Paper 3: Taxation of Corporate Gifts

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Provisions of TOPA related to gifts

- **Section 5 of Transfer of Property Act,1882 defines 'gift' as "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"**
- **Section 5 further clarifies that "In this section "living person" includes a company or association or body of individuals, whether incorporated or not..."**
- **Section 122 of TOPA:"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 donee, and accepted by or on behalf of the donee**
- **The word 'gift' need not appear in the gift for the transaction to be considered as 'gift'[*Ultima Search v ACIT*(2016)75taxmann.com205(Mumbai-Trib)**

Mode of gifting-section 123 of TOPA

- ***Gift of Immovable property*:transfer must be effected by a registered instrument signed by or on behalf of the donor, and attested by at least two witnesses.**
- ***Gift of movable property*:the transfer may be effected either by a registered instrument signed as aforesaid or by delivery.**

Note:In case of shares, transfer must be as per the provisions of Companies Act,2013

Whether a company can give or receive gifts?

M/s Direct Media Distribution Ventures Private Limited v Principal Commissioner of Income Tax (ITA No: 2211/Mum/2019)

- **There is nothing in law which stops corporates from making a gift of shares to each other, more so when the intention of the parties is supported by an internal restructuring exercise, which was driven by commercial reasons**

***Jayneer infrapower & Multiventures (P.) Ltd. v. Deputy Commissioner of Income-tax, Mumbai* [2019] 103 taxmann.com 118 (Mumbai - Trib.)**

- **There is no requirement in TOP Act that a 'gift' can be made only between natural persons out of natural love and affection**
- **As long as a donor company is permitted by its memorandum/articles of association to make a 'gift', it can do so**
- **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**

Whether a company can give or receive gifts?

<u>Chennai Tribunal in the case *Redington (India) Ltd. v. JCIT [2014] 49 taxmann.com 146*</u>

- **There is nothing against a company making gift of its property to another company.**
- **There is nothing anywhere in law, which prescribes that only natural persons can make gift on the ground of 'love and affection'.**
- **Therefore, a corporate body can make a gift.**
- **(Above case involved transfer of shares without consideration by co to its step-down WoS in Cayman Island)**

<u>*Prakriya Pharmacem v ITO*[2016]66taxmann.com 149(Guj)</u>

- **Assessee company gifted shares to its sister company**
- **It was held that section 45 (capital gains) would not be attracted as this is a gift and would attract section 47(iii)**

<u>*Deere & Co ,In re* [2011]11taxmann.com388(AAR)</u>

- **With intent to restructure its operations, JDA transferred without condideration its entire shareholding in JDIPL to JDA Singapore.This was held to be a gift and in absence of any income(capital gains) accruing, it was held that Transfer Pricing provisions also cannot be invoked. <u>(Now of course, this will be taxed u/s 56(2)(x)</u>**

Donee-based taxation of gifts[Section 56(2)(x)]

Where *any person* receives,in any previous year,from any person or persons:

- **Sum of money without consideration[Section 56(2)(x)(a)]**
- **Immovable property without consideration[Section 56(2)(x)(b)(A)]**
- **Immovable property for a consideration< Stamp Duty Value[Section 56(2)(x)(b)(B)]**
- **Specified movable property without consideration[Section 56(2)(x)(c)(A)]**
  - **shares and securities;**
  - **jewellery;**
  - **archaeological collections;**
  - **drawings;**
  - **paintings;**
  - **sculptures;**
  - **any work of art; or**
  - **bullion**
- **Specified movable property for a consideration< Fair Market Value[Section 56(2)(x)(c)(B)]**

Threshold limit of Rs.50,000 applies category-wise

- (a) Sums of money received without consideration in a previous year if the aggregate of such sums received exceed Rs. 50,000.
- (b)Immovable property received without consideration in a previous year where the stamp duty value of such property exceeds Rs. 50,000.
- (c)Immovable property received for consideration where (i) SDV exceeds 110% of consideration and (ii) such excess >Rs.50,000
- (d)Aggregate of items of specified movable property (shares and securities, jewellery, archaeological collections, paintings, drawings, sculptures, any work of art and bullion) received without consideration in a previous year if the aggregate FMV of such items received exceed Rs. 50,000.
- (e)Aggregate of items of specified movable property received in a previous year whose fair market value is more than the consideration given and where the difference aggregates to more than Rs. 50,000.

Gifts received which are tax-exempt in the hands of a co

- Receipt of money or property by a company from its 100% subsidiary which satisfies conditions of section 47(iv)
- Receipt of money or property by a 100% subsidiary from its parent company which satisfies conditions of section 47(v)
- Any transfer of capital asset in a scheme of amalgamation where amalgamated co. is Indian co. [Section 47(vi)]
- Receipt of shares by the amalgamated foreign company in a transaction covered by section 47(via)
- Any transfer of capital asset by banking company to banking institution in a scheme of amalgamation [Section 47(viaa)]
- Transfer,in a demerger,of a capital asset by the demerged co to the resulting co,where the resulting co is an Indian Co [Section 47(vib)]
- Receipt of shares by the resulting foreign company in a transaction covered by section 47(vic)
- Receipt of shares in a scheme of demerger - Section 47(vid)
- Receipt of shares in a scheme of amalgamation - Section 47(vii)
- Transfer, in relocation, of a capital asset by the original fund to the resulting fund [Section 47(viiac)]

The phrase 'receives ..... any sum of money, without consideration' [section 56(2)(x)(a)]

- **The term 'consideration' is neither prefixed by the word 'adequate' nor it is suffixed by the words 'money or money's worth'.Hence, if in any transaction there exists consideration as per the provisions of the Indian Contract Act, 1872, such transaction would not come into the ambit of section 56(2)(x)(a)[*Chandrakant H. Shah v. ITO* [2009] 28 SOT 315 (Mum.)]**
- **<u>Is interest-free loan received liable to be treated as sum of money received without consideration?</u>**
- **No...*Chandrakant H. Shah v. ITO*:the assessee has gained by way of interest-free loan and the lenders have suffered by giving interest-free loans & such suffering has got some value.Therefore, the said transaction cannot be said to be without consideration**
- **The consideration in an interest-free loan is to return the money.The detriment suffered by lender in parting with use of funds is valid consideration to support promise of repayment by the borrower. [Hon'ble Delhi High Court in *CIT v. Mridu Hari Dalmia*[1982]8Taxman138/133 ITR 550]**

Whether waiver of loan by bank is taxable as gift u/s 56(2)(x)(a)

- <u>**Jai Pal Gaba v.Income-tax Officer, Ward-III (2),Ludhiana [2019] 108 taxmann.com 494 (Chandigarh - Trib.)**</u>
- **Assessee owed loan and interest to bank Rs. 5.74 crores which became NPA**
- **Subsequently, in one time settlement(OTS) programme bank settled whole debt at Rs. 1.40 crores, thus, waived loan amount of Rs. 4.34 crores**
- **Whether waiver of Rs. 4.34 crores is taxable as sum received without consideration?**
- ***Held:* Admittedly, the loan was advanced by the banker for a consideration of interest. Advancement of loan cannot be said to be without consideration. However, later on due to losses, the loan become NPA. The bank, after considering the remote possibility of recovery of the said loan, thought it prudent to go for OTS.It was not a simple case of waiver without consideration,rather, the consideration of the waiver was the condition of depositing immediately the remaining part of the loan i.e. Rs. 140 lakhs.<u>It is not just a case where the bank had simply waived or remitted the loan amount,rather the bank to secure payment of Rs. 140 lakhs, which otherwise the bank was feeling difficult to recover, was the consideration for settlement of the loan account.</u> Hence,the amount received by the assessee as waiver cannot be said to be without consideration**

Whether waiver of loan by bank is taxable as gift u/s 56(2)(x)(a)

- **The decision must be read cautiously.**
- **One cannot jump to conclusion that every loan waiver will not be taxed u/s 56(2)(x)(a)**
- **“Simply to say that the waiver of the loan amount does not constitute a receipt, in our view, will not be appropriate as it may lead to absurd, confusing and unintended interpretation. In our view, if the donor gives to a donee certain amount directly or indirectly it does not make a difference. To elaborate further, if the donor firstly, give some amount as a loan and then waive of or relinquish the right to recover the said amount, then, in our view, on the date of such remission or relinquishment, the nature of such loan changes from loan to receipt/gift. Any other interpretation given in this respect may be exploited to come out of and defeat the purpose of section 56(2)(vi) of the Act. “**

Limit of Rs.50,000

- If the aggregate of money gifts received in a financial year exceeds Rs. 50,000, the entire amount will be taxed and not merely the amount in excess of Rs. 50,000.
- Separate limits of Rs.50,000 apply for each category of 'gift'/'deemed gift' in section 56(2)(x)

Immovable property

- **Immovable property received being land or buildings or both received without consideration is taxable in the hands of the recipient provided it is capital asset to the recipient.**
- **In other words, immovable property received will not be taxed if it is :**
  - **(a)stock-in-trade of business or profession carried on by recipient; or**
  - **(b)rural agricultural land**

Rural agricultural land

- **Rural agricultural land is land situated in India which is not urban agricultural land.**
- **Urban agricultural land means agricultural land situated in India in—**
- **(A)any area within the jurisdiction of a municipality or a cantonment board and which has a population of not less than 10,000**
- **(B)any area within the distance, measured aerially (shortest aerial distance),**
  - **(i)not being more than 2 kilometres, from the local limits of any municipality or cantonment board which has a population of more than 10,000 but not exceeding 1,00,000; or**
  - **(ii)not being more than 6 kilometres, from the local limits of any municipality or cantonment board which has a population of more than 1,00,000 but not exceeding 10,00,000; or**
  - **(iii)not being more than 8 kilometres, from the local limits of any municipality or cantonment board has a population of more than 10,00,000**
- **The expression 'population' shall mean population according to the last preceding census of which the relevant figures have been published before the first day of the previous year.**

Date of receipt of immovable property

- Date of Registration?
- Or Date of possession?
- It appears that date of receipt of possession of immovable property is the date of receipt and not the date of signing the deed or registration thereof.
- In a landmark judgment in *Mysore Minerals Ltd. v. CIT* [1999] 106 Taxman 166, the Supreme Court held that to claim depreciation, it is not necessary that the assessee should be the registered owner of the assets. Exclusive possession rights, to exclude others from enjoyment of assets, right to retain possession and defend the same are some of the characteristics of ownership which would entitle the assessee to depreciation under section 32 (so long as it was used for carrying on business or profession).
- 'Prima facie, as a matter of ordinary English language, I think 'received' means actually get into their hands.' (Per Harvey J in Pilcher v. Logan (1914) 15 SR (NSW) 24 at 27)
- The Compact Oxford Dictionary gives the following definitions of 'receive'.
- verb 1 be given, presented with, or paid 2 accept or take delivery of.

Property other than immovable property

- **shares and securities**
- **jewellery**
- **artistic work-i.e. archaeological collections, drawings, paintings, sculpture or works of art**
- **bullion**

Date of receipt of shares & securities

- **Listed shares & securities:date of receipt of credit of listed shares and securities in demat account**
- **Unlisted shares &securities:when the transferee receives the duly executed transfer deed and the relevant share certificate**

Whether allotment of bonus shares by a company to its shareholders will attract tax in shareholder's hands under section 56(2)(x)(c)

- *CIT v. Dalmia Investment Co. Ltd.* [1964] 52 ITR 567(SC): It cannot be said that bonus shares are a gift and are acquired for nothing
- Even section 55(2)(aa)(iiia) of the Act (which provides that cost of acquisition of bonus shares shall be treated as 'Nil') does not refer to the bonus shares as 'shares received without consideration'. It only considers bonus shares as 'additional financial asset allotted to the assessee without any payment and on the basis of holding any other financial asset'. Thus, bonus shares are shares received 'without payment' and not 'without consideration'.
- Where additional shares were allotted to all shareholders of company in proportion to existing shareholding of shareholder in company and after allotment of additional shares, shareholding percentage of assessee in company remained same and average value per share had also reduced and no gain had arisen in hands of assessee, provisions of section 56(2)(vii)(c) would not be applicable[*Deputy Commissioner of Income Tax, Circle-2, Jaipur v. Smt. Veena Goyal*[2020]119 taxmann.com362 (Jaipur - Trib.)]

Bonus shares

- **Mumbai Bench of ITAT in the case of Asstt. CIT v. Subhodh Menon [2019] 103 taxmann.com 15/175 ITD 449 have held that only when a higher than a proportionate allotment of fresh shares issued by a company is received by a shareholder, the provisions of section 56(2)(vii) get attracted**
- **Sudhir Menon HUF v. Asstt. CIT [2014] 45 taxmann.com 176/148 ITD 260:Mumbai ITAT following the Judgment of the Hon'ble Supreme Court in the case of Miss. Dhun Dadabhoy Kapadia v. CIT [1967] 63 ITR 651 (SC) and Hon'ble Bombay High Court in the case of H. Holck Larsen v. CIT [1972] 85 ITR 285 (Bom) held that as long as there is no disproportional allotment of shares, there was no scope for any property being received by the tax payer as there was only an apportionment of the value of the existing shareholder over a larger number of shares, no addition u/s 56(2)(vii)(c) of the Act would arise**

Whether allotment of rights shares by a company will attract tax in shareholder's hands under section 56(2)(x)(c)

- In Khoday Distilleries Ltd. v. CIT [2009] 176 Taxman 142, the Supreme Court held in the context of Gift-tax Act, 1958 that 'allotment' of rights shares by the company involves no transfer and therefore is not a 'gift'

Thank You