benefit stipulated to be paid. The question was whether the sum of Rs. 2 lakhs should be included in the estate of the deceased as property passing on the death of the deceased for the purposes of state duty. This court held that the insurance amount became property only on the death of the deceased in an accident during the subsistence of the policy. During the life time of the deceased interest was vested totally and irrevocably in the hands of the nominee. The death did not cause the property to change hands. Therefore, the sum of Rs. 2 lakhs was not includible in the principal value of the estate of the deceased for the purpose of estate duty. This Court also observed that though

it was not necessary to decide the point , had it become necessary to decide, it would have held that the sum of Rs. 2 lakhs was a separate estate from the other estate of the deceased. The same view has been taken by this Court in the subsequent case of Bharat Kumar Manilal Dalal (supra). Both these cases deal with policies of accident insurance where the amount became payable only on the death of the insurer in an accident. In such a situation, there was no question of any amount ever coming to the deceased, the amount under the policy being payable only to a nominee on insurer's death in an accident.

These cases cannot apply to the present case which deals with assignments of life insurance policies. In view of the express provisions of Section 14, the deceased must be considered to have an interest in these policies passing on his death for the purposes of estate duty.

In the case of Controller of Estate Duty v. Bomansha Framji Cama and Ors. (170 ITR 600), the Bombay High Court held that the provisions of Section 14(1) were attracted in a case where the deceased had settled on trust five policies of insurance on his life, when the premiums on the said policies after their assignment under the settlement, were paid by the deceased. The policies became fully paid up during the life time of the deceased On his death, the moneys received by his assignees were held to be property passing on the death of the deceased by virtue of Section 14(1). The Court said that the words] "kept up" mean that the policy has been and is kept valid by payment of premiums by the donee and is not allowed to lapse. In the case of a paid up policy, no further payment of premium is required to prevent it from lapsing. The past payments of premium kept the policy valid and such a policy must be considered as having been kept up by the assured for the purpose of Section 14.

Therefore, the contention of the learned counsel for the appellants that the policies do not form part of the estate of the deceased must be rejected.

Under Section 34 of the Estate Duty Act, 1953, for the purpose of determining the rate of estate duty to be paid on any property passing on the death of the deceased the properties specified in subsection (1) and (2) shall be aggregated as provided therein. Sub-section (3) of Section 34, however, provides as follows:

> " 34(3): Notwithstanding anything contained in sub-section (1) or sub-section (2) any property passing in which the deceased never had an interest, not being a right or debt or benefit that is treated as property by virtue of the Explanations to clause (15) of section 2, shall not be aggregated with any property, but shall be an estate by itself, and the estate duty shall be levied at the rate or rates applicable in respect of the principal value thereof."

It is, therefore, contended by learned counsel for the appellants that even if the life insurance policies constitute a part of the estate of the deceased, they should be separately assessed under section 34(3). Now, only such property passing on the death of the deceased in which the deceased "never had an interest" will constitute a separate estate under Section 34(3) for the purpose of determining the rate of estate duty. What is meant by the phrase "in

which deceased never had an interest"? The language of Section 34(3) is similar to the language of Section 4 of the English Finance Act of 1894 as amended by the Finance Act of 1990. Section 4 of the Finance Act, 1894 is as follows:

> " For determining the rate of estate duty to be paid on any property passing on the death of the deceased, all properties so passing in respect of which estate duty is leviable shall be aggregated so as to form one estate, and the duty shall be levied at the proper graduated rate on the principal value thereof:
> Provided that any property so passing in which the deceased never had an interest ..... shall not be aggregated with any other property, but shall be an estate by itself and the estate duty shall be levied at the proper graduate rate on the principal value thereof ..... "

In the case of Attorney General v. Pearson and Ors. (1924 (2) K. B. 375) the English court considered a case where the settlor had assigned to trustees a policy of assurance on his wife, reserving interest for himself until marriage, and thereafter to hold the moneys payable under the policy in trust to pay the income thereof to his wife during her life time and after the decease of the settlor and his wife, in trust for the children of the marriage as therein mentioned and if there is no child of the marriage, for the settlor absolutely. The court, inter alia, considered whether the money under the policy should be aggregated with the other estate of the deceased under Section 4 determining the rate of estate duty. The court asked, (page 388) "Had the deceased even an interest within the meaning of the Act in the moneys which were to become payable under the policy"? The court answered, one could not hold that the deceased never had an interest in this property. "On the contrary he had an interest in the policies before he settled them. Moreover after he settled them he had an interest in the benefit which was going to accrue or arise from them on his death, though it may have been a remote interest which he never could enjoy in possession. He had an interest during all his married life contingently upon the failure of the trusts in favour of his wife and children. If his wife and children had predeceased him the legal position would have altered, but his interest would then have become a very proximate and extremely valuable interest, and he would have died worth the capital value of the insurance money". Of course, on the facts of that case since the settlor had reserved to himself an interest in the eventuality of the failure of the trust in favour of his wife and children, it was easy for the court to come to the conclusion that the deceased had an interest in the insurance money during his life time.

In Re Hodson's Settlement, Brookes v. Attorney General (1939 (1) AER 196) the settlor had vested a trust fund in trustees upon trust that they should, if the income were sufficient, pay yearly sum of $1,200 to one $ during her life time. He also made certain other settlements under none of which there was any chance of anything accruing to the settlor. The court, in examining the application of Section 4 of the Finance Act of 1894 to decide whether the amount

under the settlement could be aggregated with the other estate of the deceased-settlor, formulated a test to decide when it could be said that the property was such that the deceased never had an interest in it. The Court observed (page 210) that in different circumstances different tests may well be applicable. however, there was one test which was properly applicable to the facts of the case before it. "That test is to ask in whose favour there would be a resulting trust of the accumulations in case all the beneficiaries under the disposition under which the property passes were do disclaim the benefits conferred on them by the disposition." If the answer is that the resulting trust would be in favour of the deceased or in favour of his representatives as such representatives, the court would be bound to hold that the property is property of which it would be untrue to say the deceased never had an interest in it.

The test so laid down in this case has been repeatedly applied by the English courts. In the case of Tennant and Ors. V. Lord Advocate (1939 (1) AER 672) the deceased effected a policy of insurance on his own life. Later on he assigned the policy to trustees whom he directed, inter alia, (i) to pay to his testamentary trustees the proceeds of the policy in satisfaction of all death duties payable by reason of his death, and (ii) to pay any residue to his children. On his death the whole proceeds of the policy were paid to the testamentary trustees for payment of death duties. The House of Lords said that for the purpose of determining the rate of estate duty, the sum realised under the policy had to be aggregated with the other estate of the deceased. Lord Russel for Killowen in his judgment observed (page 675): "I feel no doubt that the deceased had, from the commencement of the policy's existence, an interest, and for many years the sole interest, in the proceeds thereof. He could, before the assignation, have assigned or charged the entirety of those proceeds, ad even after the assignation he had a contingent interest therein by way of resulting trust, of which he could have disposed inter vivos or by will. The word 'interest' is a word capable of wide meaning, and I see no valid reasoning for limiting its scope in Section 4 as was suggested in the course of the argument. The case is really covered by the decision of Rowlatt, J., in A-G v. person..... "

In Westminster Bank Ltd. V. Attorney General (1939 (1) Chancery 610), the court of Appeal in England considered a case where a settlor assigned to bank as trustee life policy and investments on trust to accumulate the income of the investment for 21 years or during his life whichever should be shorter and thereafter to hold the settled property on trust to pay the income to other persons specified there. In considering the application of Section 4 to the amounts so settled by the deceased -settlor, the Court of Appeal followed the test laid down in Re Hodson's Settlement (supra) and the decision of House of Lords in Tennant and ors. (supra) observing that it was not possible to predicate regarding policy moneys paid in respect of a policy at one time belonging to the deceased, that the deceased never had any interest in that policy.

Our attention was drawn to a decision for the House of Lords in D'A Vigdor-Goldsmid v. Inland Revenue Commissioners (1953 A.C. 347). In that case, the settlor, inter alia, appointed a policy taken on his life and other settled property being free hold premises to his son absolutely. From the date of that appointment the premiums previously paid by the settlor were paid by his son. To the extent of

the income from the free hold, premiums thereafter were paid by the son from such income. The premiums so paid were, by the Finance Act, 1939, Section 30, attributed to the settlor. The settlor died and his son received under the policy $48,765. The Court, for the purposes of Section 2(1)(d) of the Finance Act, 1894, came to the conclusion that the money received by the son under the policy did not from part of the estate of the deceased. The question, therefore, of the aggregation of this amount with other properties of the deceased did not arise for consideration before the House of Lords in that case. In fact, the decisions in Attorney General v. Pearson and Ors., Tennant and Ors. and Westminster Bank Ltd. (supra) were referred to and it was observed that the issue in those cases was one of aggregation and, therefore, none of these three cases were directly in point. The decision, therefore, in D'A Vigdor-Goldsmid (supra) is not directly relevant to the issue in the present case.

Applying the test as laid down in Re Hodson's Settlement (supra) to the present case, prior to the assignment, the deceased clearly had an interest in the life insurance policies. Even after the assignment, had the assignees disclaimed their interest in the policies, the benefit under the policies would have resulted to the deceased or his representatives. Therefore, it cannot be said that the deceased never had an interest in the life insurance policies for the purposes of Section 34(3) of the Estate Duty Act, 1953. the amount under the three life insurance policies is, therefore, liable to be aggregated with the general estate of the deceased.

In view of the above, the other question as to whether the debts under the three policies should be paid out of the general estate of the deceased or out of the insurance money does not now survive.

In the premises, we hold that the amount under the three life insurance police is forms a part of the general estate of the deceased and that the amounts under the three life insurance policies have to be aggregated with the general estate of the deceased for the purpose of determining the rate of estate duty. The appeals are, therefore, dismissed. In the circumstances, however, there will be no order as to costs.