

BUDGET HOPES: EXEMPTING FAMILY SETTLEMENT FROM ANTI-ABUSE TAX PROVISIONS



POWER POINT

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Family businesses are the backbone of any economy across the globe. Their role in the Indian context cannot be overstated with over 85% of family-owned businesses. Further the institution of joint families and family-owned businesses stands as a hallmark of India's cultural and economic heritage.

Within this framework, family businesses have flourished, leveraging not just financial capital but also familial bonds and shared values to achieve success over generations.

Alongside the benefits of familial collaboration come inherent challenges, particularly the complexities arising from cross-holdings and intergenerational dynamics within family-owned enterprises. These complexities can lead to disputes over ownership, management control, and wealth distribution, threatening both business continuity and harmony.

Indian families utilise family settlements to navigate challenges, ensuring equitable distribution of wealth and assets among members. A family settlement is a structured agreement aimed

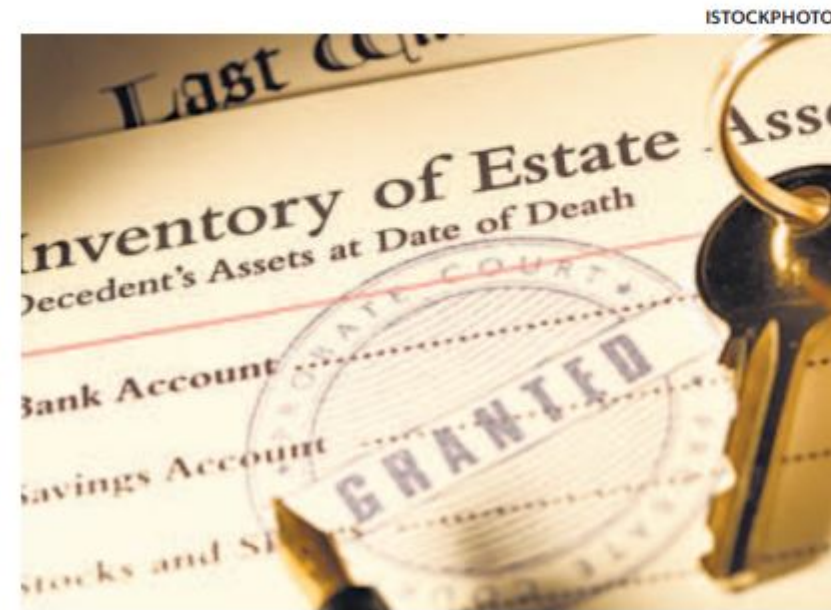
at amicably resolving disputes, thereby preserving family unity and minimising legal complexities.

By proactively addressing conflicts through formal asset division and clear delineation of responsibilities, families mitigate the risk of prolonged legal battles. This approach not only safeguards financial interests, but also reinforces cultural values of an Indian joint family. Furthermore, family settlements play a pivotal role in ensuring business continuity by providing clarity on succession planning, management roles, and ownership rights. This strategic clarity is crucial for the sustainable growth of family enterprises across generations.

Family settlements serve as pragmatic solution, offering structured framework for wealth distribution and conflict resolution, helping Indian families uphold their legacy of unity and resilience, while securing the future of their business endeavours.

Anti-abuse laws in I-T Act: There are anti-abuse laws in the Income Tax Act, which provides for tax on a person receiving a property at less than its fair market value (FMV). The difference between transaction price and the FMV is taxable in the hands of the recipient. "Property" for this purpose can include land, building, shares and securities, jewellery, bullion, or any work of art.

There are, however, exclusions from these anti-abuse provisions like gifts received from blood relatives, property received under a will or inheritance, or on total or partial partition of a Hindu undivided family. While principally, these provisions are designed to prohibit transfer of properties which are disguised as gifts or to prevent tax evasion through undervalued transfers of existing property and accordingly tax is on the recipient treat-



ing transfer price of the property to be equal to the FMV.

Since provisions are widely worded with limited exclusions therefrom, they are misapplied even in case of genuine transactions where taxing the recipient on FMV defeats the objective for which the provisions were introduced. In the absence of specific exclusion, transfer of properties among family members pursuant to a settlement attracts rigours of these anti-abuse provisions.

Suggestions for government: Family settlement is essentially just realignment of ownership among members, who have antecedent rights in those assets. However, in the absence of an express concession of a family settlement from anti-abuse provi-

sion, one relies on judgments that are beyond prescriptive laws.

This is potentially fraught with risks, and prevents families to smoothly settle. To secure tax neutrality for such settlements, it is imperative to advocate for the formal exclusion of family settlements from tax obligations through proactive engagement and legislative clarity. This strategic initiative aims to uphold integrity and significance of family arrangement within legal frame-

works while promoting clarity and fairness in taxation policies. The government must explicitly ensure transactions under a family settlement agreement should not be subjected to anti-abuse provisions., and gift of properties even between extended family members will also not be taxed.

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Therefore, acquiring shares in family-owned business through fresh issu-

ances to realign ownership must also be excluded from the rigours of anti-abuse provisions. In conclusion, the said provision was introduced to prevent misuse of gifts for tax evasion. However, family settlements, recognised by courts as legitimate ways to manage familial affairs, such as equitable asset distribution among family members or compliance with specific contractual terms, should not be subject to fetters of valuation hurdles. Such hurdles were aimed to prevent tax avoidance schemes, not to penalise legitimate and bona fide arrangements.

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