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DONEE-BASED TAXATION OF GIFTS

LEGISLATIVE HISTORY

19.1 Donor based gift-tax under the Gift-tax Act, 1958

The Gift-tax Act, 1958 required the donor to pay gift-tax on taxable gifts made by him to others. The Gift-tax Act, 1958 was abolished in 1997.

19.2 Donee-based gift-tax introduced by the Finance (No. 2) Act, 2004

The Finance (No. 2) Act, 2004, introduced the concept of donee-based taxation of gifts. The Finance Minister, in his Budget Speech of 2004 explained that the objects of donee-based gift-tax as under :

> '… a loophole requires to be plugged ***to prevent money laundering***. Accordingly, **purported gifts from unrelated persons**, above the threshold limit of ₹ 25,000, will now be taxed as income. Gifts received from blood relations, lineal ascendants and lineal descendants, and gifts received on certain occasion like marriage will continue to be totally exempt.'

The Finance (No. 2) Act, 2004 inserted clause (*v*) in section 56(2) which provided that where *any sum of money exceeding twenty-five thousand rupees* is received without consideration by an individual or a Hindu undivided family from any person on or after the 1st day of September, 2004, the whole of such sum shall be taxed as income from other sources. The proviso to clause (*v*) provided that the above provisions shall not apply to sums of money received—

(*a*) from any relative; or

(*b*) on the occasion of the marriage of the individual; or

(*c*) under a will or by way of inheritance; or

(*d*) in contemplation of death of the payer; or

The *Explanation* to clause (*v*) defined 'relative'.

The Finance (No. 2) Act, 2004 inserted sub-clause (*xiii*) in clause (*24*) of section 2 to provide that 'income' shall, *inter alia,* include 'any sum referred to in clause (*v*) of sub-section (2) of section 56'.

19.3 Taxation Laws (Amendment) Act, 2006 substituted limit of ₹ 25000 per transaction with limit of ₹ 50,000 for entire year

The TLA, 2006 amended clause (*v*) to provide that the same shall apply TO GIFTS RECEIVED from 01.09.2004 to 31.03.2006 and inserted new clause (*vi*) of sub-section (2) of section 56 with effect from 01.04.2006. The TLA, 2006 inserted new clause (*vi*) of sub-section (2) of section 56 which provided that where any sum of money, *the aggregate value of which exceeds fifty thousand rupees*, is received without consideration, by an individual or a HUF, in any previous year from any person or persons on or after 1-4-2006, the whole of the aggregate value of the sum shall be taxed as income from other sources. The threshold limit ₹ 25,000 (applicable to each transaction) was amended to ₹ 50,000 (which applies to aggregate of all transactions during the financial year). As stated by the Finance Minister in his speech in Lok Sabha on 17-5-2006, 'The intention is to prevent split transactions, which we find is happening when the threshold is ₹ 25,000'.

19.4 Donee-based taxation extended to gifts in kind by Finance (No. 2) Act, 2009

The Finance (No. 2) Act, 2009 amended clause (*vi*) of sub-section (2) of section 56 to provide that the said clause (*vi*) shall apply to gifts of money received from 1-4-2006 to 30-9-2009. The Finance (No. 2) Act, 2009 inserted a new clause (*vii*) in sub-section (2) of section 56 with effect from 1-10-2009 to expand the scope of donee-based gift tax to cover gifts received of immovable property and gifts received of specified movable property also besides gifts received of money. Consequential amendments were made to section 2(*24*) also by inserting new clause (*xv*) which provides that income includes 'any sum of money or value of property referred to in clause (*vii*) of sub-section (2) of section 56'.

The Finance Act, 2010 amended clause (*vii*) so as to bring 'bullion' within the definition of 'property' w.e.f. 1-6-2010. Accordingly, gifts received of 'bullion' on or after 1-6-2010 shall be liable to be taxed under section 56(2)(*vii*).

19.5 Limited extension of donee-based taxation to firms and closely held companies by Finance Act, 2010

In order to prevent the practice of transferring unlisted shares at prices much below their fair market value, section 56 has been amended by the Finance Act, 2010 [by inserting new clause (*viia*) in section 56(2)] to also include within its ambit transactions undertaken in shares of a company (not being a company in which public are substantially interested) either for inadequate consideration or without consideration where the recipient is a firm or a company (not being a company in which public are substantially interested).

DONEE-BASED TAXATION OF GIFTS REGIME APPLICABLE W.E.F. AY 2018-19

19.6 Donee-based taxation of gifts made universally applicable to all assessees including companies and firms

The Finance Act, 2017 amended clauses (*vii*) and (*viia*) of sub-section (2) of section 56 of the Act to make these clauses inapplicable with effect from 01.04.2017. The Finance Act, 2017 inserted a new clause (*x*) in sub-section (2) of section 56 so as to provide that receipt of the sum of money or the property by any person on or after 01.04.2017 without consideration or for inadequate consideration in excess of threshold limit of ₹ 50,000 shall be chargeable to tax in the hands of the recipient under the head 'Income from other sources'. The Explanatory Memorandum to the Finance Bill, 2017 explained the changes as follows:

> **Widening scope of Income from other sources**
>
> Under the existing provisions of section 56(2)(*vii*), any sum of money or any property which is received without consideration or for inadequate consideration (in excess of the specified limit of ₹ 50,000) by an individual or Hindu undivided family is chargeable to income-tax in the hands of the resident under the head 'Income from other sources' subject to certain exceptions. Further, receipt of certain shares by a firm or a company in which the public are not substantially interested is also chargeable to income-tax in case such receipt is in excess of ₹ 50,000 and is received without consideration or for inadequate consideration.

The existing definition of property for the purpose of this section includes immovable property, jewellery, shares, paintings, etc. These anti-abuse provisions are currently applicable only in case of individual or HUF and firm or company in certain cases. Therefore, receipt of sum

of money or property without consideration or for inadequate consideration does not attract these anti-abuse provisions in cases of other assessees.

In order to prevent the practice of receiving the sum of money or the property without consideration or for inadequate consideration, it is proposed to insert a new clause (*x*) in sub-section (2) of section 56 so as to provide that receipt of the sum of money or the property by any person without consideration or for inadequate consideration in excess of ₹ 50,000 shall be chargeable to tax in the hands of the recipient under the head 'Income from other sources'. It is also proposed to widen the scope of existing exceptions by including the receipt by certain trusts or institutions and receipt by way of certain transfers not regarded as transfer under section 47.

The amendments made by the Finance Act, 2017 to widen the ambit of donee-based taxation of gifts regime are as under:

(*a*) Section 56(2)(*vii*)/(*viia*) is made inoperative with effect from 1-4-2017 and accordingly, any sum or property received without or for inadequate consideration (as aforesaid) before 1-4-2017 shall be taxable as income under clause (*vii*)/(*viia*)

(*b*) Clause (*x*) is inserted in section 56(2) to provide that the following receipts during a previous year would be taxable as income in the hands of *any person*, under the head 'Income from Other Sources' subject to the other provisions relating thereto, made in the clause:

- Any sum of money without consideration, in aggregate exceeding ₹ 50,000 during the financial year; or
- Any immovable property without consideration, the stamp duty value of which exceeds ₹ 50,000; or
- Any immovable property for a consideration which is less than stamp duty value by an amount exceeding ₹ 50,000; or
- Any movable property (as defined and specified) without consideration where aggregate fair market value whereof exceeds ₹ 50,000; or
- Any movable property (as defined and specified) for consideration which is less than fair market value by an amount exceeding ₹ 50,000.

(*c*) The clause also provides for exceptions, mode of computation and other related provision for taxation of the above receipts.

(*d*) In section 49(4), reference of clause (*x*) is inserted to provide that cost of acquisition of property, value whereof is subject to tax

under section 56(2)(*x*), shall include such value, for computing capital gains.

(*e*) Sub-clause (*xviia*) is inserted in clause (*24*) of section 2 so as to include income referred in clause (*x*) of sub-section (2) of section 56, in the definition of income.

19.7 Salient features of new donee-based taxation regime applicable to gifts w.e.f. 01.04.2017 under clause (x)

(*a*) The receipts contemplated [any sum of money or immovable property or movable property as per (b) above], exceed threshold limit as per the table in (*b*) below are taxable

(*b*) The amount liable to tax would be:

Item received	*Threshold limit upto which not taxable*	*Amount liable to tax*
(1)	*(2)*	*(3)*
Sum of money without consideration	If such sums of money received during the previous year in question do not exceed ₹ 50000 in the aggregate	If threshold of ₹ 50,000 exceeded, entire amount received (and not just the amount in excess of ₹ 50000) is liable to tax
Immovable property received without consideration	Stamp duty value does not exceed ₹ 50000	Stamp duty value of property received (If stamp duty value of property received exceeds ₹ 50,000)
Immovable property received for consideration less than stamp duty value	Difference between stamp duty value and consideration does not exceed the higher of (*i*) ₹ 50000 and (*ii*) 5% of the consideration *Note :* With effect from AY 2021-22, the threshold limit is the higher of (*i*) ₹ 50,000 and (*ii*) 10% of the consideration	Entire difference between SDV and consideration if difference exceeds the threshold limit in column (2)
Movable property received without consideration	Aggregate fair market value of movable property received during the financial year does not exceed ₹ 50000	If threshold of ₹ 50,000 exceeded, entire aggregate FMV (and not just the amount in excess of ₹ 50000) is liable to tax

(1)	*(2)*	*(3)*
Movable property received for consideration which is less than their fair market value	Difference between aggregate FMV and consideration does not exceed ₹ 50000	If threshold of ₹ 50,000 exceeded, entire difference is taxable and not just the difference in excess of ₹ 50000

(*c*) The receipts could be by any person.

(*d*) The receipt must be on or after 1-4-2017.

(*e*) The sum of money or property received from any relative, etc. (as specified in the proviso to the clause) would not be liable to tax.

(*f*) *Explanation* to the clause provides reference of certain terms or expressions as defined in *Explanation* to clause (*vii*).

(*g*) Property is defined to mean immovable property being land or building or both and other movable properties, *i.e.*, shares and securities, jewellery, archaeological collections, drawings, paintings, sculptures, any work of art or bullion.

19.8 Whether section 68 or section 56(2)(x) or both shall apply to taxation of gifts

Section 68 of the Act has always been invoked against bogus gifts in the hands of recipient. The Finance (No. 2) Act, 2004, introduced the concept of donee-based taxation of gifts by inserting new clause (*v*) in section 56(2) with effect from 1-9-2004.

The Finance Minister, in his Budget Speech of 2004 explained that the objects of donee-based gift tax introduced to plug a loophole to prevent money laundering that was in vogue after abolition of gift tax in 1997. CBDT's *Circular No. 5/2005, dated 15-7-2005* explains the rationale of new clause (*v*) as aimed at curbing ***'bogus capital-building and money-laundering'***. Again, in the Explanatory Memorandum to Finance Bill, 2010, the objects behind donee-based transactions have been explained as 'introduced as a counter evasion mechanism to prevent laundering of unaccounted income under the garb of gifts, particularly after abolition of the Gift Tax Act.'

In *Chandrakant H. Shah* v. *ITO* [2009] 28 SOT 315 (Mum.), the Tribunal held that section 56(2)(*v*) was introduced to bring bogus gifts to tax. The Tribunal observed as under:

'……..***The Finance Minister has also emphasized on the fact of a loophole existing due to abolition of the Gift Tax Act, 1958, and, thereafter, words 'money laundering' have been used in his speech, hence, the intention is only to prevent money laundering by way of bogus gifts. The Hon'ble Finance Minister has made this intention clear by referring to the Gift Tax Act, 1958***, and by adding exception for gift received from relatives on the occasion of marriage etc. It is also noteworthy that like gift tax, the basic exemption limit has also been prescribed in the section and various exceptions provided in section 56(2)(*v*) of the Act which were also existing in the like fashion in the erstwhile Gift Tax Act, 1958, and this fact also leads to a conclusion that only bogus gifts are also brought to tax under this provision……Thus, in view of above discussion, we are of the view that ***this provision applies to the transactions where undisclosed/unaccounted income of a person is brought in his hand by way of purported gifts***.'

Since sections 68 and 56(2)(*x)* both target bogus gifts, a question arises as to which provisions will apply to taxation of gifts. Moreover, the tax implications differ between section 68 on one hand and section 56(2)(*x*) on the other.

It would be instructive to compare section 56(2)(*x*) with section 68 as these are all anti-abuse provisions to prevent money laundering in the garb of gifts:

Section 68	***Section 56(2)(x))***
Applicable to all assessees	Applicable to all assessees
No monetary threshold/exemption	Gifts above monetary threshold taxable
No exemption to gifts received from relatives or gifts received on occasions of marriage	Gifts from specified relatives or on occasions of marriage exempt
Pre-condition for attracting section 68 is that assessee maintains books of account and credits the gift in his books	Applicable irrespective of whether assessee maintains books or not and irrespective of whether he credits the gifts in his books or not
Income treated as undisclosed income under section 68 are taxable at a flat effective rate of 78% under section 115BBE(1)	Income will be taxed at applicable tax slab

In *Asstt. CIT* v. *Lucky Pamnani* [2011] 129 ITD 489 (Mum.), the ITAT held that reference to the *bona fides* of gift is unnecessary for consideration, while applying section 56(2)(*v*) of the Act. The ITAT observed as under:

'When section 56 of the Act deems a particular receipt as income from other sources, irrespective of the genuineness of the gift, it is difficult to appreciate as to why the learned CIT(A) had given prominence to the availability of copy

> of passbook and the mode of receipt of the gift etc., though it was neither the case of the assessee nor the case of the Assessing Officer at the assessment stage (since reference to the *bona fides* of gift is unnecessary for consideration, while applying section 56 of the Act)'.

In *Smt. Veena Bhatia* v. *Asstt. CIT* [2012] 52 SOT 34 (URO)/22 taxmann.com 150 (Delhi) - Which pertained to assessment year 2006-07 to which section 56(2)(*v*) applied. The assessee had received gifts of sums of money amounting to ₹ 10,36,159 from her real brother who was NRI residing abroad. Her cash book exhibited receipts of gifts of ₹ 1,65,000 from her brother in cash and ₹ 2,32,226 on 10-11-2005, ₹ 3,30,486 on 19-1-2006 and ₹ 3,09,446 again on 19-1-2006. The assessee had supplied the address of her brother and also the evidence of receipt of gift. The AO had made additions of ₹ 10,36,159. The assessee claimed that this gift comes within the ambit of exception provided in section 56(2)(*v*) of the Act because it was received from her real brother. The ITAT upheld the assessee's contentions and deleted the additions of ₹ 10,36,159. The ITAT observed as under:

> 'The case of the assessee that this gift comes within the ambit of exception provided in section 56(*v*) [*Sic:* section 56(2)(*v*)] of the Act because it was received from the real brother. The Assessing Officer has not made much discussion on this issue and has not brought any evidence on the record for doubting the claim made by the assessee. Assessing Officer doubted the genuineness of the gift only on the ground that assessee has been showing receipt of gift in almost alternate year. In our opinion, that cannot be a sound logic for doubting the gift from the blood relative. Therefore, we allow this ground of appeal in assessment year 2006-07 and delete the addition of ₹ 10,36,109'

In other words, it appears that if the assessee is able to establish receipt of gift from 'relative', the same would be exempt under section 56(2)(*v*) and additions under section 68 cannot be made in the hands of the recipient by invoking section 68.

However, the Agra Bench of ITAT in *ITO* v. *Alok Agrawal* [2012] 20 taxmann.com 472 upheld additions under section 68 of gift of ₹ 15,40,000 received by assessee from assessee's younger sister in view of the following facts:

- Younger sister of assessee was filing returns for meagre amount of ₹ 36,654 gifted ₹ 15,40,000.
- The balance upto 9-7-2005 in her bank account from which gift was made was ₹ 13,000 odd and there were huge credits of encashment of units/FDs in her account from 9-7-2005 till date of

gift and balance in her account fell to ₹ 2,000 odd amount after gift of ₹ 15,40,000 was made.

It was held that gift was in contravention of Indian customs and traditions where brother protects younger sister and does not take gifts from her. Assessee failed to furnish complete circle of all transactions from where original money came into account of younger sister. Having regard to all above facts gift received from younger sister and credited to capital account held bogus gift under section 68 and liable to be taxed.

It may be noted that unlike in *Smt. Veena Bhatia (supra)* where assessee made a specific claim for exemption under section 56(2)(*v*) in respect of gift from relative, no such specific claim for exemption was made by assessee in *Alok Agrawal (supra).* Also in *Alok Agrawal (supra),* the decision in *Smt. Veena Bhatia (supra)* nor *Lucky Pamani (supra)* was not brought to the notice of the Tribunal. It is respectfully submitted that ITAT's decision in *Alok Agrawal (supra)* is *per incurium* as it has been rendered without noticing the provisions of section 56(2) and ITAT decisions.

With effect from 1-9-2004, it appears that section 68 cannot be invoked and only section 56(2)(*v*)/(*vi*)/(*vii*)/(*x*) as applicable will have to be applied to tax gifts in view of the following reasons:

- The decisions of ITAT in *Smt. Veena Bhatia (supra)* and *Lucky Pamani (supra)*
- ITAT's ruling in *Chandrakant H. Shah (supra)* wherein the Tribunal held that section 56(2)(*v*) applied to bogus gifts. In that case, ITAT observed that 'It is also true that in the present materialistic society only relatives are likely to make real gifts out of natural love and affection though in the exceptional cases friends and distinct [*sic:* distant] relatives can also make gifts.'
- Section 56(2)(*v*)/(*vi*)/(*vii*)/(*x*) make a presumption that gifts from 'relatives' are genuine gifts out of natural love and affection and deserve to be exempted from tax and so are gifts received on occasion of marriage. Other than that, gifts received from strangers are presumed to be bogus. However, to avoid unnecessary vexation of assessees and also to avoid expending Department's resources on trivial pursuits, a threshold exemption of ₹ 25,000/₹ 50,000 provided in respect of gifts received from non-relatives and without any occasion.

- Section 56(2)(*vii*)/(*x*) also provides for taxation of fair market value of gifts of movable property received without consideration and excess of FMV over consideration of movable property received for consideration less than FMV and stamp duty value of immovable property received without consideration. Thus, section 56(2)(*vii*)/(*x*) is more scientific in valuing gifts of movable property and immovable property and not restricted to addition of amounts credited in assessee's books.
- Section 56(2)(*v*)/(*vi*)/(*vii*)/(x) are not linked to whether assessee maintains books and whether he credits gifts in his books or not.
- Specific provision prevails over general provisions.
- Section 68 uses the word 'may' making it discretionary. Section 56(2) uses the words 'shall be chargeable' and is therefore mandatory.
- Where more than one view is possible, the view beneficial to the assessee should be taken.

All the above lean weightily in favour of an interpretation that once assessee proves it is gift received by him, section 56(2)(*v*)/(*vi*)/(*vii*)/(*x*) will be applied. He need not prove that the donor is creditworthy as that would serve no purpose since section 56(2)(*v*)/(*vi*)/(*vii*)/(*x*) being specific mandatory provisions deem gifts from non-relatives as bogus and taxable except when received on occasion of marriage and deems gifts from relatives as genuine gifts and non-taxable.

19.9 Whether a company can validly give and accept gifts?

Chennai Tribunal in the case *Redington (India) Ltd.* v. *JCIT* [2014] 49 taxmann.com 146 has held that there is nothing against a company making gift of its property to another company. A transfer without consideration when claimed as a gift is always a gift. It is not possible to give any other colour. There is nothing anywhere in law, which prescribes that only natural persons can make gift on the ground of 'love and affection'. Therefore, the lower authorities have erred in law in concluding that the assessee being a corporate body cannot make a gift.

As regards transfer of shares as gift, there is nothing that prohibits a company from giving or receiving gifts. There is no requirement of a gift deed. Only requirement is that it should be authorized by its Memorandum of Association. The provision of section 5, section 122 and section 123 of the Transfer of Property Act which read as under:

Section 5 of TOPA

'5. In the following sections 'transfer of property' means an act by which a living person conveys property, in present or in future, to one or more other living persons, or to himself and one or more other living persons; and 'to transfer property' is to perform such act.

In this section 'living person' includes a company or association or body of individuals, whether incorporated or not, but nothing herein contained shall affect any law for the time being in force relating to transfer of property to or by companies, associations or bodies of individuals……'

Section 122 of TOPA

'122. 'Gift' is the transfer of certain existing movable or immovable property made voluntarily and without consideration, by one person, called the donor, to another, called the donor, and accepted by or on behalf of the donee.

Such acceptance must be made during the lifetime of the donor and while he is still capable of giving.

If the donee dies before acceptance, the gift is void'

Section 123 of TOPA

'123. For the purpose of making a gift of immovable property, the transfer must be effected by a registered instrument signed by or on behalf of the donor, and attested by at least two witnesses.

For the purpose of making a gift of movable property, the transfer may be effected either by a registered instrument signed as aforesaid or by delivery.'

A perusal of the provisions of sections 5, 122, 123 of TOPA indicate that there is no restriction on the corporate transfer of shares by way of gift. There is no requirement in TOPA that a 'gift' can be made only between natural persons out of natural love and affection which means that as long as a donor company is permitted by its memorandum/articles of association to make a gift, it can do so. Further, it is clear from section 123 of TOPA, there is no requirement of a gift deed. For movable property, a gift deed in writing is not necessary, an oral agreement with transfer of possession is sufficient to complete a gift of a movable property- *Jayneer infrapower & Multiventures (P.) Ltd.* v. *Deputy Commissioner of Income-tax, Mumbai*[2019] 103 taxmann.com 118 (Mumbai - Trib.)