CHAPTER ONE

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THEORY OF ESTATE DUTY

1.1 INTRODUCTION :

As a back as 166 B.C., what is now known as 'Tributum' was levied in ancient Rome which can be considered as the precursor of the later' Inheritance Tax' introduced in the first century A.D. While the emperor and poor were exempt from the tax, near relatives were also surprisingly exempt from it. Despite this concession in favour of relatives, the Romans continued to leave their properties to their friends rather than to their relatives.[1]

Some sort of death duties, by way of transfer or mutation duty levied at 10% of the value of the property transferred at death, were in existence in ancient Egypt as early as 700 B.C. In B.C. 169 the Roman authorities had already developed a form of inheritance tax. During the middle ages, in Europe, the tax was administered by the ecclesiastical authorities. From 17th century onwards, the Governments of France, Germany, Italy, Switzerland and Netherlands began to impose death duties. In 12th Century, a beginning was made regarding death duty in China, regular death duties of some sort came to be levied systematically in Great Britain in 1894.

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At present death duties are in existence in Australia, Newzealand, Canada, South Africa, Hongkong, Bahamas, Barbadoss, Ceylon, Jamaica, Tobago, Trinidad, British Guiana, Fiji, France, Germany, Holland, Belgium, Switzerland, Italy, Czechoslovakia, Austria, Sweden, Span, Norway, Chile, Denmark, Argentina and Japan, Among the major countries of the world, India is the only one, which today does not possess death duty in its fiscal armoury.[2]

Great Britain introduced estate duty in 1894 for the first time, Sir Willaim Harcourt, introducing the Finance Bill, 1894 made a very cryptic remark. He said " Nature gives no man power over his earthly goods beyond the term of his life."[3]

Sir William Harcourt stated that the State takes its share first before any of the successors in title or beneficieries. The reason on which this is founded is plain. The title of the State to a share in accumulated property of the deceased is an anterior title to that of the interest to be taken by those who are to share it. The State has its first title on the estate and those who take interest afterwards have a subsequent and subordinate title. Nature gives a man no power over his earthly goods beyond the term of his life. What power he possesses to prolong his will after his death, the right of a dead man to dispose of his property is

a pure creation of the law and the state has a right to prescribe the conditions and the limitations under which the power shall be exercised.[4]

1.2 LEGAL JUSTIFICATION OF ESTATE DUTY :

Professor Ely,[5] advocating the legality of imposing Estate Duty by State says that the State is a silent partner in the day to day business of each individual and without its protection it will not be possible for individual to transact any business or amass any wealth with safety and security. This parternship between the State and the individual is dissolved by death of the working partner and as a result the silent partner also is entitled to a share of the capital of business. It is generally assumed that the tax on property may be justified and said to be legal only when the Government intends to set apart the proceeds from Estate Duty for the general improvement of the masses and to fight unemployment in the country.

Mr. Ramaiya says that " The properties of persons who are dead suggest themselves in the process of elimination as fit and proper source from which to replenish the state Treasury." The State, therefore, can rightly impose taxes on his inherited property, and man receiving such property which he has not

earned during his life time shound be made to pay a portion of it to the State.[6]

1.3 ECONOMIC JUSTIFICATION OF ESTATE DUTY :

The successor inheriting the property has the ability to pay the tax as the tax is imposed on the actual value of the property passing after the death of the predecessor. The tax is imposed in proportion to the respective ability of the successor to pay the tax. The property of high value is taxed at a higher rate and hence the system of taxation is progressive. But as the Estate Duty is charged on the capital value of a property, Imposition of Estate Duty also satisfies the Cannons of taxation. The Principle of certainty is satisfied in as much as the time of payment, the amount to be paid become clear to the assessee.

The principle of economy is satisfied as the cost of collecting the tax would not be much because the assessment is made only once in a generation instead of collecting it annually as in the case of income tax.[7]

1.4 SOME THEORIES OF ESTATE DUTY :

Some quid-pro-quo theories have been advanced to justify death duties. By quid-pro-quo is meant that one thing is paid for another. Whenever, a levy is made it should be able to give

some specific service, some of these theories are briefly stated below. :

1.4.1 COST OF SERVICE THEORY :

Cost of service theory is a very antique from of the quid-pro-que doctrine and is embodied in probate fees acts of a country. It treats the death duty or to be more precise the inheritance tax, as a fee which is paid by the those inheritors of property that utilise the service of the probate courts. The probate courts which involve some expenditure to the Government levy duties and only those persons who utilise the service of the Government, pay to the extent of the cost of the service. In short, death or estate duty is, according to this theory, looked upon as a legal fee paid to the Govt. for acquiring rights to the property of the deceased by Government sanction, recognition and record.

1.4.2 VALUE OF SERVICE THEORY :

By value of service is meant the value of the service done by the public authority to individuals. To be more precise, any levy or imposition that takes into consideration the value of service cannot be justifiable, and logically taken under the head tax, However, this principle might stand on a better footing than the cost of service theory.

Though the value of service principle in the case of inheritance tax is appreciable, it provides no basis for the levy of the estate duty. On the whole, it is a theory which lends a little weight in the levy of tax in general and death duties in particular.

1.4.3 THE STATE PARTNERSHIP THEORY :

The Government is always a passive and silent partner in the creation of wealth. It therefore, must get in the form of tax, some portion of estate changing hands on the death of the owner. The estate of the decedent has been considered to be a social product. Gladstone arguing in favour of these duties said" The carrying of property in perfect security over the great barrier which death places between man and man is perhaps the very highest achievement, the most signal proof of the power of the civilized institutions, and an instance so capital of the great benefit conferred by law and civil institutions upon mankind and of the immense enlargement that come to natural liberty through the medium of the law, That I conceive nothing more rational than that, if taxes are to be raised at all, the state shall be at liberty to step in and take from him who is then forward to enjoy the whole in security that portion which may be bonafied necessary for public purpose."[8]

1.4.4 UNEARNED INCOME THEORY :

The amount of property inherited by the beneficiary can be considered as an unearned income. The inheritor gets the property without any effort. The unearned income might not be expected and the inheritor would not mind any progressive death duties levied. "Hardship depends upon disappointment; disappointment upon expectation; and if the law of succession levies nothing, he will not expect anything."[9] The concept of death duties as a defferred income tax on unearned income was prevalent in the United Kingdom when it was first imposed. It takes into consideration the ability of the inheritor to pay death duties and to a great extent, fulfils the function of taxation as a socio-economic measure.

1.4.5 PRIVILEGE THEORY :

It has been contended by some legalists that no natural right can be established for bequests and inheritances. Transfer of property has been looked at as a privilege accorded by the inheritance laws of the state, and whatever the state grants in the shape of laws, it might deprive the inheritors of the same, by another set of laws. Inheritance and bequests have therefore, been looked at from the angle of privileges

that the beneficiaries enjoy under a government. The state has every right to demand a duty from the beneficiaries for the privlege accorded to them. As Shultz remarked", Clearly this doctrine allows the widest possible latitude in the levying of inheriteance taxes; if the 'quo' of the state, the privilege to receive or transmit inherited property is equivalent to the values of the property in question, then the 'quid' that can be demanded from the heir or deducted from the estate is limited only by the value of that property."[10]

4.6 BACK TAX THEORY :

Some times estate duty is supported by the back tax theory. Another recent theory in defence of death duties is on the ground that during the life time of the decedent, several taxes imposed on property and income might have been evaded or avoided by him. Taxes might not have reached that particular property and income which have been accumulated without taxation. It is argued that a person who accumulates a fortune could be presumed to have avoided some legitimate taxes. Mr. Nichols justified death duties as " the only practicable means of reaching the great mass of personal property consisting of stock bonds, notes and other easily concealed objects which readily escape the annual assessment but which must, when the owner dies, pass through the probate court and are then exposed to

official examination."[11] The taxes that have been avoided by the decedent during his life time must ultimately be borne by the heir who inherits his property.

However, the generally accepted principle justifying the taxation of transfer of property at death is that of ability to pay. Similarly, estate duty is justified on the grounds of more equal redistribution of wealth.

1.5 BASE AND COVERAGE :

The estate duty is generally assessed on the aggregate estate passing after death which consists of many items and varieties of property, Section 45 of the Finance Act (1940) of the United Kingdom defines property to include any interest in property movable or immovable and proceeds of sale thereof and any money or investment for the time beings representing the proceeds of sale. The estate duty is imposed therefore, on all property whether personal or real, settled or unsettled.[12]

The following is a classification of property of which an estate duty was paid in England in the year ended on the 31st March 1926.

1. British Government Securities issued since 1914.

2. Other Government and Municipal Securities.

3. Shares in joint stock companies etc.

4. Cash in the house and at the bank.

5. Money lent on mortgages, bonds, bills etc.

6. Trade Assets.

7. Policies of Insurance.

8. Household goods etc.

9. Land.

10. House property and business premises.

11. Mines and minerals.

12. Ground rents etc.

13. Other personal property.

14. Other reality.

The list given above indicates that almost every type of good which has some economic value and the sale of possession of which gives the owner some economic power is a part of property to be taxed by estate duty.

1.6 RATE STRUCTURE :

There is difference in the rate of estate duty among various countries. The following table shows rate scale of estate duty of various countries. The coverage of the death or estate duties is determined by :

a) The limit of exemption and,

b) The number of deaths in a year, after which properties above the exemption limit pass hands.

TABLE NO. 1.1

DEATH DUTY RATES APPLICABLE IN INDIA AND OTHER COUNTRIES OF THE BRITISH COMMON WEALTH (1952-1954) (In Percentages)

Value of Estate (Rs.)	India	Australia	Canada	Ceylon	Newzealand	Pakistan	South Africa	U.K.
1	2	3	4	5	6	7	8	9
100000	Nil	1.86	Nil	4.00	14.32	Nil	3.00	3.00
150000	2.50	3.60	Nil	5.00	16.56	6.00	4.00	6.00
200000	4.38	4.61	Nil	7.00	18.24	6.00	4.00	8.00
300000	7.08	7.62	11.00	8.00	22.72	8.00	7.00	15.00
500000	10.25	10.96	17.00	10.00	28.22	12.00	11.56	24.00
750000	13.50	16.20	23.00	11.00	38.26	15.00	16.55	35.00
1000000	15.13	20.74	26.00	12.00	42.80	25.00	21.28	40.00
1500000	18.42	26.10	29.00	14.00	44.80	30.00	23.50	50.00
2000000	20.06	26.34	32.00	16.00	44.80	30.80	23.64	50.00
3000000	23.28	26.81	35.00	18.00	44.80	35.00	23.76	60.00
4000000	26.28	27.27	38.00	20.00	44.80	35.00	23.82	60.00
5000000	28.03	27.64	41.00	25.00	44.80	35.00	23.99	65.00
7500000	32.02	27.90	44.00	30.00	44.80	35.00	24.00	70.00
10000000	34.01	27.90	48.00	30.00	44.80	35.00	24.00	70.00
15000000	36.01	27.90	52.00	35.00	44.80	35.00	24.00	80.00
20000000	37.00	27.90	52.00	40.00	44.80	35.00	24.00	80.00
30000000	38.00	27.90	54.00	40.00	44.80	35.00	24.00	80.00

The conversion rate used for different currencies is as follows Rs.(India) 100 = £(Australia) 9.6875 =$ (Canada) 21 = Rs (Ceylon & Pakishtan) =100 £ (U.K.) (Newzealand and South Africa) 7.5

Source : I.S.Gulati 'Capital Taxation in a Developing Economy (India) orient Longmans Private Ltd. Calcutta P. 166.

1.6.1 COMPARISION OF RATES OF ESTATE DUTY :

From table No. 1.1, it is seen that rates of estate duty in U.K are the highest in respect of similar slabs of estate value in different countries. On the other hand rates of estate duty are lowest in South Africa. In Newzealand, the rate structure is progressive in the lower range of estate value (only upto Rs. 10 lakhs) beyond which it remains stable. The same is true in case of Pakistan. In case of India, it can be said that the rate structure incorporates a proper gradually increasing progressivity. In case of other countries, the progressivity is not smoothly countinuous. On the whole, the rate structure of estate duty in India can be described as moderately progressive but on the lower side. In the subsequent period it has been made steeply progressive on the higher side.

1.7 EXEMPTIONS :

In England exemption limit was raised from £ 100 to £ 2000, in 1946-47. As a result 50,000 out of 200,000 estates did not remain liable to taxation. Exemption is given on insurance policies and household goods upto a certain limit.

In Australia and India, agricultural land is exempted from valuation of estate duty. Gifts, policies of insurance upto a certain limit are exempt from valuation of estate. Amounts left for female dependents are also exempt. House hold goods upto a certain limit are also exempt from estate duty.

1.8 SHIFTING AND INCIDENCE OF ESTATE DUTY :

In understanding the shifting and incidence of estate duty, it is necessary to have a proper justification for the state's right to impose estate duty. It is true that in a system of private property, individual should have (generally has) some right to determine how his property will be distributed upon his death.[14]

However, it must be noted that the right to property is not a natural right, it is a creature of the social and legal system and thus is legally established by common consent.[15] It is but natural that as an extension of protection function, the transfer of property must take place under the aegis of Government. Therefore, the Government presents its tax claims at the time of death of a person whose property is distributed between heirs. When the tax is imposed and paid before the distribution of property between heirs, it is known as estate duty. If the tax is to be imposed on the shares of property going to individual heirs, it is known as inheritance tax.[16]

So far as incidence of estate duty is concerned, it is generally maintained that the estate duty places, the whole incidence upon the successors or inheritors of the estate. It is said that dead men can not bear tax burden. Moreover, there is no mechanism by which tax can be shifted beyond the successor.[17]

This theory can be accepted only if following assumptions are true.

i) Those who create estates during their life time do not think about death duties.

ii) They have what they can only for the purpose of estate building. However, some people may think of estate duty in an anticipation of the death taxes. Whenever, the objective in estate building is the creation of wealth of a given amount after taxes, then the rate of saving during the testator's life time must be greater than it would have been without tax. It means that the testator creates an estate (after taxes) by setting a fund for tax payment. The additional self denial required to meet the tax represents the burden of a tax on the deceased. We, therefore, conclude that incidence of estate duty can be on testator, the successor's or upon both.[18]

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