

INCOME-TAX IMPLICATIONS ON DEATH AND SUCCESSION



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"He said that there was death and taxes, and taxes was worse, because at least death didn't happen to you every year."

- From the novel 'Reaper Man' by Terry Pratchett

Background

In India, income-tax is levied on every person earning taxable income. Interestingly, death of an individual does not relinquish him from his income-tax liability. It is not only the physical properties but also the rights and obligations (including the obligation to discharge tax liabilities) of the deceased which pass on to some other living persons. This article attempts to explore several issues related to the chargeability of income-tax in respect of:

- A. **Income of the deceased up to the date of death**
- B. **Income of the deceased after the date of death**
- C. **Income of the estate of the deceased subsequent to distribution to the legatees/legal heirs**
- D. **Succession of property of a Hindu Undivided Family ('HUF')**

Before we deep-dive into the principles and provisions of the Income-tax Act, 1961 ('the IT Act') in relation to death and succession, it is important to revisit the two modes in which the succession of the property of a deceased person takes place in India:

- **Testamentary succession:**

Succession as per the directions regarding the distribution of estate contained in the Will or any other testamentary document is known as 'testamentary succession'. The person executing it is referred to as the 'testator' and the person to whom the property is directed to be given is the 'legatee' or 'beneficiary'. The 'executor' is the individual named in the Will who is responsible for ensuring that the instructions given in the Will are carried out.

The testamentary succession in India of followers of all religions other than Muslims is governed by the **Indian Succession Act, 1925**. Succession of the properties of Muslims (testamentary as well as non-testamentary) is governed by *Sharia law* based on the verses of Quran.

- **Intestate Succession/Non-testamentary succession:**

When an individual dies without making any valid Will, succession of his property is governed by the laws of inheritance applicable to the deceased and the 'legal heirs' entitled under the applicable law take share in the property as a matter of right conferred on them by the applicable laws of inheritance.

Intestate succession of the properties of Hindus, Sikhs, Jains and Buddhists are governed by the **Hindu Succession Act, 1956 ('HSA')**. Succession of the properties of Christians, Parsis and followers of other religions (other than Muslims) is governed by the provisions of the **Indian Succession Act, 1925**. However, succession to the properties of Hindus whose marriages are solemnised under the **Special Marriage Act, 1954** is not governed by the HSA but by the **Indian Succession Act, 1925**¹.

A. Income of the deceased up to the date of death

Section 159 of the IT Act lays down that where a person dies, his legal representative(s) shall be liable to pay any sum which the deceased would have been liable to pay, if he had not died, in the like manner and to the same extent as the deceased. For the aforesaid purposes –

- a) Any proceeding taken against the deceased before his death is deemed to be taken against the legal representative and may be continued against him from the stage at which it stood on the date of the death of the deceased;
- b) Any proceeding which could have been taken against the deceased if he had survived may be taken against his legal representative;
- c) All the provisions of the Act shall apply in relation to proceedings taken or continued against the legal representative.

Section 159 of the IT Act creates a legal fiction and provides the machinery provision for the assessment and recovery of dues from the estate of a deceased person². The legal representative shall be deemed to be an assessee for the purposes of this Act in respect of income received by, or accrued to, the deceased up to the death and in respect of all proceedings continued or taken against him which could have been taken on the deceased.

Meaning of 'legal representatives'

Section 2(29) of the IT Act adopts definition of the term 'legal representative' from Section 2(11) of the **Code of Civil Procedure, 1908**. It means a person who in law represents the estate of a deceased and includes any person who inter-meddles with the estate of the deceased and where a party sues or is sued in a representative character, the person on whom the estate devolves on the death of the party so suing or sued. The term legal representative has a much wider connotation and includes legal heirs, executors or administrators.

The capacity of the executor to represent estate derived under the Will does not depend on whether a probate is obtained. All the executors administering the estate may be held to be the legal representatives of the deceased and liable to the extent of the property taken possession of by them³.

Liability of legal representatives

The liability of the legal representative under this section is restricted to the previous year in which the demise of the individual has taken place⁴. Furthermore, the liability is restricted up to the date of death and only in respect of income that has accrued to the deceased up to the date of death⁵.

¹By virtue of section 21 of the Special Marriage Act, 1954

²Arvind Bhogilal v. CIT [1976] 105 ITR 764 (Bombay)

³First Addl. ITO v. Mrs. Suseela Sadanandan [1965] 57 ITR 168 (SC)

⁴CIT v. Hukumchand Mohanlal [1971] 82 ITR 624 (SC)

⁵Raghunathdas Kanani v. Addl. CIT [1979] 2 Taxman 584 (MP)

The liability of the legal representative is limited to the extent of the estate of the deceased which is in the possession of the legal representative and is not a personal liability⁶. However, personal liability of the legal representative exists, where pending a tax liability, the legal representative disposes of or parts with any assets of the deceased. In any case, the arrears of tax liability of the deceased assessable in the hands of a legal representative cannot be adjusted against refund, if any, due to the legal representative in his individual capacity⁷.

There is no provision under the IT Act obligating the legal representatives of the deceased to voluntarily inform the income-tax authorities about the death of an assessee⁸. However, with a view to avoid unnecessary complications, it would be prudent for the legal representative or the executor to register himself as 'Representative Assessee' on the income-tax e-filing portal.

Continuation of existing assessment/re-assessment proceedings

An assessment on a dead person is not enforceable in law⁹. The requirement of issuing a notice or order to a correct person and not a dead person is not merely a procedural requirement but an important prerequisite for the validity of such notices/ orders. Accordingly, the notices / orders issued in the name of a dead person is not protected by the provisions of Section 292B or Section 292BB of the IT Act (which provide that minor mistake / defect / omission does not invalidate the impugned proceedings) since it is fundamental to the proceedings¹⁰.

If the assessee dies before the assessment proceedings are completed, the Assessing Officer (AO) is required to ensure compliance of Section 159(2) of the IT Act by bringing all legal representatives on record before passing any assessment order¹¹. A notice issued to the legal representative should clearly mention that it is served upon him in his capacity as a legal representative of the deceased and that the assessment proposed is that of the income of the deceased person¹². An omission to serve or any defect in the service of notices provided by the procedural provisions may render the assessment order irregular (depending upon the nature of the provisions not complied with), but does not make the assessment void or illegal¹³.

Penalty proceedings

The word "any sum" has been inserted in Section 159(1) of the IT Act in place of the words "any tax" which appeared in the provisions of section 24B of the erstwhile Income-tax Act, 1922¹⁴ so as to also cover interest and penalty. Accordingly, a penalty already imposed on the deceased prior to his death may be demanded from the legal representative and collected out of the estate. The penalty proceedings for a default committed by the deceased can be started or continued against the legal representatives.

⁶Union of India v. Mrs. Sarojini Rajah [1974] 97 ITR 37 (Madras)

⁷Hasmukhlal v. ITO [2011] 117 Taxman 231 (MP)

⁸Savita Kapila v. ACIT [2020] 426 ITR 502 (Delhi)

⁹CIT v. Amarchand N. Shroff [1963] 48 ITR 59 (SC)

¹⁰Mrs. Vanitha Gopal Shetty and Others v. ACIT (Writ Petition No. 19840/2019 (T-IT) before the Hon'ble Karnataka High Court;

Sumit Balkrishna Gupta v. ACIT [2019] 414 ITR 292 (Bombay)

¹¹CIT v. Dalumal Shyamumal [2005] 144 Taxman 151 (MP)

¹²CIT v. Sumantbhai C. Munshaw (deceased) [1981] 5 Taxman 27 (Gujarat)

¹³CIT v. Jai Prakash Singh [1996] 219 ITR 737 (SC)

¹⁴Pari materia to Section 159 of the IT Act

Several courts¹⁵ have held that there is no prohibition in law against initiation and levy of penalty on the legal representatives of the deceased person pursuant to provisions of Section 159(2) of the IT Act in case the same was initiated while the assessee was alive or initiated on the legal representatives after the death of the assessee by bringing all the legal representatives on record. However, there are several contrary judgements (i.e. in the favour of assessee). The **Delhi Bench of the Hon'ble Income Tax Appellate Tribunal ("Tribunal")**¹⁶ has held, "In section 159, there is no mention of penalty proceedings. It is amply clear that proceedings under section 159(2) do not include penalty proceedings". Similarly, the **Madras Bench of the Hon'ble Tribunal**¹⁷ has held that as per Section 271(1)(c) of the IT Act, penalty can be levied only on that person who has concealed the particulars of income or filed inaccurate particulars of income. The use of the words 'such person' in Section 271(1)(c) of the IT Act clearly mandates the authority to levy penalty only on the same person who has filed the return of income and concealed the particulars or filed inaccurate particulars in such return. Accordingly, it was held that if the return had been filed by the deceased assessee (against whom no penalty proceedings was initiated), penalty proceedings could not be now levied on the legal representatives who have not filed the return of income. While this ruling is in the context of the penalty provisions under the old regime, its principles can be applied even to the new penalty regime under Section 270A of the IT Act.

Appeals

After filing the appeal, if the assessee dies, his legal representatives may continue with the impugned appeal. An appeal filed by the income-tax authorities against a dead person is incompetent and a nullity¹⁸. The name of the deceased person needs to be substituted with the names of the legal representatives to constitute a valid appeal. In case an appellate authority passes an order in the name of a dead person, then such a matter requires re-adjudication by the relevant appellate authority¹⁹.

Prosecution

The provisions of Section 159(2) cannot be invoked to launch prosecution against the legal representatives in respect of any offences committed by the deceased assessee. The prosecution of any offence would abate with the death of the deceased.

B. Income of the deceased after the date of death

(i) In case the deceased passes away intestate

The property of the deceased person would automatically get devolved on the legal heirs immediately on death due to operation of laws of inheritance applicable to the deceased person. Hence each legal heir would be assessable on the income in respect of his share of estate from the date of death of the deceased person in addition to his personal income.

(ii) In case the deceased assessee passes away testate (i.e., after executing a valid Will)

The chargeability of tax in respect of the income for the period commencing on and from the date of death of a testate person till the complete distribution of his estate is dealt with in the provisions of Section 168 of the IT Act. These provisions make it obligatory on the income-tax authorities to tax the income from the estate of the deceased person in the hands of the 'executor' only.

¹⁵*Smt. Tapati Pal v. CIT [2002] 124 Taxman 123 (Cal.); Late Iqbal Hussain v. ITO [2007] 111 TITJ 717 (Allahabad Tribunal)*

¹⁶*ITO v. V.P. Sharma [2006] 154 Taxman 34 (Delhi Tribunal)*

¹⁷*CIT v. Dr. K.C.G. Verghese [2019] 416 ITR 155 (Madras)*

¹⁸*CIT v. Smt. Santosh Rani [1996] 88 Taxman 209 (MP)*

¹⁹*Ramesh M. Mehta v. ACIT [2014] 222 Taxman 142 (Madras)*

Meaning of 'executor'

For the purposes of this section, the term 'executor' has been defined to include an administrator or other person administering the estate of a deceased person. It is provided that if there is only one executor, he would be assessable in the status of an 'individual' but if there are more than one, they shall be assessed as an Association of Persons ('AOP'). Furthermore, the residential status of the executor for the purposes of assessment of income of the estate pending distribution shall be the same as the residential status of the deceased person during the previous year in which the death occurred.

It should be noted that a court receiver appointed by a court to sell the properties of the deceased and distribute the sale proceeds amongst the creditors is neither an executor appointed under the Will nor an administrator and therefore, is not an executor within the meaning of Section 168 of the IT Act²⁰.

Assessment in the hands of an Executor

The Executor is responsible for filing of the return of income and payment of taxes under the IT Act in respect of the estate of the deceased person. The executor shall be assessed in respect of the income of the estate separately from his personal income. The assessment of an executor under Section 168 of the IT Act should be made separately from his personal assessment even if the executor is the sole beneficiary and has applied a part of the estate to his benefit²¹. Thus, a separate PAN would be required for filing the return of the estate of the deceased person. The executor will continue to be assessed until the estate is completely distributed among the beneficiaries. If the estate is not fully administered, the legal heirs cannot be charged to tax²². The executor who is assessed under Section 168 of the IT Act has the right of retention and reimbursement of tax paid or payable by him²³.

In a case where the deceased assessee left two Wills covering different properties situated in India and England wherein different and distinct set of executors were appointed for each Will, the income-tax authorities made a single assessment under Section 168 of the IT Act. In this regard, the **Hon'ble High Court of Gujarat**²⁴ held, "the word 'estate' itself signifies the totality or entirety of the property of a deceased. The contention that there were two separate estates was thus not well-founded in law. A single assessment in the status of "AOP" in respect of the aggregate income from the two estates was, therefore, validly made under section 168."

In case the executors carry on the business of the deceased for some time in the course of winding-up the estate, the profits made by them in carrying out such business should be assessable under Section 28²⁵ of the IT Act. Similarly, the income of the discontinued business should also be taxed in the hands of the executors in the year of receipt as per the provisions of section 176(3A) and Section 176(4)²⁶ of the IT Act.

Set-off and carry forward of losses

Section 78(2) of the IT Act states that except in the case of succession through inheritance, a successor of a business or profession shall not carry forward the losses of the predecessor. Accordingly, a legatee or a legal heir should be able to carry forward and set-off the business losses of the deceased person. Furthermore, it has been held that notwithstanding the status of the executors being an AOP, they are entitled to claim set-off on account of the balance of brought forward losses incurred by the deceased person prior to his death²⁷.

²⁰ITO v. K. Krishnamachari [1985] 11 ITD 194 (Hyderabad Tribunal)

²¹CIT v. Bakshi Sampuran Singh [1982] 133 ITR 650 (Punjab & Haryana)

²²Navnit Lal Sakarlal v. CIT [1992] 193 ITR 16 (SC)

²³Section 169 r.w. Section 162 of the IT Act

²⁴Maharani Vijaykunverba Saheb v. CIT [1982] 8 Taxman 60 (Gujarat)

²⁵Profits and gains of business or profession

²⁶Discontinued business

²⁷CIT v. G.B.J. Seth [1981] 6 Taxman 318 (MP)

Specific legacy

A specific legacy is one where a testator bequeaths to any person a specific part of his property, which is distinguishable from all other parts of his property. For example, bequest of a specific diamond ring, a certain piece of silk cloth, a certain amount of currency notes in an identified chest, etc. The significance of specific legacy lies in the fact that in case of deficiency of assets to pay legacies, the specific legacy is not liable to abate with the general legacies. The specific legacies always have priority in matters of devolution. In computing the total income of any previous year, any income of the estate distributed to or applied to the benefit of any specific legatee shall be excluded. The income so excluded should be included in the total income of the previous year of such specific legatee.

Costs, expenses and payments to beneficiaries/legatees

Payment of the *addya sradh* expenses, cost of probate, death duties, other debts due to the state or the periodic payment to beneficiaries (other than specific legatees) out of the income of the estate in compliance with the obligatory directions of the testator, cannot be deducted in computing the executor's income chargeable to tax from the estate²⁸. Since it is merely a case of application of income, it should not entitle the executors to claim any deduction in respect of the income so applied.

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C. Income of the estate of the deceased subsequent to distribution to the legatees/legal heirs

Once the share of estate of the deceased becomes the property of the legatee on distribution in terms of the Will, the respective legatee becomes chargeable to tax in respect of income arising from the assets received by him in his individual capacity, which accrues from the period commencing from the date of distribution of the assets by the executor/ administrator. The income is computed under the respective heads of income in accordance with the normal provisions of the IT Act. However, as discussed earlier, a legal heir of an intestate deceased person would be assessable on the income in respect of his share of estate from the date of death of the deceased person itself, since the property devolves onto them immediately by operation of the applicable laws of inheritance.

²⁸P.C. *Mullick v. CIT* [1938] 6 ITR 206 (Privy Council)

If the bequest under the Will is in favour of more than one person jointly, the income from such bequest is assessed as income of the AOP (which shall be required to obtain a separate PAN and file its income-tax returns). In case the Will creates a testamentary trust and a bequest is in favour of such a trust, it is assessable as trust's income in accordance with the provisions of Section 160 to 166 of the IT Act.

Section 47(iii) of the IT Act specifically excludes any transfer of a capital asset under a Will from being subjected to capital gains tax in the hands of the deceased transferor. A legatee/ legal heir receives his share of estate as a 'capital receipt', not liable to tax. Receipt of any property under a Will or by way of inheritance is also not subject to deemed gift tax in the hands of the legatee/ legal heir as per the provisions of Section 56(2)(x) of the IT Act.

An interesting issue came up before the **Mumbai Bench of the Hon'ble Tribunal**²⁹ where in the income-tax authorities alleged that sum received by the assessee from legal heirs for giving up his rights to contest the Will of a close relative was a casual receipt earned by the assessee without any consideration and therefore chargeable to tax under the provisions of Section 56(2)(v) of the IT Act. It was held that 'consideration' referred to in the provisions of section 56(2)(v) of the IT Act has to be understood as per the definition of consideration given under Section 2(d) of the **Indian Contract Act, 1872**. The assessee has abstained from contesting the Will and such an act constitutes a valid consideration for receipt of sum of money from the legal heirs. Thus, the amount received by the assessee cannot be said to be without any consideration and is accordingly not taxable under the deemed gift tax provisions of Section 56(2)(v) of the IT Act. The decision of the **Mumbai Bench of the Hon'ble Tribunal** should be applicable even with respect to the new deemed gift tax provisions contained in Section 56(2)(x) of the IT Act.

In case, the legatee / legal heir disposes of any capital asset acquired by him in succession, income from the transfer of such capital asset shall be subject to tax under the head capital gains. Section 49(1) of the IT Act provides that where the capital asset became the property of the assessee under a Will or by succession or inheritance or devolution, the cost of acquisition of the asset shall be deemed to be the cost in the hands of previous owner for the purposes of computing capital gains. Similarly, Section 2(42A) of the IT Act states that for the capital asset which becomes the property of the assessee in the aforesaid circumstances, the period of holding of the previous owner shall also be considered as the period of holding of the assessee for determining whether the capital asset is short term or long term. Furthermore, the courts have held that it is the year of acquisition of the previous owner that is relevant for the purpose of indexation of the cost of acquisition and not the year when the assessee received it under a Will or by succession or inheritance or devolution³⁰.

D. Succession of property of an HUF

An HUF is a body consisting of persons (sons as well as daughters³¹) lineally descended from a common ancestor and include their spouses living together. Income arising from the assets of the family is assessed as income of HUF distinct from the individual income of each coparcener. It continues to be so assessed till a partition is effected and a finding of partition is given by the income-tax authorities. HUF is a legal entity and not a natural person who can die and hence cannot be regarded as a 'deceased person'. Section 159 and Section 168 of the IT Act are applicable only to a natural person. Furthermore, on the death of the Karta of the HUF, the HUF continues to be in existence.

²⁹Purvez A. Poonawalla v. ITO [2011] 138 TT] 673 (Mumbai Tribunal)

³⁰CIT v. Manjula J. Shah [2013] 355 ITR 474 (Bombay)

³¹Pursuant to The Hindu Succession (Amendment) Act, 2005, a daughter is now vested with all rights equal to son including the right to become coparcener by birth or seek partition of the HUF property.

Partition of the property of the HUF

As per Explanation to Section 171 of the IT Act, partition means:

- (i) *Where the property admits of a physical division, a physical division of the property, but a physical division of the income without a physical division of the property producing the income shall not be deemed to be a partition; or*
- (ii) *Where the property does not admit of a physical division, then such division as the property admits of, but a mere severance of status shall not be deemed to be a partition.*

Although, as per the Hindu law, partial partition of the HUF either as regards its assets or as regards members is fully valid, the income-tax laws do not recognise such a 'partial partition'. The income-tax laws require that partition of HUF should be full as regards all the assets as well as in respect of all the members. So, unless there is total partition of the HUF, the income arising in respect of the partly distributed assets shall be continued to be taxed in the hands of the HUF. After a finding as regards total partition is recorded as per the provisions of Section 171 of the IT Act, the HUF as an entity is assessed up to the date of partition and thereafter each member or group of members (referred to in common parlance as smaller HUFs of descendants of the Karta) is individually subjected to tax in respect of income from assets falling to their share.

Devolution of interest in the HUF property

Prior to the amendments introduced by the Hindu Succession (Amendments) Act, 2005 ('2005 Amendments'), Section 6 of the HSA provided that on the death of a Hindu, his interest in the coparcenary property would devolve by rule of survivorship, upon the surviving members of the coparcenary and not in accordance with the provisions related to intestate succession of the HSA.

However, the 2005 Amendments have abrogated the rule of survivorship. The replaced Section 6 of the HSA states that when a Hindu dies, his interest in the property of HUF governed by the Mitakshara law, shall devolve by testamentary or intestate succession, as the case may be, and not by survivorship and the coparcenary property shall be deemed to have been divided as if a partition had taken place.

In a recent judgement, the **Hon'ble Supreme Court**³² has clarified that the partition referred to in the replaced Section 6 of the HSA is notional and for the limited purpose of ascertaining the share of the deceased coparcener which he would have been entitled to, if a partition had actually taken place immediately before his death. Fiction is only for ascertaining share of a deceased coparcener which would be allotted to him (and which would devolve by testamentary or intestate succession on his death to the legatees / legal heirs) as and when the actual partition takes place.

Disposal of interest in the HUF by way of a Will

As per the provisions of Section 30 of the HSA, any Hindu can dispose of by Will, any property which is capable of being so disposed of by him. The Explanation to the said section clarifies that the interest of a Hindu in a Mitakshara coparcenary property is a property capable of being disposed of by such Hindu and is accordingly capable of being transferred by testamentary disposition.

The issue for consideration here is that when a bequest is made of the interest of the testator in an HUF property, whether the legatee being the member of the family takes it (i) for himself as his 'individual' asset; or (ii) for and on behalf of the HUF headed by himself (i.e. smaller HUF). In the former case, income from such property after distribution is assessable in his individual assessment and in the latter case, as income of the smaller HUF represented by him.

³²Vineeta Sharma v. Rakesh Sharma and Others [2020] 9 SCC 1

It was well a settled position in Mitakshara law that all property of a father or grandfather (self-acquired or ancestral) descends on the sons or grandsons is taken by them as their ancestral property. Their male issue would derive an interest by birth in such property. The position however has become debatable with the HSA under which the son takes it not under the rule of survivorship but in the manner of testate or intestate property.

In the context of a testamentary disposition of the interest in an HUF, the **Hon'ble Supreme Court**³³ has considered the issue in detail. It held that there should be no presumption one way or the other and that the question was primarily one of intention of the donor / testator to be gathered from the gift deed / Will along with the surrounding circumstances in each case. The desire of the donor that the donee should take the property in his own absolute individual capacity or as head of a coparcenary to which he belongs, is a matter to be determined on the basis of donor's / testator's intention regarding the kind of interest which the donees / legatees were to take in the properties devised to them.

Conclusion

Tax implications in respect of the income of the deceased person are summarised as follows:

Upto the date of death	After the date of death till distribution	After distribution
Assessed in the hands of legal representatives under Section 159 of the IT Act	Testate demise Assessed in the hands of executors of the estate under Section 168 of the IT Act Intestate demise Assessed in the hands of legal heirs in respect of their share of the estate	Assessed in the hands of the legatees / legal heirs in their individual capacity. In case a bequest under the Will is in favour of more than one person jointly - then assessed as income of AOP

In recent years, many of us have experienced sudden deaths of our near and dear ones on account of the COVID-19 pandemic. These tragic incidents have resulted in complex situations, especially when tax considerations were overlooked. It is therefore imperative that a careful evaluation from tax and legal perspectives are analysed before an individual executes his Will or undertakes any succession planning measures to ensure that a greater part of the estate is available to the intended legatees / legal heirs instead of being squandered away in discharging income-tax liabilities.

It is essential that the duties and liabilities imposed upon legal representatives / executors under the IT Act are carried out diligently. It includes obtaining and collating the details about all the legatees / legal heirs and the entire estate of the deceased person, the herculean task of filing appropriate return of income and payment of correct amount of taxes, defending the estate of the deceased person in any pending tax litigation, closing the bank and demat accounts of the deceased after transferring the assets and finally surrendering the PAN by writing an application the AO under whose jurisdiction the PAN is registered. If you are a legal representative or an executor of the Will of a deceased person, know that – “with great power comes great responsibility”.

Disclaimer: The material / opinion expressed is exclusively my own and does not express the views of Cyril Amarchand Mangaldas.

³³ *Arunachala v. Muruganatha* AIR 1953 SC 495

