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R.M. ARUNACHALAM ETC.

v.

COMMISSIONER OF INCOME TAX, MADRAS

JULY 9, 1997

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[S.C. AGRAWAL AND D.P. WADHWA, JJ.]

*Income Tax Act, 1961:*

C Sections 45(1), 48(ii), 49(1) and 55(1)(b) read with Estate Duty Act, 1953—Sections 53(1) and 74(1)—Property after the Death of the owner devolving upon widow and daughter in equal shares—Widow dying and under her Will, properties becoming the property of the assessee—Many properties disposed of by the assessee during various accounting years relevant to AYs 1966-67 to 1972-73—Under the circumstances, the proportionate part of the estate duty, paid consequent to the death of the original owner and his widow, D relevant to the properties sold by the assessee, held neither 'cost of acquisition' nor 'cost of improvement' of the said properties.

E Capital gains—Deductions—"Cost of acquisition"—Amount paid by the heir of a mortgaged property to clear the mortgage—Held, deductible under Section 48 as cost of acquisition.

*Transfer of Properties Act, 1882:*

Sections 58 and 100—Charge and mortgage—Distinguished

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*Words & Phrases:*

"Cost of acquisition" and "cost of improvement"—Meaning of in the context of Income Tax Act, 1961.

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Constitution of India—Article 136—Special Leave jurisdiction—New plea—Income tax—Diversion of Income—Properties acquired under 'Will' subsequently sold—Estate duty paid on such properties, whether deductible in computing the capital gains arising out of such sale on the ground of diversion of income—Held, question having been raised for the first time before the Supreme Court and being entirely independent of the issues considered by

H Tribunal and High Court, not entertained by the Supreme Court.

R, who had considerable moveable and immovable properties, died leaving behind his widow U and daughter S. The properties of R devolved upon the legal heirs in equal shares. The assessee-appellant being the adopted son, inherited the properties belonging to U under her will. During the previous years relevant to AYs 1966-67 to 1972-73, the assessee sold various properties of R bequeathed to him by U. A question arose as to whether the estate duty paid by the assessee with respect to such sale of property could be regarded as "cost of acquisition" or "cost of improvement" for the purpose of computation of income tax under the Income Tax Act. The Income Tax Officer computed the capital gains on the ground that under Explanation to Section 49(1) of the Act, R alone should be considered as the previous owner. Assistant Commissioner as well as the Tribunal rejected the order of assessment by the ITO. However, the Tribunal referred the said question to the High Court, which answered the said question against the assessee. Hence the present appeal.

The assessee contended that in view of Section 74(1) of the Estate Duty Act, estate duty payable in respect of the properties of R and U was the first charge on the capital assets and that the amount paid by the assessee towards the estate duty to the extent it related to those assets should be treated as "cost of acquisition" or "cost of improvement" under Section 45 read with Section 55 of the Income Tax Act and deducted in computing the capital gains arising out of the sale of such properties by the assessee. It was for the first time contended before this Court that estate duty paid was deductible in computing the capital gains on the ground of diversion of income.

Dismissing the appeals, this Court

Held : 1. A charge differs from a mortgage in the sense that in a mortgage there is transfer of interest in the property mortgaged while in a charge no interest is created in the property charged so as to reduce the full ownership to a limited ownership. The creation of charge under Section 74(1) of the Estate Duty Act cannot, therefore, be construed as creation of an interest in the property that is the subject matter of the charge. The creation of the charge under Section 74(1) only means that in the matter of recovery of estate duty from the property which is the subject matter of the charge the amount recoverable by way of estate duty would have priority over other liabilities of the accountable persons. In that sense

A the claim in respect of estate duty would have precedence over the claim of the mortgage because a mortgage is also a charge. The High Court has, therefore, rightly held that as a result of the charge created under Section 74(1) of the Estate Duty Act, it could not be said that title of assessee to the immovable properties received by him from U was incomplete and imperfect in any way. In the context of the facts, the High Court has found that the assessee has admittedly become the full owner of the assets even before the payment of estate duty and on payment of the same he had not acquired a new right, tangible or intangible, in the assets. It cannot, therefore, be said that the amount proportionate to the estate duty paid by the assessee on the properties that were transferred should be treated as "cost of acquisition of the assets under Sections 48 and 49 read with Section 55(2) of the Income Tax Act. Since the title of the assessee to the immovable properties acquired was not incomplete and imperfect in any way, it cannot also be said that as a result of the payment of the estate duty by the assessee there was improvement in the title of the assessee and the said payment could be regarded as "cost of improvement" under Section 48 read with Section 55(1)(b) of the Income Tax Act. [79-B-G]

*Smt. S. Valliammai v. CIT*, (1981) 127 ITR 713 (Mad) (FB), affirmed.

E *Dattatreya Shanker Mote & Ors. v. Anand Chintaman Datar & Ors.*, [1975] 2 SCR 224, *State Bank of Bikaner & Jaipur v. National Iron & Steel Rolling Corpn.*, [1995] 2 SCC 19, relied on.

*Commissioner of Income Tax v. V. Indira*, [1979] 119 ITR 837 (Mad); *Smt Sarala Devi v. Commissioner of Income Tax*, (1996) 222 ITR 211 (Ker), referred to.

F *Winans v. Attorney General*, 1910 AC 27, referred to.

2. The payment made by a person for the purpose of clearing off the mortgage created by the previous owner is to be treated as cost of acquisition of the interest of the mortgage in the property and is deductible under Section 48 of the Act. [82-C]

3. In taking the view that in a case where the property has been mortgaged by the previous owner during his lifetime and the assessee, after inheriting the same, has discharged the mortgage debt, the amount paid by him for the purpose of clearing off the mortgage is not deductible for the purpose of computation of capital gains, the Kerela High Court in *Ambat*

*Echukutty Menon's Case* failed to note that in a mortgage there is transfer of an interest in the property by the mortgagor in favour of the mortgagee and where the previous owner has mortgaged the property during his lifetime, which is subsisting at the time of his death, then after his death his heirs only inherit the mortgagor's interest in the property. As a result of such payment made for the purpose of clearing off the mortgage debt the interest of the mortgagee in the property has been acquired by the heir. The said payment has, therefore, to be regarded as "cost of acquisition" under Section 48 read with Section 55(2) of the Act. The position is, however, different where the mortgage is created by the owner after he has acquired the property. The clearing off the mortgage debt by him prior to transfer of the property would not entitle him to claim deduction under Section 48 of the Act because in such a case he did not acquire any interest in the property subsequent to his acquiring the same. [81-F-H; 82-A-C]

*Ambat Echukutty Menon v. Commissioner of Income Tax*, (1978) 111 ITR 880, overruled.

*Salay Mohamad Ibrahim Sail v. Income Tax officer*, (1994) 210 ITR 700 (Ker); *K.K. Idiculla v. Commissioner of Income Tax*, (1995) 214 ITR 386 (Ker), impliedly overruled.

*Commissioner of Income Tax v. Daksha Ramanlal*, (1992)197 ITR 123 (Guj.), approved.

4. The submission regarding diversion in relation to the amount paid by way of estate duty has been raised by the assessee for the first time before this Court. This is an entirely independent issue which has not been considered by the Tribunal or the High Court. It cannot be permitted to be raised for the first time at this stage. [80-F-G]

CIVIL APPELLATE JURISDICTION : Civil Appeal Nos. 6098-6101 Of 1983 Etc.

From the Judgment and Order dated 23.12.80 of the Madras High Court in T.C. Nos. 994-997 of 1979

Ms. Janki Ramachandran for the appellant in C.A. No.4386/97.

G.C. Sharma, B.K. Prasad, B.S. Ahuja and C. Radha Krishna for the Respondent.

A The Judgment of the Court was delivered by

S.C. AGRAWAL, J. Special leave granted in Special Leave Petition No. 10737 of 1981.

B These appeals filed by the assessee involve the question whether the estate duty paid by the assessee under the provisions of the Estate Duty Act, 1953, to the extent it relates to the property that is transferred by the appellant, can be regarded as 'cost of acquisition' of the said property or 'cost of improvement' to the said property for the purpose of computation of capital gains under the Income Tax Act, 1961 (hereinafter referred to as 'the Act'). Civil Appeals Nos. 6098-6101 of 1983 relate to assessment years 1966-67 to 1970-71, Civil Appeal No. 860 of 1988 relates to assessment year 1972-73 and Civil Appeal arising out of S.L.P. (C) No. 10737 of 1981 relates to assessment year 1971-72.

D Ramanathan Chettiar, who had considerable movable and immovable properties, died on January 26, 1958 leaving behind his wife, Smt. Umayal Achi and daughter, Smt. S. Valliammi as his legal heirs. On his death the said properties devolved upon the aforesaid heirs in equal shares and a partition was effected between them under which certain properties were given to Smt. Umayal Achi and the rest to Smt. S. Valliammi. Smt. E Umayal Achi adopted the assessee as her son in April 1961. She later died on August 20, 1964 leaving a will bequeathing all her properties to the assessee as her adopted son. During the previous years relevant to the assessment years in question the assessee disposed of various properties of Ramanathan Chettiar that were bequeathed to him by Smt. Umayal Achi.

F In respect of the assessment years 1966-67, 1967-68, 1969-70 and 1970-71 the assessee offered Rs. 7,537, Rs. 1,84,480, Rs. 19,015, and Rs. 32,118 respectively as capital gains arising from the said transfers. For that purpose, the assessee had taken the cost of acquisition of the capital assets concerned at their market value as on August 20, 1964, the date on which he became entitled to them under the Will from his adoptive mother. The

G assessee claimed that since estate duty had been paid consequent upon the death of Ramanathan Chettiar and Smt. Umayal Achi, the proportionate part thereof as is attributable to the value of the properties sold should be deducted in computing the capital gains. The Income Tax Officer rejected the said contention and computed the capital gains for the assessment years

H 1966-67, 1967-68, 1969-70 and 1970-71 at Rs. 80050 and Rs. 489876,

Rs.55758 and Rs. 81254 respectively on the ground that under Explanation to Section 49(1) of the Act, Ramanathan Chettiar alone should be considered as the 'previous owner' and that consequently the appellant would be entitled to adopt as the cost of acquisition of the properties sold their value as on January 1, 1954. Appeals filed against the said orders of assessment of the Income Tax Officer were rejected by the Appellate Assistant Commissioner as well as the Income Tax Appellate Tribunal (hereinafter referred to as 'the Tribunal'). At the instance of the assessee, the Tribunal referred the following question to the Madras High Court :-

"Whether in computing the capital gains on the sale of properties made by the assessee during the previous years relevant for the assessment years 1966-67, 1967-68, 1969-70 and 1970-71 , proportionate estate duty paid on the death of Shri Ramanathan Chettiar and Shrimati Umayal Achi in respect of properties sold should be deducted?"

Since the Division Bench of the High Court was not inclined to agree with the view taken in the earlier judgment of the said High Court in *Commissioner of Income Tax v. V. Indira*, (1979) 119 ITR 837, on the meaning of the words "cost of improvement" in Section 55(1)(b) of the Act, the matter was referred to a Full Bench of the High Court. The Full Bench of the High Court in its impugned judgment dated December 23, 1980 *Smt. S. Valliammai & Anr. v. Commissioner of Income-tax, Madras*, (1981) 127 ITR 713 has answered the said question against the assessee and in favour of the Revenue. Civil Appeals Nos. 6098-6101 of 1983 have been filed by the assessee against the said judgment of the High Court.

In respect of assessment year 1971-72 the assessee claimed similar deduction of proportionate estate duty paid in respect of the properties sold which claim of the assessee was declined and the following question was referred to the High Court :-

"Whether in computing the capital gains on the sale of the properties made by the assessee during the previous year relevant for the assessment year 1971-72 the proportionate estate duty paid on the death of Shri Ramanathan Chettiar and Smt. Umayal Achi in respect of the properties sold should be deducted?"

**A** By judgment dated July 29, 1981, the High Court, following the impugned judgment of the Full Bench, answered the said question in the negative and against the assessee. Civil Appeal arising out of Special Leave Petition (C) No. 10737 of 1981 has been filed against the said judgment of the High Court.

**B** In respect of assessment year 1972-73 similar question referred by the Tribunal was similarly answered against the assessee by the High Court by its Judgment dated November 24, 1986. Civil Appeal No. 860 of 1988 has been filed against the said judgment of the High Court.

**C** Before we deal with the submissions of the learned counsel for the assessee, it would be convenient to take note of the relevant provisions of the Act relating to capital gains. Under sub-section (1) of Section 45 of the Act any profits or gains arising from the transfer of a capital asset effected in the previous year are chargeable to income tax under the head "Capital Gains" and are deemed to be the income of the previous year in which the transfer took place. Section 48 which prescribes the mode of computation of income chargeable under the head "Capital Gains" and permissible deductions, at the relevant time, provided as follows :-

**E** Section 48. Mode of Computation and deductions - The income chargeable under the head "Capital gains" shall be computed by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, namely :-

**F** (a) expenditure incurred wholly and exclusively in connection with such transfer;

(b) the cost of acquisition of the capital asset and the cost of any improvement thereto."

**G** Section 49 makes provision regarding the cost of acquisition with reference to certain modes of acquisition of the assets. Sub-section (1) of Section 49 provided as under :

"Section 49. *Cost with reference to certain modes of acquisition.*-

**H** Where the capital asset became the property of the assessee

(i) on any distribution of assets on the total or partial partition of a Hindu Undivided Family; A

(ii) under a gift or will;

(iii) (a) by succession, inheritance or devolution; or

(b) on any distribution of assets on the dissolution of a firm, body of individuals or other association of persons, or; B

(c) on any distribution of assets on the liquidation of a company, or

(d) under a transfer to a revocable or an irrevocable trust, or C

(e) under any such transfer as is referred to in clause (iv) or clause (v) or clause (vi) of Section 47

the cost of acquisition of the asset shall be deemed to be the cost for which the previous owner of the property acquired it, as increased by the cost of any improvement of the assets incurred or borne by the previous owner or the assessee, as the case may be. D

Explanation.- In this sub-section the expression "previous owner of the property" in relation any capital asset owned by an assessee means the last previous owner of the capital asset who acquired it by a mode of acquisition other than that referred to in clause (i) or clause (ii) or clause (iii) of this sub-section". E

The expressions "cost of improvement" and "cost of acquisition" for the purpose of Sections 48, 49 and 50 have been defined in Section 55 of the Act. In clause (b) of sub-section (1) of Section 55 "cost of improvement" was thus defined : F

"(b) "cost of improvement", in relation to a capital asset,- G

(i) where the capital asset became the property of the previous owner or the assessee before the 1st day of January, 1954, and the fair market value of the asset on that date is taken as the cost of acquisition at the option of the assessee, means all expenditure of a capital nature incurred in making any additions or alterations to H

A the capital asset on or after the said date by the previous owner or the assessee; and

(ii) in any other case, means all expenditure of a capital nature incurred in making any additions or alterations to the capital asset by the assessee after it became his property, and, where the capital asset became the property of the assessee by any of the modes specified in Section 49, by the previous owner, but does not include any expenditure which is deductible in computing the income chargeable under the head 'Interest on securities', 'Income from house property', 'Profits and gains of business or profession', or 'Income from other sources', and the expression 'improvement' shall be construed accordingly."

In sub-section (2) of Section 55 the expression 'cost of acquisition' was defined in the following terms :

D "(2) For the purposes of Sections 48 and 49, 'cost of acquisition', in relation to a capital asset.-

(i) where the capital asset became the property of the assessee before the 1st day of January, 1954, means the cost of acquisition of the asset to the assessee or the fair market value of the asset on the 1st day of January, 1954, at the option of the assessee;

E (ii) where the capital asset became the property of the assessee by any of the modes specified in sub-section (1) of Section 49, and the capital asset became the property of the previous owner before the 1st day of January, 1954, means the cost of the capital asset to the previous owner or the fair market value of the asset on the 1st day of January, 1954 at the option of the assessee;"

(Rest omitted).

G A perusal of the aforesaid provisions would show that for the purpose of computation of income chargeable under the head 'Capital gains' the cost of acquisition of the asset and cost of improvement thereto are to be deducted in view of Section 48(b). Under sub-section (1) of Section 49 in a case where the capital asset became the property of the assessee under any of the modes specified in (i), (ii) and (iii), which include succession, H testamentary as well as non-testamentary, the cost of acquisition of the

asset is to be deemed to be the cost for which the previous owner of the property acquired it as increased by the cost of any improvement of the assets incurred or borne by the previous owner or the assessee, as the case may be. Under the Explanation to sub-section (1) of Section 49 previous owner in relation to any capital asset owned by an assessee means the last previous owner of the capital asset who acquired it by a mode of acquisition other than that referred to in clauses (i), (ii) and (iii) of sub-section (1).

In the present case, the capital assets became the properties of the assessee under the Will executed by Smt. Umayal Achi, i.e., under clause (ii) of sub-section (1) of Section 49. The capital assets became the property of Smt. Umayal Achi under sub-clause (a) of clause (iii) of sub-section (1) of Section 49 by succession after the death of her husband Ramanathan Chettiar. By virtue of the Explanation in sub-section (1) of Section 49 Ramanathan Chettiar has been treated as the previous owner of the assets by the Income Tax Officer. In view of Section 48(ii) for computation of income chargeable under the head "Capital gains" deduction can be claimed in respect of cost of acquisition of the capital asset or the cost of improvement thereto.

The question for consideration is whether the estate duty paid in respect of the estate of Ramanathan Chettiar and the estate of Smt. Umayal Achi, to the extent such duty related to the assets in question, can be claimed as a deduction as 'cost of acquisition' or as 'cost of improvement'.

Under Section 53(1) of the Estate Duty Act it was prescribed that where any property passes on the death of the deceased (a) every legal representative to whom such property so passes for any beneficial interest in possession or in whom any interest in the property so passing is at any time vested : (b) every trustee, guardian, committee or other person in whom any interest in the property so passing or the management thereof is at any time vested, and (c) every person in whom any interest in the property so passing is vested in possession by alienation or other derivative title, shall be accountable for the whole of the estate duty on the property passing on the death but shall not be liable for any duty in excess of the assets of the deceased which he actually received or which, but for his own neglect or default, he might have received. In Section 74 of the Estate Duty

**A** Act the following provision was made :-

**B** "Section 74. (1) Subject to the provisions of Section 19, the estate duty payable in respect of property movable, or immovable, passing on the death of the deceased, shall be a first charge on the immovable property so passing (including agricultural land) in whomsoever it may vest on his death after the debts and encumbrances allowable under Part VI of this Act; and any private transfer or delivery of such property shall be void against any claim in respect of such estate duty.

**C** (2) A rateable part of the estate duty on an estate, in proportion to the value of any beneficial interest in possession in movable property which passes to any person (other than the legal representative of the deceased) on the death of the deceased shall be a first charge on such interest :

**D** Provided that the property shall not be so chargeable as against a bona fide purchaser thereof for valuable consideration without notice.

**E** (3) The Controller may release the whole or any part of any property, whether movable or immovable, from charge under this section in such circumstances and on such conditions as he thinks fit."

**F** Before the High Court it was urged on behalf of the assessee that under Section 74(1) of the Estate Duty Act a first charge has been created on the immovable property of the deceased for the purpose of securing payment of the estate duty in respect of properties, movable or immovable passing on the death of the deceased and that as a result an interest has been carved out of the immovable properties of the deceased in favour of the Government and that the said interest has been acquired by the assessee on payment of the estate duty and, therefore, amount of proportion of the estate duty paid by the assessee in respect of the properties sold should also be treated as 'cost of acquisition' under Section 55(2) of the Act. In the alternative it was submitted that the estate duty paid by the assessee should be treated as 'cost of improvement' of the assets sold.

**H** The contention that estate duty paid should be treated as cost of

acquisition was rejected by the High Court on the view that it is only when the title acquired is defective, incomplete or imperfect, the cost of making the title complete and perfect can be treated as the cost of acquisition. According to the High Court, though under Section 74(1) of the Estate Duty Act, a charge is created on the immovable properties for payment of estate duty in respect of all properties passing on death the title to the immovable properties acquired cannot be said to be incomplete or imperfect in any way. The High Court has observed that the charge created under Section 74 is quite ambulatory in effect and in extent, depending on the nature of the assets passing on the death and the discretion of the Controller of Estate Duty to release the whole or any part of the property from the charge, if the circumstances so warrant under sub-section (3) of Section 74. The High Court has stated that where the deceased left immovable property as well as cash sufficient to meet the estate duty liability on his estate, the Controller may release the immovable property from charge in view of the availability of sufficient cash and in that case, . . . there is no effective statutory charge on the immovable property. According to the High Court when she acquired, by inheritance, half of the properties held by Ramanathan Chettiar, on his death, Smt. Umayal Achi got full and complete title therein and likewise when the assessee got the properties under the Will of Smt. Umayal Achi, he got full and complete title therein and the non-payment of the estate duty did not result in their getting an imperfect or incomplete title in the property. The High Court has, therefore, held that since the assessee became the full owner of the assets even before the payment of estate duty, he has not acquired any new rights, tangible or intangible, in the assets.

The High Court has also rejected the alternate claim put forward by the assessee that the estate duty paid is to be treated as the cost of improvement of the assets sold. While holding that in the case of a tangible asset an addition can be only in the form of physical addition but in the case of intangible assets, the addition cannot be physical and, therefore, it is not possible to say in every case that without any physical addition to the capital asset there can be no improvement thereto and that whether physical addition is necessary or not will depend on the nature of the asset, the High Court has observed that in the present case the court was concerned with tangible assets and that by paying the estate duty and there by releasing the property from the charge under Section 74, the assessee cannot be said to make any addition in the property as such.

A The High Court has further observed that in the present case it is not possible to say that the capital assets were the only assets for which the estate duty could be paid and, therefore, there was a danger of the capital assets being proceeded against in enforcement of the charge. The High Court has found that the assessee admittedly became the full owner of the assets even before the payment of estate duty and on payment of the same the assessee had neither acquired any new right in the assets nor had the assessee's title to the assets been improved.

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C On that view of the matter, the High Court has held that no exception could be taken to the decision in *Commissioner of Income Tax v. V. Indira.* (supra) and the said decision did not require reconsideration. In that case the assessee's father had gifted to her a house property. A third party had filed a suit claiming title to an area of land forming part of the gifted property. The assessee compromised with the said third party by paying him a sum of Rs. 6,943. She claimed that in computing the capital gains arising out the sale of the property the said sum of Rs. 6,943 should be deducted as 'cost of improvement' of the property under Section 48 read with Sections 49(1) and 55(1)(b) of the Act. The said claim was rejected by the Income Tax Officer as well as by the Assistant Appellate Commissioner. But the Tribunal held that in paying the said amount the assessee perfected her title to the property by removing the cloud cast on it by a rival claimant and this involved an improvement to the assessee's title to the property and, therefore, the amount in question would constitute the cost of acquisition within the meaning of Section 49(1) of the Act and the assessee was eligible to the deduction claimed by her. The High Court did not agree with the said view of the Tribunal and held that the amount of Rs. 6,943 should not be treated as the cost of acquisition to the previous owner and, therefore, it could not qualify for deduction as cost of acquisition of the asset and it could not also be treated as 'cost of improvement thereto' as the expression 'thereto' would appear to cover a case where the amount is expended on the asset itself.

G In the judgment of the High Court a reference has been made to the judgment of the Kerala High Court in *Ambat Echukutty Menon v. Commissioner of Income Tax*, (1978) 111 ITR 880 [Kerala], wherein it was held that an assessee could not claim deduction of the amount paid by him to discharge a mortgage on the asset as the cost of improvement of the asset sold under Section 48 of the Act.

Smt. Janaki Ramachandran, the learned counsel appearing for the assessee, has urged that in view of the Section 74(1) of the Estate Duty Act, estate duty payable in respect of the properties of Ramanathan Chettiar and Smt. Umayal Achi was the first charge on the capital assets that were transferred by the assessee and that the amount paid by the assessee towards the estate duty, to the extent it related to those assets, should be treated as 'cost of acquisition' or in any event 'cost of improvement' under Section 48 read with Section 55 of the Act. The learned counsel has placed reliance on the observations of Lord Chancellor Loreburn in *Winans v. Attorney General*, (1910) A.C. 27, explaining the difference between Estate Duty and Legacy and Succession duties. The Learned counsel has also invoked the principle of diversion governing computation of income chargeable to tax for the purpose of excluding the amount payable as estate duty and has relied upon the decision of the Kerala High Court in *Smt. Sarala Devi v. Commissioner of Income Tax*, (1996) 222 ITR 211 wherein this principle has been applied in the matter of computation of Capital Gains.

As noticed earlier under Section 53(1) of the Estate Duty Act the persons referred in clauses (a) to (c) thereof were accountable for the payment of estate duty on the property passing on the death of the deceased. Although this liability was in respect of the entire amount of estate duty payable in relation to such property it was limited to the assets of the deceased that were actually received or which but for his own neglect or default, might have been received by such accountable person. Sub-section (5) of Section 53 prescribed that where two or more persons were accountable, they were liable jointly and severally for whole of the estate duty on the property so passing. This would show that the liability of the accountable persons was personal but limited to the assets of the deceased actually received or which might have been received by the accountable person. At the same time, under Section 74(1) of the Estate Duty Act the estate duty payable in respect of the property, movable or immovable, passing on the death of the deceased was the first charge on the immovable property so passed to whomsoever it may vest on his death. What is the legal effect of the creation of this charge under Section 74 of the Estate Duty Act ?

In Section 100 of the Transfer of Property Act, 1882 the following provision is made regarding charges :

A "Section 100, CHARGES, where immovable property of one person is by act of parties or operation of law made security for the payment of money to another, and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property; and all the provisions hereinbefore contained which apply to a simple mortgage shall, so far as may be, apply to such charge.

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C Nothing in this section applies to the charge of a trustee on the trust-property for expenses properly incurred in the execution of his trust, and, save as other expressly provided by any law for the time being in force, no charge shall be enforced against any property in the hands of a person to whom such property has been transferred for consideration and without notice of the charge."

D Construing the said provision, this Court in *Dattatraya Shanker Mote & Ors. v. Anand Chintaman Datar & Ors.*, [1975] 2 SCR 224, has said :-

E "It is apparent from the provisions of the above section that a charge does not amount to a mortgage though all the provisions which apply to a simple mortgage contained the preceding provisions shall, so far as may be, apply to such charge. While a charge can be created either by act of parties or operation of law, a mortgage can only be created by act of parties. A charge is thus a wider terms as it includes also a mortgage, in that every mortgage is a charge, but every charge is not mortgage. The Legislature while defining a charge in Section 100 indicated specifically that it does not amount to a mortgage. It may be incongruous and in terms even appear to be an anti-thesis to say on the one hand that a charge does not amount to a mortgage and yet apply the provisions applicable to a simple mortgage to it as if it has been equated to a simple mortgage both in respect of the nature and efficacy of the security. This misconception had given rise to certain decisions where it was held that a charge created by a decree was enforceable against a transferee for consideration without notice, because of the fact that a charge has been erroneously assumed to have created an interest in property reducing the full ownership to a limited ownership. The declaration that 'all the provisions hereinbefore contained which

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apply to a simple mortgage shall, so far as may be, apply to such charge' does not have the effect of changing the nature of a charge to one of the interest in property." [pp. 232, 233] A

This would show that a charge differs from a mortgage in the sense that in a mortgage there is transfer of interest in the property mortgaged while in a charge no interest is created in the property charged so as to reduce the full ownership to a limited ownership. The creation of a charge under Section 74(1) of the Estate Duty Act cannot, therefore, be construed as creation of an interest in property that is the subject matter of the charge. The creation of the charge under Section 74(1) only means that in the matter of recovery of estate duty from the property which is the subject matter of the charge the amount recoverable by way of estate duty would have priority over other liabilities of the accountable person. In that sense the claim in respect of estate duty would have precedence over the claim of the mortgagee because a mortgage is also a charge. [See: *State Bank of Bikaner & Jaipur v. National Iron & Steel Rolling Corporation* 1995 (2) SCC 19]. The High Court has, therefore, rightly held that as a result of the charge created under Section 74(1) of the Estate Duty Act, it could not be said that title of the assessee to the immovable properties received by him from Smt. Umayul Achi was incomplete and imperfect in any way. In the context of the facts of this case, the High Court has found that the assessee had admittedly become the full owner of the assets even before the payment of estate duty and on payment of the same he had not acquired a new right, tangible or intangible, in that assets. It cannot, therefore, be said that the amount proportionate to estate duty paid by the assessee on the properties that were transferred should be treated as 'cost of acquisition of the assets' under Sections 48 and 49 read with Section 55(2) of the Act. Since the title of the assessee to the immovable properties acquired was not incomplete and imperfect in any way, it cannot also be said that as a result of the payment of the estate duty by the assessee there was an improvement in the title of the assessee and the said payment could be regarded as 'cost of improvement' under Section 48 read with Section 55(1)(b) of the Act. B C D E F G

In *Winans v. Attorney General* (supra) the question for consideration was whether foreign bonds and certificates payable to bearer passing by delivery and marketable on the London Stock Exchange, were, when physically situate in the United Kingdom at the death of owner, liable to H

A Estate duty under the Finance Act, 1894, even though the deceased was domiciled abroad. It was urged that the principle of domicile which governs the liability to Legacy and Succession duties was also applicable to Estate duty. The said contention was negated by the House of Lords and a distinction was made between Estate duty and Legacy and Succession duty. In that context, Lord Chancellor Loreburn said :-

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"Legacy and succession duties fall upon the benefits received by survivors on their accession upon a death. Estate duty falls upon the property passing upon a death, apart from its destination ." [p. 30]

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These observations of Lord Loreburn, on which reliance has been placed by Smt. Ramachandran, relate to chargeability of Estate duty and have no bearing on the question whether any interest is created in the property in respect of the Estate duty payable on the property. That is a question which has to be considered in the light of the provisions contained

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in the Estate Duty Act of our country. On a consideration of the said provisions (especially Section 74), we have found that as a result of the creation of the charge under Section 74 no interest is created in the property which is the subject matter of such charge.

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The submission regarding diversion in relation to the amount paid by way of estate duty has been raised by the assessee for the first time before this Court. Before the Tribunal as well as before the High Court the contentions urged on behalf of the assessee were confined to a claim for deduction by way of cost of acquisition or cost of improvement under Section 48 of the Act. The questions referred to by the Tribunal to the

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High Court have to be considered in the light of the said submissions. The submission regarding diversion involves the question whether apart from the deductions permissible under the express provision contained in Section 48 of the Act, deduction on account of diversion is permissible in the matter of computation of capital gains under the Act. This is an entirely independent issue which has not been considered by the Tribunal or the

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High Court. It cannot be permitted to be raised for the first time at this stage. We, therefore, do not propose to go into this question.

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While we are affirming the impugned judgment of the High Court, we are unable to endorse the view of the Kerala High Court in *Ambat Echukutty Menon v. Commissioner of Income Tax* (supra) to which refer-

ence has been made by the High Court in the impugned judgment. In that case, the assessee, as one of the heirs, had inherited property from the previous owner who had mortgaged the same during his life time and after his death the heirs, including the assessee, had discharged the mortgage created by the deceased. The said property was subsequently acquired under the Land Acquisition Act and for the purpose of capital gains the assessee sought deduction of the amount spent to clear the mortgage. The High Court held that the capital asset had become the property of the assessee by succession or inheritance on the death of the previous owner under Section 49(1) of the Act and the cost of acquisition of the asset is to be deemed to be the cost for which the previous owner acquired it, as increased by the cost of any improvement of the assets incurred or borne either by the previous owner or by the assessee. According to the High Court, having regard to the definition of the expression 'cost of improvement' contained in Section 55(1)(b) of the Act, in order to entitle the assessee to claim a deduction in respect of the cost of any improvement, the expenditure should have been incurred in making any additions or alterations to the capital asset that was originally acquired by the previous owner and if the previous owner had mortgaged the property and the assessee and his co-owners cleared off the mortgage so created, it could not be said that they incurred any expenditure by way of effecting any improvement to the capital asset that was originally purchased by the previous owner. This decision has been followed in subsequent decisions of the High Court in *Salay Mohamad Ibrahim Sail v. Income-Tax Officer and Anr.* (1994) 210 ITR 700, and *K.V. Idiculla v. Commissioner of Income-tax* (1995) 214 ITR 386. A contrary view has been taken by the Gujarat High Court in *Commissioner of Income Tax v. Daksha Ramanlal* (1992) 197 ITR 123. In taking the view that in a case where the property has been mortgaged by the previous owner during his life time and the assessee, after inheriting the same, has discharged the mortgage debt, the amount paid by him for the purpose of clearing off the mortgage is not deductible for the purpose of computation of capital gains, the Kerala High Court has failed to note that in a mortgage there is transfer of an interest in the property by the mortgagor in favour of mortgagee and where the previous owner has mortgaged the property during his life time, which is subsisting at the time of his death, then after his death his heir only inherits the mortgagor's interest in the property. By discharging the mortgage debt his heir who has inherited the property acquires the interest of the mortgagee in the

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- A property. As a result of such payment made for the purpose of clearing off the mortgage the interest of the mortgagee in the property has been acquired by the heir. The said payment has, therefore, to be regarded as 'cost of acquisition' under Section 48 read with Section 55(2) of the Act. The position is, however, different where the mortgage is created by the owner after he has acquired the property. The clearing off the mortgage debt by him prior to transfer of the property would not entitle him to claim deduction under Section 48 of the Act because in such a case he did not acquire any interest in the property subsequent to his acquiring the same. In *Commissioner of Income-tax v. Daksha Ramanlal* (supra) the Gujarat High Court has rightly held that the payment made by a person for the purpose of clearing off the mortgage created by the previous owner is to be treated as cost of acquisition of the interest of the mortgagee in the property and is deductible under Section 48 of the Act.
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For the reasons aforementioned, the appeals are dismissed. But in the circumstances there will be no order as to costs.

R.K.S.

Appeals dismissed.