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Gift Taxation in India: Reforms and Loopholes

Dr. Kiran Kumar M[1], Reshma M[2], Manoj Hegde N[3], H L Sharadhi[4]

Assistant Professor, Department of Finance, Faculty of Management Studies, CMS Business School, Jain (Deemed to be University) Bengaluru, Karnataka, India[1]

MBA Finance Students, Faculty of Management Studies, CMS Business School, Jain (Deemed to be University) Bengaluru, Karnataka, India[2,3&4]

ABSTRACT: Gift taxation in India is an important revenue measure that governs wealth transfers and prevents tax evasion. Loopholes in the existing system, however, allow individuals to legally avoid taxation by using family trusts, asset transfers, and strategic gifting. This research assesses public awareness, gaps in the existing system, and the need for reforms in India's gift tax system. Survey results indicate that a large percentage of the population lacks adequate knowledge of gift tax legislation, resulting in non-compliance. Most respondents cited loopholes that allow tax evasion, and this calls for enhanced enforcement and legislative reforms.

The results show that although gift taxation is intended to encourage financial openness, its efficacy is compromised by lack of uniform enforcement and regulatory loopholes. The research emphasizes the necessity for reforms like lowering exemptions, harmonizing tax rates, and raising penalties for non-compliance. More stringent tracking of high-value gifts such as cash, jewelry, and luxury goods can enhance compliance. Public awareness is also essential in making taxpayers aware of their responsibilities.

The study examines the impact of tax legislation on gifting behavior, with some making changes to their gifts in order to avoid taxation. There is widespread public support for reform, especially closing loopholes concerning family trusts and non-monetary transactions. With the growing frequency of wealth transfers in India, there is a need for a more organized and transparent tax system.

India's gift tax regime needs legislative changes, stronger enforcement, and public awareness programs. Reinforcing regulatory actions while educating taxpayers can help ensure that gift taxation serves its desired purposes. These observations offer useful suggestions to policymakers to develop a fairer and more efficient tax regime.

KEYWORDS: Gift Taxation, Tax Evasion, Wealth Transfer, Tax Reforms, India, Tax Compliance, Legal Loopholes, Public Awareness, Tax Policy, Enforcement Mechanisms

I. INTRODUCTION

In order to regulate the flow of wealth and ensure tax compliance, gift taxation is an important part of a country's financial system. With the abolition of the Gift Tax Act in 1998 and the later addition of provisions regarding gifts in the Income Tax Act, of 1961, India's gift taxes have undergone significant changes over time. There are still many legal loopholes for these advances, allowing individuals and institutions to exploit exemptions and avoid paying taxes. Government revenues lost as well as potential for abuse of tax concessions for money laundering and benami transactions are issues brought about by these loopholes in laws.

Key Clauses and Exclusions in Gift Taxation

Currently, gifts of money, property, and certain movable assets are considered taxable under the Income Tax Act under certain conditions.

The tax framework includes:

Gift Exemptions to Family Members: There are exemptions of certain family members, such as parents, brothers and sisters, and spouses, from tax charges on gifts offered to them. But individuals often make use of this exemption by shifting enormous sums within family arrangements for the purpose of avoiding taxes.

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Inheritance and Marriage Exemptions: Gifts made in the wake of an inheritance or at a wedding ceremony are not subject to tax. This provision is common sense in theory, but has been exploited for the purpose of passing unreported funds in the form of sham inheritance claims or wedding gifts.

Threshold for Taxation: The entire value of gifts from non-relatives is taxable if their total value exceeds ₹50,000 during a fiscal year. To escape taxes, taxpayers often split gifts among multiple recipients or strategically structure transactions to remain below this threshold.

Gift of Immovable Property: The difference between the stamp duty value and any consideration paid is taxable if the immovable property is received as a gift and its stamp duty value is more than ₹50,000. Nonetheless, undervaluing real estate and making false claims in real estate transactions. Legal Gaps in the Taxation of Gifts Despite these clauses being present, there are still a number of legal loopholes that enable individuals to evade taxes.

Some of the most important shortcomings are:

Several Transactions to Remain Under the Threshold: To evade tax, most individuals split large gifts into smaller amounts and donate them to a number of recipients or over various fiscal years since only non-relative donations exceeding ₹50,000 are taxable.

Benami Transactions: To prevent property from being retained in the name of a benamidar (proxy), the Benami Transactions (Prohibition) Act, 1988, was enacted. However, individuals may use close friends to retain assets in their names but conceal them as gifts owing to enforcement lacunas.

Abuse of Charitable and Religious Contributions: Certain taxpayers make charitable or religious contributions in money through churches or charities and claim such as voluntary contributions that are tax-exempt only to receive the money back in some other form.

False Marriage Gifts and Inheritances: Individuals can invent enormous amounts as wedding gifts or inherited wealth to justify unreported money since gifts received at marriage or as an inheritance are exempt from tax.

Valuation Manipulation in Real Estate: In an effort to reduce their tax burden, taxpayers often understate the value of gifts of immovable property, and this results in the government losing revenue.

II. RESEARCH OBJECTIVES

1. To evaluate the efficiency of the current gift tax regime in India through the examination of public awareness, rates of compliance, and the effectiveness of exemptions.
2. To determine the key loopholes in India's gift tax regime, such as the abuse of family trusts, asset-based gifting, and tax evasion schemes.
3. To recommend policy changes and enforcement actions that can increase transparency, reduce tax evasion, and enhance the overall effectiveness of the gift tax system in India.

III. REVIEW OF LITERATURE

Rao, M. G. (2021 There have been major changes in tax systems in several countries over the last two decades for a variety of reasons. The objective of this paper is to analyse the evolution of the tax system in India since the early 1990s. The paper describes and assesses the introduction of new forms of direct and indirect taxes, their revenue and equity implications, and the successes achieved in their implementation. The paper concludes that after eight years of reform, improving the tax system remains a major challenge in India.

Rao, M. G. (2023, July) This paper analyzes India's tax policy, highlighting its low revenue productivity. Key issues include the fragmented tax assignment between Union and State governments, leading to income tax avoidance; multiple objectives causing excessive exemptions and distortions; ad hoc taxation of easily accessible sectors; difficulty taxing the unorganized sector; multinational tax abuse via base erosion and profit shifting; and weak administrative capacity. Political resistance to reforms, termed the "tyranny of status quo," further impedes progress, explaining the slow and ineffective nature of tax reforms in India.

Rao, M. G., & Rao, R. K. (2021) Global tax systems have seen significant reforms in the last two decades, driven by diverse factors. Developing nations faced fiscal imbalances, using tax policy for budgetary correction. Transitioning

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economies needed tax reforms to replace public enterprise profits and align with market-driven strategies. Globalization pushed for tariff reductions, requiring new revenue sources, and emphasized minimizing tax system costs. The supply-side reforms of the Thatcher-Reagan era also influenced developing countries. These reforms aimed to adapt tax systems to changing economic landscapes and enhance efficiency.

Jain, P. (2023) This paper examines India's taxation within a broader South-East Asian context. As a large, developing federal republic with high GDP growth, India faces fiscal challenges, including a structurally imbalanced budget and high public debt. Public spending prioritizes general services over welfare. The tax system, resembling an "early stage" Musgravian model, relies heavily on complex indirect taxes, hindering VAT implementation. Direct taxes are underdeveloped, and import duties remain significant. Social contributions are absent. Key issues include obsolete indirect taxation and intergovernmental fiscal relations. Tax reforms, initiated in the 1990s, are ongoing, with VAT implementation being a crucial step.

Shome, P., & Shome, P. (2021)India's landmark Goods & Services Tax (GST), implemented in 2017, aimed to unify indirect taxes, boost GDP, and reduce evasion. Delayed by political issues, GST consolidated taxes like Excise, VAT, and Service Tax into a consumption-based VAT with input tax credits. This paper analyzes the proposed GST framework against the previous system, highlighting its impact on employment and various sectors. It focuses on revealing the complexities of the prior regime, addressing issues like tax multiplicity and cascading effects, and comparing the merits and demerits of both systems

IV. RESEARCH METHODOLOGY

Data Collection:
Primary data was collected using Google Forms. The survey consisted of multiple-choice questions to evaluate the respondents' views on loopholes in gift taxation and its reforms. The majority of respondents belonged to the age group of 18-34 with varied incomes

Sampling Techniques:
A convenience sampling approach was used to select participants. The survey link was distributed via email and social media platforms, targeting taxpayers. Participation was voluntary, and respondents were either working professionals or business owners to ensure relevant data collection.

V. DATA VISULAZATION & INTERPRETATION

CATEGORY	COUNT	PRECENTAGE
INCOME LEVEL(ANNUAL)		
BELOW 2 LAKHS	6	13.6%
2 LAKH- 5 LAKHS	14	31.8%
5 LAKH- 10 LAKH	7	15.9%
10 LAKH & ABOVE	11	25%
PREFER NOT TO SAY	6	13.6%
GIFT TAX AWARENESS		
YES	21	47.7%
NO	11	25%
SOMEWHAT	12	27.3%
AVOID GIFT TAX		
USING FAMILY TRUSTS	17	38.6%
STRUCTURING GIFTS BELOW TAXABLE THRESHOLDS	22	50%
GIFTING ASSETS INSTEAD OF CASH	28	63.6%
EXPLOITING JURISDICTIONAL DIFFERENCES	10	22.7%

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INTERPRETATION

• The findings indicate that there are loopholes within India's gift taxation system, especially concerning family trusts and non-cash transfers.
• Gaps in awareness imply that numerous individuals might unintentionally breach or bypass gift tax regulations, highlighting the need for improved public education.
• Legal methods of tax avoidance (trusts, asset transfers) underscore the necessity for more rigorous regulations and monitoring systems.
• The public's backing for reforms, such as heightened penalties and tighter enforcement, indicates that policy modifications would likely be embraced if executed effectively.
• Given that cash and luxury goods are the most frequently gifted assets, tax authorities might contemplate

HYPOTHESIS

- **Null Hypothesis (H_0):** Awareness of gift taxation laws is independent of income level.
- **Alternative Hypothesis (H_1):** Awareness of gift taxation laws is dependent on income level.

Data Analysis

1) Chi square test

Relationship	Test Statistic (χ^2)	Degrees of Freedom	p-value	Interpretation
Income Level and Gift Tax Awareness	10.80	8	0.213	Not Significant

The chi-square test indicates no statistically significant relationship between income levels and awareness of gift taxation laws ($p = 0.213 > 0.05$). Since the p-value (0.2135) is greater than the typical significance level of 0.05, we fail to reject the null hypothesis (H_0). Therefore, based on the data, we conclude that there is no significant relationship between income level and awareness of gift taxation laws.
The analysis suggests that awareness of gift taxation laws does not significantly depend on income level in this sample. It indicates that individuals across different income levels exhibit similar levels of understanding about gift taxation laws.

2) Correlation analysis

Relationship	Correlation Coefficient (ρ)	p-value	Interpretation
Income and Gift Tax Awareness	0.194	0.207	Weak, Not Significant

The Spearman correlation coefficient ($\rho = 0.194$) suggests a **weak positive relationship** between income and gift tax awareness — meaning that as income increases, there is a slight tendency for gift tax awareness to increase as well. However, the **p-value of 0.207** indicates that this relationship is **not statistically significant** at conventional levels (typically $p < 0.05$).
This means we **cannot confidently conclude** that there is a real association between income and gift tax awareness in the population based on this sample. The observed correlation might have occurred by chance.

3) Regression Analysis

Relationship	Coefficient	p-value	Interpretation
Intercept	-0.8128	0.0986	Not Significant
Income Code → Awareness	0.4456	0.0566	Marginally Significant ($p \sim 0.05$)
Model LLR (Chi^2)	—	0.0468	Model fit is statistically significant
Pseudo R^2	0.065	—	Indicates low explanatory power (6.5%)

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The logistic regression model indicates a **marginally significant relationship** between income and gift tax awareness (coefficient = 0.4456, p = 0.0566), suggesting that higher income levels may be associated with increased awareness, though the evidence is not strong enough to confirm this with high confidence (just above the conventional $p < 0.05$ threshold).

The **intercept** is not statistically significant (p = 0.0986), implying no strong baseline effect when income is zero (though its interpretive value is limited in this context).
The **model's overall fit** is statistically significant, as indicated by the **Likelihood Ratio Chi-square test** (p = 0.0468), suggesting that the predictors improve the model compared to a null model.

However, the **Pseudo R^2 of 0.065** reveals that the model accounts for only **6.5% of the variation** in awareness. This indicates **low explanatory power**, meaning other important factors likely influence awareness beyond income.

VI. CONCLUSION

Gift taxation is a key wealth transfer control tool and tax evasion stopper in India. However, the findings indicate that a considerable segment of the population is not well aware of the gift tax laws, which could lead to inadvertent non-compliance. The report highlights existing legal loopholes that enable individuals to legally evade taxes through techniques such as asset-based giving and family trusts.

Enhanced information efforts and more stringent enforcement of tax legislation could significantly raise compliance levels. Based on the findings, most individuals are willing to comply with tax laws if they know what is expected of them. Thus, to enhance the effectiveness of gift taxation in India, a comprehensive approach involving legislative reforms, education campaigns, and monitoring systems is required.

Also, since the most common items of gift being money, jewelry, and luxury items, the government should consider instituting additional monitoring procedures for large values. In order to enhance accountability and transparency, this can include mandatory reporting requirements for gifts over a certain value.

In summary, gift taxation is an effective tool in India's tax system, but currently, legal defects, public unawareness, and unequal enforcement are weakening its effectiveness. A more robust and equitable tax system should be established by correcting these problems with well-planned policy reforms and increased public involvement, ensuring that gift taxation serves its intended purpose.

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