

Division of Family Trusts May Now Face Capital Gains Tax

Fear of higher tax has put on hold several families' plans for a split

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Mumbai: A Budget proposal has forced two siblings to rethink their decision to split their real estate family business. The Mumbai-based brothers are worried that transferring assets from their family trust and transferring and swapping shares from their unlisted companies could now attract tax which, as per the budget proposal, will be anywhere between 20% and 30% if done below a fair market value. They have now approached lawyers and advisors to know the real impact.

"The Budget proposal has created an issue for family settlement wherein if the shares of a private company are owned by a family trust and are transferred to a beneficiary at a value lower than fair market value. The family trust shall be obliged to pay tax on the differential amount bet-

ween fair market value and the value at which such shares were transferred," said Hemal Mehta, partner, Deloitte Haskins & Sells.

According to experts, in a family settlement, shares are always transferred at a lower value. This would create problem for families that are looking to divide business or split family wealth.

"Any transfer of unquoted equity shares at a price lower than the fair market value will only seek to shift the tax burden from the recipient/transferee (under Section 56(2) (VIA)) to the transferor," said Prem Rajani, managing partner, Rajani Associates.

Industry insiders say that the fear of tax has put on hold several families' plans of a split. For instance, the grandchildren of a Kolkata-based patriarch have put on hold their plan to split the assets,

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including a listed and an unlisted company, after the February 1 budget announcement.

Legal experts say there are court judgments where it has been clarified that there can be no tax on family divisions, but it's not part of the law. So, the budget announcement may override these earlier judgments. Also, the court judg-

ments speak only about division of wealth between 'first degree' of blood relatives, so cousins fighting for grandparent's property will anyway have to pay capital gains.

Industry trackers say this will also lead to many families taking a relook at their family trust structures. Experts point out that two types of trusts are being created or restructured—the first is by young entrepreneurs who have made millions through start-ups for effective wealth management and succession planning, and the second type is by the traditionally rich, mostly those who are growing old and may not be able to manage their assets and investments, both in India and overseas.

Experts say that in certain cases capital gains tax may also be applied to family trusts.

"In case of settlement of family trust, where shares are transferred to the trust and if STT is not paid at that time and now, or subsequently, any family split happens, then it may trigger the payment of capital gains tax, although there are certain grey areas and needs clarifications," said Vishwas Pathak, director, Universal Trustees, a firm that specialises in managing family and corporate trusts.

