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SCOPE OF INHERITANCE TAX IN INDIA

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Introduction

Inheritance tax is the tax levied upon the property inherited by the legal successors in the event of the death of its predecessor. Inheritance tax, though being a progressive tax, has long been subject to debates around the world. While it is supported by the propagators of social justice and equality who view it as a means to reduce inequality by bridging the gap between rich and poor, it's opposed by people who 'priorities liberal property rights,' these are the people who argue that government should not intervene in the matter of family property and refuses to pay double tax on same property. Scholars of countries who have implemented Inheritance tax are convincing their countries to abolish Inheritance tax, whereas countries where inheritance tax is not levied are considering of implementing it. Inheritance Tax aspires to prevent wealth accumulation in the hands of few and redistribution of wealth. However, It is often under scrutiny because of lack of its effectiveness and failure to solve the problem of income distribution.

India is one of the countries that does not levy inheritance tax; however, it would be interesting to note that India did have estate duty in the past. It was introduced in 1953 but was abolished in the year 1958. Nevertheless, there have been speculations that government is planning to re-introduce inheritance tax. Therefore, the objective of this paper is to discuss whether bringing back inheritance tax would be beneficial to India, considering its social and economic structure, evaluating alongside the inheritance tax model of United Kingdom. Furthermore, it will be discussing the fine line of difference between inheritance tax and estate tax and will talk briefly about estate duty of 1953.

Throughout the course of history, there always have been a struggle between public good and individual freedom. Inheritance tax falling in this sphere of struggle between liberty of an individual and common good, it too have been part of debate throughout the history. Inheritance Tax in earlier times was called death tax as it is the tax that arises from the death of an individual and dates back to the Roman empire. The contemporary form of this tax evolved under the medieval kingship era, where the sovereign was the ultimate ruler, and his permission was required to change ownership of the property in the event of death of its owner.

Most countries have evolved a system of taxing property when it moves between generations. There are two types of inheritance tax systems around the world, a donee-based system called inheritance tax and a donor-based system called estate tax. Though inheritance tax and estate tax are often used interchangeably, there is a fine difference between the two of them. An estate tax is levied on the total value of all property of person who has died, while inheritance tax is levied on 'value of individual inheritance received from a deceased person's estate'. The estate tax applies tax on donor and is often called 'everything tax' as such tax is collected on everything owned by the deceased person, Inheritance tax applies on the recipient is calculated on number of heirs and their wealth. It is easier to administer estate tax than inheritance tax because only value to the entire estate needs to be determined in the estate tax, while total tax is calculated separately according to the number of heirs and their wealth.

Inheritance Tax structure In United Kingdom

India and UK share a long history together; laws formed during British rule such as IPC 1860, Contracts act 1872 still continues to be followed in India. Even laws made in the post-independence era has its roots linked to Britain. India and Britain also share the same political democratic system. However, there also exists wide disparities in social, economic and cultural structure. In United Kingdom, the history of inheritance tax is extensive and complex dating back to 1694; the contemporary form of this tax was introduced in 1986. It is regulated by the 'Inheritance Tax Act 1984', which is a levied on the net value of the property making it actually a donor-based tax. It is a single structure of Inheritance tax where the property of deceased is charged at a "flat rate of 40 percent with a nil rate band of £3,25,000 i.e. no tax is charged where the value of your estate is below £3,25,000"[1]. No tax is levied on gifts which are made seven years before death however, with the introduction of new rules in 2006, it attracts tax to Gifts made to trust whether given during lifetime or on death.

The basic threshold is £3,25,000, which can be increased to £500,000 if the estate of deceased includes residential property, it is known as 'residence nil rate band' introduced by Summer Finance Bill 2015, coming into effect in 2017 with the aim to reduce burden of tax for families by making it easier to pass the family home to direct descendants without a tax charge. Initially, it was set at 1,00,000 pounds in 2017 with 25,000 increase every year till 2020, where this allowance would be at 175,000 pounds. To benefit from RNRB, property must be inherited by direct descendants. "If the net value of the estate is above £2 million, the additional nil-rate band will be tapered away by £1 for every £2 that the net value exceeds that amount."[2]

The threshold for gifts is 3000 pounds each tax year ie, gifts made upto limit of 3000 pounds would not be treated as 'estate' as long as the person making gifts is alive for seven years from the date of making such transfer; however, tax would be levied if the person dies within seven years of making such gift even though it is within the limit of 3000 pounds. Inheritance tax is charged at 40 percent on gifts made within 3 years prior to death. Gifts made between 3 to seven years before death are taxed on a sliding scale known as 'taper relief".

In the UK, inheritance tax is attracted when the property is transferred between generations; hence in cases where the property is transferred to a living spouse or a civil partner, inheritance tax is not applicable. Furthermore, "If you're married or in a civil partnership and your estate is worth less than your threshold, any unused threshold can be added to your partner's threshold when you

[1] Inheritance Tax, Overview <https://www.gov.uk/inheritance-tax>

[2]" Inheritance Tax: main residence nil-rate band and the existing nil-rate band https://www.gov.uk/government/publications/inheritance-tax-main-residence-nil-rate-band-and-the-existing-nil-rate-band/inheritance-tax-main-residence-nil-rate-band-and-the-existing-nil-rate-band

die known as transferable nil rate band. This means their threshold can be as much as £1 million"[3].

Inheritance tax, much like all over the world, has been a controversial issue in UK for a long time. One of the significant criticism that is homogeneous all around the world is that it seems as 'double taxation'. Since people are already taxed on their money in the form of 'income tax' or in UK also as in 'capital gain tax', it is argued that the inheritance tax is in form of a second tax on the same income. Another criticism that inheritance faces is that it generates little revenue and does virtually nothing to equalize the distribution of wealth. However, these claims of inheritance tax-generating little revenue were valid in back in year 2000s; inheritance bill has been on the rise since 2009. "Receipts from inheritance tax rose from 2.7 billion in 2010-11 to a record of 5.4 billion in 2018-19. Furthermore, an increase of 15 percent is seen in estates paid inheritance tax (IHT) from 24,500 in the year 2016-17 to 28,100 in the year 2018-19"[4]. This has been seen as a result of the government freezing threshold at 325,000. However, numbers do not depict the whole picture, though it has increased revenue of government, there has been no substantial effort to make Inheritance tax more effective in achieving its ultimate goal of reducing inequality and prevention of accumulation of wealth few hands. It has failed in this aspect of reducing wealth inequality, as wealthy people benefits from loopholes of the provision. Exemptions given on lifetime gifts, alongside with other exemptions like no inheritance tax on agricultural land, wealthy people gets around it by gifting their inheritance during their lifetime while middle-class people who are just above the limit are unable to opt for such route. These loopholes "may create even more inequality as the inheritance tax is said to be quite voluntary tax for the rich while the not-so-rich are subject to tax". These loopholes in a structure rather undermine the whole existence of inheritance tax and are one of the primary reasons for the unpopularity of inheritance tax in UK.

The study of inheritance tax in UK shows that through its constant reform in tax structure since 2009, the government has been able to generate substantive revenue. However, it still has a long way to implement an effective structure without loopholes to stride towards inheritance tax's ultimate objective of reducing inequality of wealth.

<u>Scope of Inheritance Tax in India-</u>

In India, inheritance tax was levied from the year 1953 till it was abolished in 1958. It was a donor-based system governed by 'Estate duty act 1953', which imposed tax on the net value of property inherited. India, at the time of independence, suffered from wide disparities between rich and poor with no source of revenue with government; thus, an inheritance tax was introduced to promote wealth distribution, reduce inequality, and generate revenue alongside. The highest tax rate was as high as 85%, which was taxed on property worth more than 20 lakhs. " The property deemed to be part of one's estate included property which the deceased

[3]" Inheritance Tax, Overview <https://www.gov.uk/inheritance-tax>

[4] Inheritance Tax statistics: commentary <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/832126/IHT_Commentary.pdf>

individual at the time of his / her death was competent to dispose of,"[5]. Tax was not charged on estate of value below 1 lakh and Rs 50000 for Hindu Undivided property. Inheritance tax was levied only when property is transferred between generations, and no tax had to be paid if the property is transferred to spouse. "Gift of property made in contemplation of death shall be deemed to pass on the donor' s death".[6] "Gifts made during lifetime made within period of six months before death in case of public charitable purposes and within two years for other purposes were deemed to pass on death."[7] However, "exemption were provided in case of gits made to charitable purposes up to a maximum of INR 2,500 and of INR 1,500 in case of other gifts."[8] Throughout its span of 30 years, Estate duty was subjected to numerous criticism. The major criticism it faced was its total inability to achieve goals it was sought to achieve. Inheritance tax was implemented with aspiration of prevention of accumulation of wealth in the hands of few and a tool to bridge the gap between rich and poor in the country. The act also faced its criticism because of complexity in the act where different rules of valuation were assigned to different kind of property. Estate tax, along with wealth tax was together seen two taxes on same base, criticising it for being double tax. Furthermore, revenue generated by the tax was minimal, while administration cost remained high. The wealthy found it easy to evade estate tax by concealing their property via the practice of holding Benami property, which government was unable to curb. As a result, it rendered Estate duty ineffective in generating any substantial revenue. Estate duty was finally abolished as it failed to achieve any of its objectives.

With recent speculations of re-introducing inheritance in India, it is only imperative that we look at the arguments advanced both in favor and against inheritance tax.

It is argued that considering India's circumstances where "91% of the adult population has wealth below USD 10,000. At the other extreme, a small fraction of the population (0.6% of adults) has a net worth over USD 100,000 and the top richest 1% own 51.5% of the total wealth".[9] It is quite evident there is a wide disparity between rich and poor, and considering this inequality imposition of inheritance tax is desirable. It is believed that introduction of inheritance tax will act against inequality in wealth and do away with the accumulation of wealth in the hands of few. As it is charged only on the small top rich proportion of population, it will not only generate additional revenue for government but will help government in bridging the gap between rich and poor. Considering the rising inequality, there is school of thought which believes that inheritance tax will be a vital step toward achieving its objective of an equitable society. For them passing on excess wealth leads to concentration of wealth in the hands of few families, and it is only natural for the government to tax such transactions as it is against the principle of equality.

[5] Section 2(15) of the Estate Duty Act, 1953
[6] Section 8 of the Estate Duty Act, 1953
[7] Section 9(1) of the Estate Duty Act, 1953
[8] Section 33(1) (a) and (b) of the Estate Duty Act, 1953
[9] Global wealth report: Credit Suisse <https://www.credit-suisse.com/media/assets/corporate/docs/publications/research-institute/global-wealth-report-2018-en.pdf>

"On the onset, an inheritance tax may appear as a noble cause to pursue, especially in a country like India where 800 million people in villages require basic services like clean drinking water, sanitation, education, and so forth"[10]. However the government should also carefully look at the arguments advanced against it. Critics have argued that Globally inheritance tax has failed to be a major source of revenue in any country in which it has been implemented. "In UK, despite an increase in revenue generated, it contributed only "0.3 percent of total GDP in 2018".[11] Similarly, in "USA, it generated only 16,672 million dollars in 2019 compared to 29,010 million dollars in 2000 despite having fourth highest estate tax rate in OECD countries, contributing only to 0.1 percent of total revenue generated".[12] While its contribution is up to 2 percent in countries like Taiwan and the Republic of Korea, which is considerably high compared to other countries, it is still relatively low. Another major criticism is its failure to reduce the gap between rich and poor on contrary it is argued that it has even widened the gap between the two as rich people often escape tax rather easily and people who are only just above the threshold are subjected to it which can be quite evidently seen in UK. "Richest 5% in America own two-third of the wealth which has risen from 55.20 in 2001 to 66.70 in 2016."[13] Though there are numerous other factors affecting it, claims that the Inheritance tax helps redistribute income cannot be substantiated by facts. Another criticism is related to avoidance of inheritance taxis in the majority of countries where inheritance tax is implemented cases of evasion of such tax is rampant, which hampers its objective to achieve its goals. Furthermore, the cost of its administration is quite high compared to the low tax return. Since all the rich people will evade the tax through numerous practices, including the transfer of their wealth to trust or tending to form Hindu Undivided property to evade this tax and it is only the middle class who are just above the threshold will be harassed by such laws. In India, since the tax-paying community is already a small proportion, only 4 percent of the population who are already paying high GST rates and other taxes, the introduction of inheritance tax would only be an additional burden. In India, its citizens are guaranteed freedom of religion by its constitution as fundamental right since marriage laws and succession are different for different religions, making inheritance laws itself very complicated in India. With no Uniform civil code to govern these, the introduction of inheritance tax would only result in forming a complicated legislation following the footsteps of its predecessor Estate duty of 1953. Such complicated legislation would only result in higher litigation and administration cost with loopholes, which people could exploit, only rendering such tax ineffective.

CONCLUSION -

Despite numerous debates around the inheritance tax, major economies around the world have implemented it in their country.

[10] Tushar Gupta, 'Why The Government Was Right In Skipping The Inheritance Tax' < https://swarajyamag.com/economy/budget-2019-why-the-government-was-right-in-skipping-the-inheritance-tax>

[11] Revenue Statistics - OECD countries: Comparative tables <https://stats.oecd.org/index.aspx?DataSetCode=REV>

[12] Office of Management and Budget, Table 2.5, Composition of Other Receipts, <https://www.whitehouse.gov/omb/historical-tables/>

[13] https://inequality.org/facts/wealth-inequality/

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In japan inheritance rate is highest at 55 percent, followed by South Korea, where the rate is 50 percent, France at the rate of 45 percent, UK and US tax property at the rate of 40 percent. Inheritance Tax is means to promote redistribution of wealth and to prevent its accumulation in the hands of a few. However, in India, the implementation of such a tax is currently unsuitable owing to the county's various socio-economic issues coupled with the lack of real numbers to back claims of inheritance tax. Inheritance tax is a domain with great prospects of redistribution of wealth and reducing the gap between rich and poor, considering the rising inequality in India, the need for the introduction of inheritance tax is not a distant future. In such a case, a lot depends on how the tax is structured, the rate at which it is levied, kind of exemptions given, etc, so that it can achieve the goals it was sought for. In such a event, a careful deliberation on the implementation of such tax would be crucial. Appropriate measures of tackling Benami property, a higher threshold for targeting only upper-class rich people with generous exemption, low tax rate, measures like automating the process of tax collection for smooth functioning, mechanism for ill-liquidated assets should be taken into consideration for encouraging full and proper compliance and building acceptability and creating a broader taxpayer base. The government should not hurry in the re-introduction of such far-reaching legislation, and only after proper consideration to all factors a decision should be taken.

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