THE GIFT TAX

By

PROFESSOR R. J. TARAPOREVALA

FORUM OF FREE ENTERPRISE

SOHRAB HOUSE, 235, D. NAOROJI ROAD, BOMBAY-1

"People must come to accept private enterprise not as a necessary evil, but as an affirmative good."

—Eugene Black

President, World Bank

THE GIFT TAX

By

Professor R. J. TARAPOREVALA

A gift tax has been proposed by the Finance Minister in the budget of the Government of India for the year 1957-58, i.e., the assessment year 1958-59. The Finance Minister justified the introduction of this new tax as being necessary for plugging an important loophole in the structure of direct taxation in India. He claimed in his budget speech that "the transfer of properties through gifts to one's near relations or associates is one of the commonest forms of avoidance of not only the Estate Duty but also of Income-Tax, Wealth Tax and even the Expenditure Tax. The only way of effectively checking this practice is to levy a tax on gifts." This argument may be logically correct. But "gifts from one person to another provide a convenient means of avoiding or reducing liability to Estate Duty, Income-tax, Wealth-tax, and Expenditure-tax" and have become specially attractive because of the sharply progressive rates at which the government has levied the various direct taxes resulting in a crushing and an unbearable burden of taxation being imposed on the middle and richer classes.

A gift tax exists in a few countries of the world like U.S.A., Canada, Japan, Australia and New

Zealand. The provisions of the Gift Tax Bill (1958) can now be analysed in relatioq to the existing legal framework and economic conditions in India and the experience of foreign countries in the working of gifts taxes.

Under the Gift Tax Bill a tax on the value of gifts made after 1st April 1957 is to be imposed in India. The tax is payable by individuals, Hindu Undivided Families, firms, associations of persons, public limited companies of which the affairs and the majority of shares are controlled by less than six persons, the subsidiaries of such public limited companies, all private limited companies and charitable institutions or funds which are not covered by Section 15B of the Indian Income-Tax Act.

The tax is payable on the market value of the gift as on the date of the gift. The determination of such market value is left entirely to the discretion of the gift tax officials. Thus the Bill provides that "the value of any property other than cash transferred by way of gift shall . . . be estimated to be the price **which in the opinion of the Gift-tax Officer** it would fetch if sold in the open market on the date on which the gift was made."

According to the Gift Tax Bill a gift is defined as "the transfer by one person to another of any existing moveable or immoveable property made voluntarily and without consideration." A special section provides for artificially including within this definition the gift element in four special types

of transfers of property. These are: first, transfers of property made for nominal or inadequate consideration; second, transfers of property for consideration which although stipulated is not meant or likely to pass from the transferee to the transferor; third, release or discharge from one's debts or liabilities and fourth, withdrawals or appropriations from property owned jointly by a joint holder other than the one who made the original investment or deposit. Further, in order to make the application of the Bill as wide as possible transfer of property is defined to include "any transaction entered into by any person with intent thereby to diminish directly or indirectly the value of his own property and to increase the value of the property of any other person." These excessively wide and sweeping provisions will enable gift tax officers to include every conceivable transfer of property within the definition of the term gift for the purposes of the Bill.

The various problems which this definition of gifts will give rise to will now be analysed. They can be divided into two parts. First there are the problems connected with the subject matter of the gift. Second there are the problems of consideration.

SUBJECT MATTER OF THE GIFT

The main problems connected with the subject matter of the gift relate to forgiveness of indebtedness and joint ownership.

Forgiveness of Indebtedness:

Under the Gift Tax Bill "where there is a release, discharge, surrender, forfeiture or abandonment of any debt, contract, or other actionable claim or of any interest in property by any person in favour of another, the value of the release, discharge, surrender, forfeiture or abandonment shall be deemed to be a gift made by the person responsible for the release, discharge, surrender, forfeiture or abandonment." It is provided that this clause shall not apply to "any debt which is proved to the satisfaction of the Gift Tax Officer to have become irrecoverable." These provisions will almost force creditors to take full legal remedies against their debtors. If a creditor settles or compromises a debt he will run the risk of being forced to pay gift tax on the amount which he has foregone. This will happen if the tax officer is of the opinion that the amount foregone could perhaps have been recovered by the creditor through further steps and litigation against debtor. Further, persons possessing rights under contract and actionable claims under law will be forced to indulge in litigation to the fullest possible extent to enforce their rights and claims. If they fail to do so they may be deemed to have abandoned their rights and claims and therefore be liable to pay gift tax on the value of these rights and claims.

These provisions of the Gift Tax Bill are likely to cause great hardship without any justification.

They will tend to disrupt the normal relationship between debtors and creditors and between parties, to contracts. Creditors and owners of rights under contracts or actionable claims will have an unpleasant choice before them: either to incur substantial costs of litigation often with very little chance of success or to abandon their claims and further pay gift tax on them. Commenting on these provisions the editorial of **The Hindu** rightly stated that "that anyone who generously foregoes his claim to principal or interest . . . should be penalised for it seems to be obviously unfair."

It is recommended that these provisions of the Bill should be altered. They may perhaps be made applicable to such transactions as take place between relatives—in which cases the absence of such provisions may provide a loophole for avoidance of the tax. But these provisions should not apply to such transactions which take place between persons who are in no way related or to "arm's length business transactions" unless the tax authorities can prove that in the particular case there was a deliberate intention of making a gift as shown by special circumstantial evidence. The opinion of two famous American jurists, Professors Lowndes and Kramer, on this point may be noted. They correctly point out that:

> "Where a creditor as part of an arm's length business transaction forgives a debt it seems clear that he does not intend to make a gift of any part of the debt for which he fails to receive

consideration, but that he is really exchanging the debt on what appear to him to be the most advantageous terms possible under the circumstances. If a man forgives a debt with the intention of making a gift to the debtor, there is no reason why this should not be treated as a taxable gift. But to tell a man who has lost a substantial sum in an unhappy business deal that he must pay a gift tax upon the loss would be an absurdity. . . ."

Joint Tenancies and Bank Accounts:

Under the Gift Tax Bill where a person who is absolutely entitled to property has it vested in his own name and the name of another person jointly, any withdrawals or appropriations made by the other person out of such property for his own benefit would be deemed to be a gift from the person owning the property to the other person in whom it was jointly vested. This provision is likely to cause some grave administrative difficulties in relation to discovering the purpose for which such withdrawals or appropriations were made, especially from joint bank accounts. A simple example will illustrate the difficulties likely to arise here. If a man A deposits money into a joint account for himself and his wife B, any withdrawals from such account made by B for her own use or benefit would be deemed to be gifts from A to B. But if B withdraws from the account amounts required to pay the household expenses such withdrawals

would not constitute a gift from A to B because A is bound to maintain and support his wife. Payments made by A to B for running the household or withdrawals made by B from their joint account in lieu of such payments would therefore not be taxable gifts. In such a joint account the administrative problems will be to discover which of the parties drew the various cheques out of the account and then to find out the purpose for which such withdrawals were utilised. In most cases it will be extremely difficult and even impossible for an assessee to prove conclusively that a particular withdrawal from a joint account was used for a particular purpose. Thus unless a husband and wife keep detailed records of their expenditure down to the last rupee—and such cases must be most rare—how can a wife prove conclusively that a particular withdrawal from their joint back account owned by her husband was used for the household expenses and not by her for her own pleasures or benefit?

The effect of these provisions will be that persons who may have maintained joint bank accounts purely for the sake of convenience and without any idea of making gifts through such accounts will find themselves in difficulty with the tax officials. They may be called upon to produce detailed records of the purpose for which each cheque drawn from such joint accounts by the joint holder other than the original owner of the money was utilised. It is most unlikely that many persons will

have kept such records for withdrawals made by them from joint accounts after 1st April 1957. Hence they may be called upon to pay gift tax on amounts which were not really given as gifts but of which they are unable to prove the purpose or use. This will be unfair. It is recommended that the Bill should be amended so as to make these particular provisions applicable from 1st April 1958 so that persons having property vested in joint names can at least take steps to meet the requirements of these provisions. For the future persons having joint bank accounts for the sake of convenience would be well advised to dissolve such accounts and to hold the money in their individual names separately in order to escape from the possibilities of considerable harassment from the tax officers in respect of these provisions of the Gift Tax Bill.

Consideration:

The special problems arising out of the definition and nature of consideration are analysed next. Under the Gift Tax Bill a gift is made when property is transferred from one person to another voluntarily and without consideration or for inadequate consideration or for consideration which is not likely to pass from the transferee to the transferor. Hence transfers of property which are made involuntarily or for adequate consideration cannot be treated as gifts. The Bill does not define the term consideration. Therefore the definition of

consideration under the Indian Contract Act must be taken as applicable to the Gift Tax Bill. Under the Contract Act the essence of consideration is that the promisee (or the transferee) takes upon himself some kind of burden or detriment which may consist in parting with something of value or in undertaking a legal responsibility or in foregoing the exercise of legal right. That which is given up must be something which the law can regard as having some value so that the giving of it affects a real, though it may be a very small, change in the promisee's position—this is good, sufficient or valuable consideration. Even compromise of a doubtful claim is valid consideration. Past consideration is also valid consideration under Indian law. However the adequacy of consideration is not necessary for the purposes of the Indian Contract Act.

The problems likely to arise will relate to the determination of adequacy of consideration. Where the consideration takes the form of personal services rendered or the foresaking of a legal right or the settlement of a doubtful claim .it will be extremely difficult to prove that the consideration was adequate. It has been pointed out that valuation is left entirely to the discretion of the gift tax officers. It is possible and likely that the tendency of the officers will be to argue that the consideration paid was 'inadequate and to assess many transfers of property to gift tax—even in cases where there was in fact no gift made. Some parti-

cular problems of special importance are now outlined.

Bad Business Bargains:

If a person enters into a business transaction which later on appears to have been a bad bargain he will run the further risk of being asked to pay gift tax on it. The gift tax officer will have the right to examine all business bargains and transactions. If the officer feels that an assessee did not get for a transfer of property what in the officer's opinion would have been adequate consideration he may assess the party to gift tax on the difference between what he thinks would have been adequate consideration and the price actually realised. Thus the provisions of the Gift Tax Rill may result in a gift tax being levied on business transactions and bargains which may in retrospect appear to have been bad but which were made without the slightest idea of making a gift. The Bill should provide for the exclusion of such transactions from its scope. It should be provided that there will not be a taxable transfer even though a transfer is made for what appears to be inadequate consideration when there is a sale, exchange or transfer of property in the ordinary course of business (i.e. a transaction which is bona fide, at arm's length and free from donative intent). Such a provision exists in the American gift tax law.

Partnerships:

There are many instances in which a person

is admitted into partnership by an existing firm without paying any consideration in money terms. For example many professional firms of lawyers, accountants and architects admit into partnership men possessing the necessary professional qualifications and ability, whose services would be valuable to the firm, without charging the new entrant for goodwill or for the other assets of the firm. Under the Gift Tax Bill the existing partners of such firms may be deemed to have made a gift of the share in the partnership to the new entrant. They may be charged gift tax on it. Of course it may be argued that the value of the services of the new entrant to the firm constitutes adequate consideration for giving him a share in the partnership. But it will be extremely difficult to assess the value of the personal services of the new partner in money terms. The tendency of some tax officers may be to put a low value on such services. Thus the partners of the firm will be deemed to have made a taxable gift if the share of partnership earnings assigned to the newly created partner is in excess of the value of his services (in the opinion of the gift tax officer) to the firm and such surplus comes from some assets of the firm including goodwill.

The effect of these provisions will be that entry into partnership firms will have to be paid for by investing capital. Young men with talent but without financial resources will not be admitted into partnership free because then the exist-

ing partners may have to pay gift tax. The setting up of this artificial barrier to the progress of young and enterprising men, especially professional men, who do not possess initial capital, cannot be justified in the socialistic pattern of society in which it is sought by the government to reduce the disadvantages arising out of inequality of wealth. The Bill should be suitably amended to remove from its scope entry into partnership firms—except that in those cases perhaps where the gift tax officer can prove conclusively by circumstantial evidence that there was an effort on the part of the assessee to make a gift through admitting his relatives or associates into partnership without charging any consideration.

Bonus and Gratuity Payments

Bonus and gratuity or retirement benefit payments given by employers to their employees may be treated as gifts and taxed under certain circumstances where consideration appears to be lacking or inadequate. The position of workers drawing less than Rs. 500 per month can be considered first. These workers are covered by the laws relating to industrial disputes. They can press their demands for payment of bonus out of profits and gratuity or retirement benefits against their employers by raising industrial disputes which can be entered into official conciliation proceedings and thereafter be decided by industrial tribunals. If an employer pays bonus or gratuity to such workmen under an

award of a labour court or an industrial tribunal or in settlement of their claims to receive such payments or under the provisions of any contract of service there will be no question of including such payments under the definition of gift. But it is possible that an employer will be deemed to have made a gift if he voluntarily pays his workmen a bonus or gratuity or retirement benefits without receiving any demand for such payments from the workers. Of course it may be argued that under the existing labour laws and practices the workmen have almost got rights to such payments under certain circumstances and so the satisfaction of such rights by the employer should not be treated as a gift. But such an argument may not be accepted by the Gift tax officers.

In the case of executive or supervisory staff drawing over Rs. 500 per month the payment of a bonus or gratuity or retirement benefit would not constitute a taxable gift only if it is made under the terms of a contract of service or employment. But voluntary payment of bonus or gratuity to executives by an employer will be treated as gifts under the Gifts Tax Bill because executive staff is not covered by industrial disputes and labour laws and they cannot demand bonus or gratuity as a right nor can they press any such demands before labour courts or indust ial tribunals.

The provisions of the Gift Tax Bill are unfair and undesirable in so far as they will enable tax

officers to tax as gifts normal and voluntary payments for bonus and gratuity by employers to their workers and executive staff—even though such payments cannot be looked upon as gifts in the usual sense. If the present provisions of the Bill are enacted they will make employers extremely hesitant to pay bonuses and gratuity to their employees voluntarily. They will make it necessary for the employees to make repeated formal demands for the payment of bonuses and gratuity. This will increase industrial strife and strain labour relations. It is therefore recommended that payments of bonus, gratuity and other retirement benefits by employers to all employees should be specifically exempted from the scope of the Gift Tax Bill.

EXEMPTIONS:

Under the Gift Tax Bill the tax is not to be charged on certain exempted items. Gifts of immoveable property outside India and gifts of moveable property outside India where the donor is not. a citizen of India or where the donor, not being an individual, is a non-resident of this country are exempted from the gift tax. Gifts made under a will or in contemplation of death are also exempted from the tax presumably because they would be covered by estate duties.

Gifts of savings certificates which are declared by the gover ent to be gift-tax free, gifts to government or any local authority and gifts of policies of insurance or annuities to the assessee's wife, children or other dependants (subject to a maximum of Rs. 10,000 value of such policies for each donee) are exempted from the gift tax. This merely amounts to favoured treatment for the government, its savings certificates and to its Life Insurance Corporation.

Charitable Gifts:

The exemptions contained in the Gift Tax Bill for charitable gifts or donations are too narrow, inadequate and definitely niggardly. 'Gifts to charitable institutions and funds recognised under Section 15B of the Indian Income-tax Act and gifts for other charitable purposes upto a maximum of Rs. 100 in respect of each gift are exempted from the payment of gift tax. There are many charitable institutions and funds in the country which are not covered by Section 15B of the Income-tax Act. Thus all communal or religious charities i.e. institutions or funds "expressed to be for the benefit of any particular religious community" are excluded from Section 15B of the Income-tax Act. There are thousands of such institutions and funds throughout the country which are doing excellent work in the relief of poor and destitute persons of various communities. It is not right to penalise gifts to such institutions and funds by imposing the gift tax on them. Indeed as the Bill stands today such charitable and religious institutions will

not even be exempt from the gift tax in respect of amounts and benefits handed out by them for charity (except on amounts of less than Rs. 100). It is recommended that the discrimination against such institutions and funds—i.e. those not covered by Section 15B of the Indian Income-tax Act—which exists in the Gift Tax Bill should be removed. The Bill should exempt from the tax all gifts made by an assessee for any charitable or religious purpose.

The value of gifts which can be made for charitable purposes direct to needy individuals by an assessee without attracting the gift tax is restricted to Rs. 100 per such gift. It is surely not correct to limit personal charity to such a low sum. Today Rs. 100 will not even pay the college fees of a poor student for one year—and there are many generous persons even today who help poor students to get their education by contributing their college fees on a personal basis. It is therefore necessary that the exemption for gifts made to individuals for charity be raised to Rs. 500' per gift if not a higher figure.

Marriage Gifts:

The exemptions contained in the Gift Tax Bill for gifts made on the occasion of marriage are most inadequate. Gifts made by an individual only to a "female relative dependent upon him for the necessaries of life on the occasion of her marriage" are

exempt from the tax upto a maximum of Rs. 10,000 in respect of each such relative. Gifts made by a Hindu Undivided Family only "to any female member of the family who under any law, order or decree of a court is entitled to maintenance from the joint family property on the occasion of her marriage" are exempt from the tax upto a maximum of Rs. 10,000 in respect of each such relative. These exemptions must be broadened considerably. Gifts made to both male and female relatives, whether dependent or not, on the occasion of their marriage should be exempt from the gift tax. To penalise gifts made to male relatives and to female relatives who earn their livelihood and so are not dependent on the occasion of their marriage as is done by the Gift Tax Bill is to offend against our age-old social customs and is a violation of social decency.

Gifts to a Wife:

Gifts made by a husband to his wife upto a maximum of Rs. 1 lakh are exempt from the gift tax. This is a fair and proper exemption.

Basic Exemption Allowance:

There is a basic allowance from the gift tax under which gifts upto Rs. 10,000 made in any one year are exempted. But this exemption is reduced arbitrarily to Rs. 5,000 if the taxable gifts made to any one donee in the year exceeds Rs. 3,000. The

exemption of Rs. 10,000 per year can hardly be called generous in these days when the value of money has shrunk to **a** fraction of what it was ten or fifteen years ago. At best this exemption gives a little relief from the burden of the new tax. But there is absolutely not the slightest justification for arbitrarily reducing this exemption to Rs. 5,000 merely because gifts to an individual exceed Rs. 3,000 in the year. The official notes on clauses of the Gift Tax Bill claim that "this reduction of basic exemption is meant to discourage large gifts being made to the same individual." Gifts of between Rs. 3,000 and Rs. 10,000 today would amount in terms of real purchasing power to gifts of between Rs. 600 and Rs. 2,000 under pre-war conditions. It is difficult to understand how such gifts can be termed as 'large.' It would have been more discreet for the government not to have given this ridiculous explanation of this provision for the reduction of the basic exemption allowance. The provision for reducing the basic exemption allowance to Rs. 5,000 is completely arbitrary, without justification and must be removed from the Bill before it is passed.

Small Gifts must be Exempted:

Under the Gift Tax Bill every rupee given away by an individual in excess of the exemptions outlined so far will have to be declared as a gift and the **tax** will have to be paid thereon. It is surely not proper that the law should require citizens of

this country to keep detailed records of and to declare small and petty amounts which they may give away generously during the year. It is most degrading that the small generosities of human beings should be brought under the detailed scrutiny of the State. It is therefore recommended that the Bill should exempt very small gifts—say of less than Rs. 100 per gift—made by an assessee.

To sum up, the exemptions provided under the Gift Tax Bill are far from adequate. Their scope must be extended considerably.

CHARGE OF THE TAX:

Under the Gift Tax Bill the donor of the gift is liable to pay the tax. However if the tax cannot be recovered from the donor it may be recovered from the donee. Under this harsh provision the donee will have to pay the tax attributable to the gift received by him but at the rates of tax applicable to the donor. The tax is to be charged on the value of gifts made by the donor.

The basis of charging the gift tax is wrong and inequitable. The liability for the gift tax, as also for the estate duty, should be placed on the donee and not on the donor. The ultimate incidence or burden of the tax falls on the donee or the person receiving the gift. To the extent that there is a tax on gifts the donee receives less than he would have received in the absence of such a tax. Today the estate duty is wrongly levied on the donor on

the false notion that the burden or incidence of the duty falls on the deceased person. But the true burden of estate duty falls on the heirs and surely not on the dead man. If a man's property is reduced after his death by the death duties his economic power during his lifetime is not affected. Death duties only reduce the economic power and wealth of the heirs and so should be levied on. the heirs.

The gift tax and estate duty must be levied on the persons who receive the gifts or the legacies. The rate of the gift tax and of estate duty should depend not on the size of the gift or legacy or on the wealth of the donor. The rates of tax should depend on the wealth possessed by the person receiving the gift or legacy. Thus if a poor man receives a gift or legacy he should pay tax on it at a much lower rate than if the same gift is received by a very rich man. This would be the ideal solution because the tax would thus be related to the ability to pay the tax (as measured by his total wealth) of the person on whom the burden of the tax falls, namely, the donee or the person receiving the gift or legacy.

The method of charging the tax on the donor as proposed in the Gift Tax Bill is inequitable and unfair. Since the ultimate burden of the tax falls on the donee the present tax proposals will mean that the tax will fall equally on all persons receiving gifts from the same donor irrespective of whether the donees are rich or poor. Thus if **a** man gives away Rs. five lakhs as gifts the tax will be the same whether the gifts are made to one rich person or to fifty poor persons. The donees who are poor will have to bear the same incidence of the tax as the donees who are rich. This is clearly inequitable. A gift tax on the donee in relation to his total wealth is the only fair solution. Such *a* method of charging the gift tax was recommended by the Kaldor Report. This is another important recommendation ignored whilst it has put into effect many of his other recommendations which suited the purposes of the government.

A method of charging the gift tax on the donee according to his total wealth may even encourage *a* more even distribution of wealth. Today a donor will have to pay the same gift tax whether the gifts are given to one rich man or to fifty poor persons. But if the tax is assessed on the persons receiving the gifts in relation to their wealth the total tax payable may be a substantially less if the gifts are distributed amongst fifty poor persons than if it is given to one rich man. The idea that less of his gifts will be taken away by the government through the gift tax if the gifts are made to more and poorer persons may encourage donors to distribute their gifts more evenly and preferably to poorer persons. Such a gift tax may therefore encourage **a** reduction in the inequalities of wealth and income in the country which should suit the present socialistic goals of the government ideally.

RATES OF TAX:

'Under the Gift Tax Bill the tax is to be levied on a sharply progressive scale in which the rates of tax rise from 4% to 40% of the value of the gifts. The rate of tax is to be determined by the total value of all taxable gifts made by the assessee during the preceding five years. However gifts made before 1st April 1957 even though within the five year period are not to be taken into account for the purposes of the Bill and so are excluded from the gift tax.

The rates of tax appear to be not excessive at the moment. But it must not be forgotten that whenever a new tax is introduced its rates are always kept at reasonable levels initially in order to secure the acceptance of the tax. Thereafter the tendency of the government will be to raise the rates of the tax in order to increase its revenues. Thus for example when the Income tax was first introduced in various countries it was levied at rates which may appear to be nominal by today's standards. The rate of income tax was initially often less than 5%. But over the years governments of all countries have slowly raised the rate at which the tax is payable until today the maximum rate of income tax is more than 60% in most countries and in India it is 84%. The danger of the rates of gift tax being increased over the years to come is there and is great.

CONFLICT OF LAWS AND DOUBLE TAXATION

In the Statements of Objects and Reasons of the Gift Tax Bill the Finance Minister claimed that "with the introduction of this tax, the integrated tax structure which the Government have been aiming at will be complete." But the present structure of direct taxation can hardly be called 'integrated' in the true sense of that term. The various tax statutes contain many conflicting provisions and display considerable confusion in their principles. Indeed such is the lack of integration between the various tax laws that many items may be taxed twice and even thrice in the same year and in the hands of the same taxpayer.

Income Tax & Gift Tax:

The Indian Income Tax Act and the Gift Tax Bill (when passed) will impose double taxation on a number of items. Thus there may be a number of items like secret commissions paid, bonus and gratuity, a portion of travelling and entertainment expenses and even contributions to political parties which may be disallowed as deductions in computing the profits of a business for income tax purposes. Such items may also fall within the definition of a gift under the new Bill. Hence such items will first be treated as income or profit of the business and subjected to the income tax. Simultaneously they may be deemed to be gifts made by the

business and be subjected to the gift tax in the same year and in the hands of the same assessee, i.e., the business. Such double taxation is manifestly unfair and probably not even intended by the government. The Gift Tax Bill should be amended suitably to remove from its scope such cases in which double taxation may be imposed.

Expenditure Tax & Gift Tax:

A comparison between the Expenditure Tax Act and the proposed Gift Tax Rill reveals many discrepancies and much confusion in relation to the exemptions granted under the two laws. Under the Expenditure Tax Act premiums paid by an assessee on insurance policies for his dependants are exempt from the expenditure tax presumably because the maintenance of such policies is considered to be fair personal consumption expenditure which should be allowed to a person,—and there is no limit to the amount of such premiums. But the Gift Tax Bill exempts such policies only upto the maximum value of Rs. 10,000 per dependant from the gift tax. This exemption limit should be removed from the Bill. The Expenditure Tax Act exempts from the tax all expenditure incurred by an assessee "for any public purpose of a charitable or religious nature." A similar exemption for gifts made for such purposes should be introduced into the Gift Tax Bill in place of the proposed narrow and inadequate exemptions contained in the Bill. The Expenditure Tax Act exempts from the tax

"any expenditure incurred by the assessee on the maintenance of his parents subject to a maximum of Rs. 4,000." The Gift Tax Bill has no such exemption. But such an exemption must be introduced into the Gift Tax Bill because in the context of our social conditions and customs the maintenance of aged, old, unemployed or needy parents is a duty. It will offend decency and values to treat such expenditure on the same footing as other voluntary gifts and to levy a gift tax on it.

Estate Duty & Gift Tax:

The provisions of the Estate Duty Act and its amendments proposed in the budget overlap the provisions of the Gift Tax Bill in a manner which will cause considerable uncertainty, anxiety and unjustified hardship to many assessees. Under the provisions of the Estate Duty (Amendment) Bill, 1958, gifts **inter vivos** or gifts made by a person in his lifetime during a period of five years before his death will be liable to estate duty. If a person makes gifts which are governed by the various exemptions contained in the Gift Tax Bill such gifts will be liable to estate duty if the person dies within five years after making the gifts. Thus the provisions of the Gift Tax Bill in respect of the exemptions will provide only partial relief from taxation. In the interest of equity and in order to remove uncertainty in respect of the tax liability on such gifts it is recommended that gifts exempted from the gift tax should be totally excluded

from the provisions of the Estate Duty law.

Under a proposed amendment to the Estate Duty Act no estate duty will be payable on property on which the gift tax has been paid if such property is also included in the estate of the deceased for estate duty purposes presumably by the assessee's death within five years of making such gifts. However such property, on which the gift tax has already been paid, will be taken into account for aggregation purposes for determining the rate of estate duty payable. This is a rather harsh and unfair provision. It should be provided that gifts on which the gift tax has been paid should be totally excluded from the scope of the estate duty law.

If the government wishes to have a proper integrated structure of taxation it should take steps to remove the conflict in the provisions of the various tax laws on the lines suggested.

ADMINISTRATION:

The administrative procedure prescribed by the Gift Tax Bill is the same as that used for the other direct taxes like Income tax, Wealth tax and Expenditure tax. The administrative machinery to be used for gathering the gift tax is the existing one used for collecting the other direct taxes.

The Gift Tax Bill contains an interesting provision for encouraging prompt payment of the tax. The Bill provides for a rebate of 10% on advance

payments towards tax liability made within fifteen days of making the gift. A rebate of 10% on moneys paid in advance would be an attractive advantage for the assessees provided it related to a period of a year or so. However it may take the tax officials much more than a year to complete the assessments. The tendency may be to take three to four years to complete the assessments, especially of those cases in which advance payments have been made as is often done in the case of the other direct taxes. Under such circumstances a rebate of 10% on amounts paid in advance towards tax liability would cease to be attractive. It would amount to a return of about 2½% to 3% on the moneys paid in advance and this would be far from attractive for the assessees. It is therefore recommended that the Bill should provide for a rebate of 10% per annum on advance payments made towards the tax. Such a provision will encourage the tax officers to complete assessments quickly and will also provide a definite attraction for assessees to make advance payments.

The discretionary powers vested in the tax officials by the Gift Tax Bill are enormous and excessively wide. Indeed today tax officials in India enjoy powers under the various tax laws which are far wider and in excess of the powers vested in the tax officials of any other free country of the world. If the government wants these powers of the officials to be used in a fair and efficient manner it should take immediate steps to improve the morale

and the working conditions of the officials. It should attract into the administration of the tax laws persons with first class ability, integrity and character. The most important and effective step to achieve this is to raise the salaries of the tax officials in order to make them commensurate with the greatly increased burden of responsibility and work which has been imposed upon them since May 1957 due to the introduction of various new direct taxes. The tax officials should be paid at least Rs. 1,000 per month. Their grades of salary should enable them to rise to at least Rs. 2,000 per month after some years. The salaries of senior tax officials should also be proportionately up-graded. This was recommended by the Kaldor Report which had noted that "if an extra crore of rupees were spent on raising the standard of salaries in the Revenue Department ... the return to the State in terms of additional revenue collected is bound to be many times the additional cost." This is one of the important recommendations of the Kaldor Report which has so far been conveniently and unfortunately not implemented by the Government of India.

In the budget speech the Finance Minister claimed that "the Taxation Enquiry Commission also had accepted the Gift Tax as theoretically an attractive proposition." But the Commission had in fact opposed the introduction of the gift tax on administrative grounds. Thus the Taxation Enquiry Commission had reported that:

"A gift tax is theoretically an attractive proposition, but it requires considerable experience of the operation of estate duty before it can be introduced. One of the pre-requisites for operating successfully a tax of this nature would be to introduce the submission by income-tax assessees of a statement of assets and liabilities. As more experience is gained in this type of work, the feasibility of introducing a gift tax can be considered. Moreover the rates of death duty are at present low. The value of a gift tax as a second line of defence for estate duty is greater if the rates of the latter are steeply progressive. We are, therefore, not in favour of introducing the gift tax at this stage."

The objection to the gift tax on administrative grounds as reported by the Commission would appear to be valid even today. The wealth tax has been introduced only a few months ago. The tax officials have hardly any experience in handling the statements of assets and liabilities submitted by assessees for the wealth tax. The experience of administering the estate duty is also not sufficient for the officials to ensure a proper handling of the gift tax by them. The present administrative machinery appears to be inadequate for handling the gift tax and imposing it properly and efficiently.

As against an expected yield of Rs. 3 crores annually from the gift tax the budget provides for an additional expenditure of only Rs. 8 lakhs for ex-

pansion of the staff at various levels in the administrative machinery in order to handle the additional burden of work. But this provision for the expansion of the administrative machinery appears to be extremely inadequate. It will imply a further overloading of the present tax officials with the administrative burdens of the gift tax—with a probable decrease in their efficiency.

The provisions of the Gift Tax Bill, as of the other tax statutes introduced recently, are excessively wide, harsh and inequitable. It is possible that the government has deliberately taken vast powers with the intention of administering the laws leniently thereafter. This approach to taxation is not commendable. Bad laws which are leniently administered give rise to many injustices and hardships being imposed on some taxpayers whilst giving scope for favoured or preferential treatment being given to other tax-payers. It is far more desirable to enact good laws of taxation which are reasonable and are properly drafted and then to administer such laws efficiently and fairly so that all tax-payers are treated equally.

Views expressed in this booklet do not necessarily represent the views of the Forum *of* Free *Enterprise.*

The text of a public lecture delivered under the auspices of Forum of Free Enterprise on March 28, 1958, in Bombay.)

——000——

HAVE YOU JOINED THE FORUM ?

Annual Membership Fee *is* Rs. 10/-

6/A/58

Popular Press (Bom.) Private Ltd., Bombay 7.

60