REINTRODUCING INHERITANCE TAX IN INDIA: A PATH TO WEALTH REDISTRIBUTION

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1. ABSTRACT

The fact that nearly 40.6% of India's wealth is held by only 1% of the population in the nation shows the deep and widening inequality in the nation.[1] A recent study by Oxfam India showed that, with a population of over 1.4 billion, the bottom 50% of the population holds less than 3% of the nation's wealth.[2] Figures like this clearly point out the unequal concentration of wealth in the nation and calls for a need to adopt better methods of redistribution of wealth. One way of achieving this might be by making necessary changes in the taxation system in our nation, more specifically, through the reintroduction of Inheritance Tax. Historically, India did have an inheritance tax under the Estate Duty Act of 1953, which was later abolished in 1985 due to administrative inefficiencies. The meager income of 2 crore that it generated was not considered significant enough.[3] But changing times have once again sparked light on the need to implement it. This paper will analyze the implications and objectives of inheritance tax, followed by an assessment from the constitutional and economic point of view. It will then look into an analysis of nations such as Japan and South Korea where this system is still in place. Lastly, the paper will conclude by analyzing the pros and cons of whether Inheritance Tax must be reintroduced in India.

[1] Oxfam India, *Survival of the Richest: The India Story*, The India Supplement 2023, 7, https://d1ns4ht6ytuzzo.cloudfront.net/oxfamdata/oxfamdatapublic/2023-01/India%20Supplement%202023_digital.pdf?kz3wav0jbhJdvkJ.fK1rj1k1_5ap9FhQ.

[2] *Id.* at 8.

[3] Divyam Sharma, *India Had Its Own Inheritance Tax Till 1985. Why It Was Abolished*, NDTV (Jun. 4, 2024, 6:31 PM), https://www.ndtv.com/india-news/india-had-its-own-inheritance-tax-till-1985-why-it-was-abolished-5514552.

2. INTRODUCTION

Inheritance tax is a form of a tax which is imposed on the recipients by the state, which is particularly imposed on the assets or property inherited from a deceased person. This tax can reach rates as high as 55%, depending on the country. Inheritance can be received either through a will or under the deceased's personal law.[4]

To calculate inheritance tax, the first step is to ascertain the total value of the deceased's assets, including investments, real estate, and other property, while accounting for any arrears and liabilities. An inheritance tax is imposed on that portion of the inheritance that exceeds a specified exemption amount. Beyond this threshold, the tax is typically calculated on a graduated scale. For example, if a state imposes an inheritance tax on assets exceeding $200,000 and you inherit $275,000, you must pay taxes on $75,000. With a tax rate of 15%, the inheritance tax due would be $11,250. ($75,000 x 0.15)

The threshold amount and the tax rate depend more on the relationship between the deceased and the inheritor rather than on the value of the assets inherited. Generally, the closer the familial relationship of the inheritor to the deceased, the higher the threshold and the lower the tax rate that is levied. Inheritance tax ensures that the successive generations are not unfairly enriched by the wealth accumulated by their predecessors, henceforth promoting a more equitable distribution of wealth across society.[5] India currently does not impose an inheritance tax.

3. HISTORY OF INHERITANCE TAX IN INDIA

3.1 Emergence

The concept of inheritance, while favorable in a number of aspects, has a chance of being fundamentally harmful to many due to unequal access to resources at birth. As a concept on its own, many proponents have put forward a system whereby the rest of society benefits from one’s inheritance. Inheritance tax has been applied in India previously in terms of estate duty which also went by the term “death tax.” Even though India is among the countries where inheritance tax is not currently enforced, it was previously implemented as estate duty under the Estate Duty Act of 1953.[6]

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[4] Janet Berry-Johnson, *Inheritance Tax: What It Is, How It's Calculated, and Who Pays It*, INVESTOPEDIA (Jun. 4, 2024, 5:27 PM), https://www.investopedia.com/terms/i/inheritancetax.asp.
[5] *Id.*
[6] Estate Duty Act, 1953, No. 34, Acts of Parliament, 1953 (India).

3.2 Abolishment

However this act was repealed by finance minister V.P. Singh, who claimed that it had not succeeded in promoting social equality or closing the wealth gap. In addition, the laws had different calculation standards for various kinds of property, which made them complicated and led to protracted legal disputes over property value and high administrative expenses. As many people looked for ways to avoid paying the inheritance tax, such as hiding inherited properties and taking part in benami property transactions, collections from the levy remained low.[7] Various countries have also stayed the imposition of inheritance tax, where it has faced backlash but has withstood the same. The main purpose behind it was to reduce social inequalities. It was hoped to cause a big enough change on the economic cycle, but the underlying notion is that the state deserves a portion or cut from your property which was resentful enough.

4. CONSTITUTIONAL PERSPECTIVE

4.1 Constitutional provisions

The Indian Constitution provides the framework for levying inheritance tax through specific entries in its Schedules. The power to levy estate duty was derived from Entry 88 of List I (Union List) in the Seventh Schedule of the Indian Constitution. This entry reads: *"Estate duty in respect of property other than agricultural land."*[8] This placed the power to levy inheritance tax squarely with the central government. The constitution however, made a distinction between agricultural and non-agricultural land. Entry 48 in List II (State List) gives states the power to levy *"Estate duty in respect of agricultural land."*[9] This dual structure reflects India's predominantly agrarian economy at the time and the constitutional framers desire to give states control over agricultural matters.

Article 38 directs the state to *"promote the welfare of the people by securing... a social order in which justice, social, economic and political, shall inform all the institutions of national life."*[10] While Article 39(c) directs that *"the operation of the economic system does not result in the concentration of wealth... to the common detriment."*[11] Therefore an estate tax aligns

[7] *supra* note 3.
[8] INDIA CONST. VII schedule, List I, Entry 88.
[9] INDIA CONST. VII schedule, List II, Entry 48.
[10] INDIA CONST. art. 38.
[11] NDIA CONST. art. 39, § c.

with these principles by redistributing wealth and preventing its concentration.

4.2 Inheritance tax and Article 14

Article 14 - Equality before law[12] permits reasonable classification for taxation purposes. The Supreme Court in several cases has held that a law can make reasonable classifications if:

a. The classification is based on intelligible differentia.
b. The differentia has a rational relation to the object of the Act.[13]

The Estate Duty Act made distinctions based on:

a. Value of the estate (higher value, higher tax)
b. Relationship to the deceased (closer relatives got more exemptions)
c. Type of property (agricultural vs. non-agricultural)

These classifications were deemed reasonable and rationally related to the Act's objectives of reducing wealth inequality and raising revenue.

It can be established that abolishing the tax favored the wealthy, allowing them to pass on untaxed wealth. After the abolition of the tax in 1985, some have argued that the absence of inheritance tax violates Article 14. Taxing income from work while not taxing inherited wealth discriminates against those who earn their wealth, favoring those who inherit it. Allowing untaxed inheritance perpetuates and aggravates wealth inequality over generations, undermining the "equality of opportunity" that Article 14 seeks to protect. A significant Article 14 issue was the wide discretion given to tax officials in valuing estates. This led to allegations of arbitrary and unequal treatment, with similar properties valued differently.

India's history with inheritance tax shows the changing views on Article 14. At first, the tax was considered fair and in line with equality principles. When it was abolished, opinions were divided - some praised the move, while others criticized it in the context of Article 14. Even now, the lack of inheritance tax sparks debate about equality. This highlights that in taxation, equality involves balancing economic goals, fairness in administration, and social justice.

5. ECONOMIC EFFECTS

Coming to the impact of Inheritance tax on the economy, here is some factual data to give a background. India currently is a $3.5 trillion economy standing in the 5th place globally, and

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[12] NDIA CONST. art. 14.
[13] State of West Bengal v. Anwar Ali Sarkar, AIR 1952 SC 75.

has generated a GDP of Rs. 272.41 lakh crore in nominal terms, showcasing a significant economic performance in the past few decades.[14] In spite of the growth, India's poverty is ranked 96th of the 195 countries on the World Population Review.[15] Around 44.8% of the population gets a salary of around $3.65 a day, and overall the poverty rate is 21.9%.[16] This data shows India still has a long way to go and a factor which might aid in reaching the desired goal is by redistributing the accumulated wealth.

A report published by the World Bank in 2022, highlights that a progressive tax system would be a vital and an essential solution for the betterment of the economy and the report also states people are more willing to pay taxes in a progressive system as it enhances tax compliance and revenue generation. Along with this, the data also shows that direct taxes have reduced the economic inequality as seen in nations like the United States and Luxembourg than in nations like Vietnam and Togo.[17]

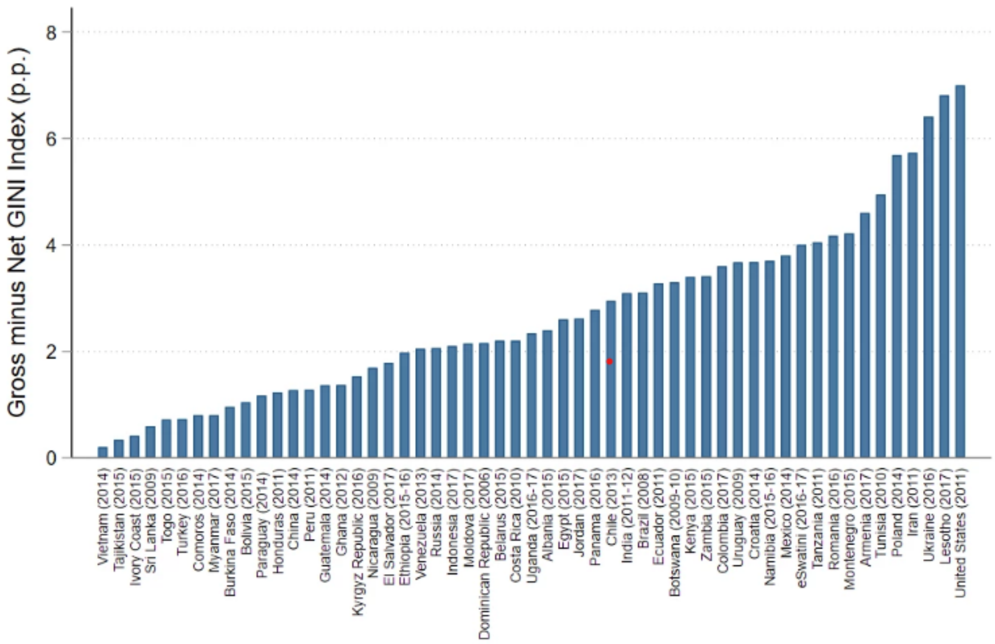

Image 1 - Graph of how progressive taxation and transfers reduce income inequality[18]

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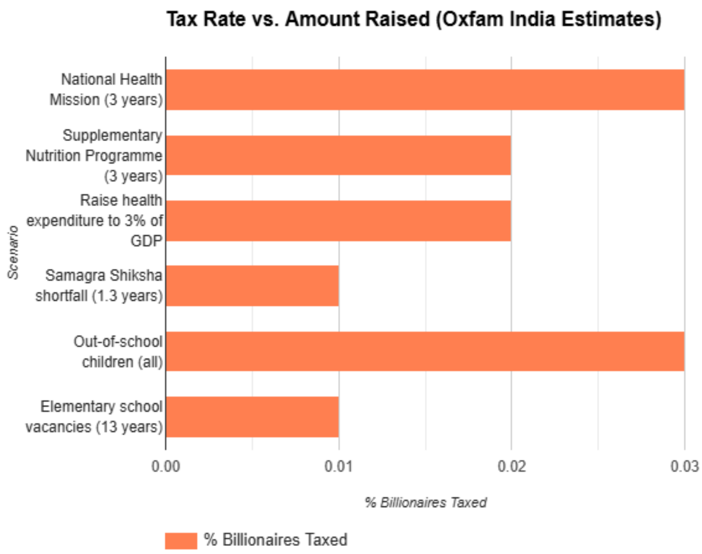
[14] Ministry of Statistics & Programme Implementation, *ESTIMATES OF GROSS DOMESTIC PRODUCT FOR THE SECOND QUARTER (JULY-SEPTEMBER) OF 2023-24*, PIB (Jun. 3, 2024, 11:36 AM), https://pib.gov.in/PressReleasePage.aspx?PRID=1981170.
[15] World Population Review, *Poverty Rate by Country 2024,* https://worldpopulationreview.com/country-rankings/poverty-rate-by-country (last visited Jun. 5, 2024).
[16] *Id.*
[17] Christopher Hoy & Chiara Bronchi, *Why does the progressivity of taxes matter?*, WORLD BANK BLOGS (Jun. 4, 2024, 6:54 PM), https://blogs.worldbank.org/en/governance/why-does-progressivity-taxes-matter.
[18] *Id.*

The above graph depicts and shows the difference between gross income inequality (before taxes and transfers) and net income inequality (after taxes and transfers) across various countries. Countries with a larger gap between the gross and net GINI index effectively use progressive taxation to reduce income inequality. This data is evidence of the fact that Progressive taxes are one of the factors towards a successful economy.



'Survival of the Richest', a recent survey conducted by Oxfam, stated the need to tax the rich and go for a more progressive taxation system in the nation.[19] A progressive tax system is known for its ability to reduce income inequality and enhance the likelihood of implementing countercyclical fiscal policies, which will drastically improve the economy and this is what we are looking for even in the present Indian economy as well.[20]

Based on the data presented below by Oxfam, it is evident that taxing the rich could be a highly effective solution for addressing several critical funding needs in India. This data clearly shows that even by minimally taxing the super rich, it won't make a huge difference to them, but can make a remarkable contribution to society.

Image - 2

The X axis depicts no. of billionaires taxed and the Y axis depicts how much their tax money can actually contribute to society.

[19] *supra* note 1.
[20] *supra* note 17.

For instance, the first bar shows that 3% of wealth tax on the Indian billionaires can fund the National Health Mission, the largest healthcare scheme in India with an allocation of INR 37,800 crores for 3 years.[21]

Similarly, there are other schemes and programs who's funding can be supported by taxing a nominal percentage on the ultra rich.

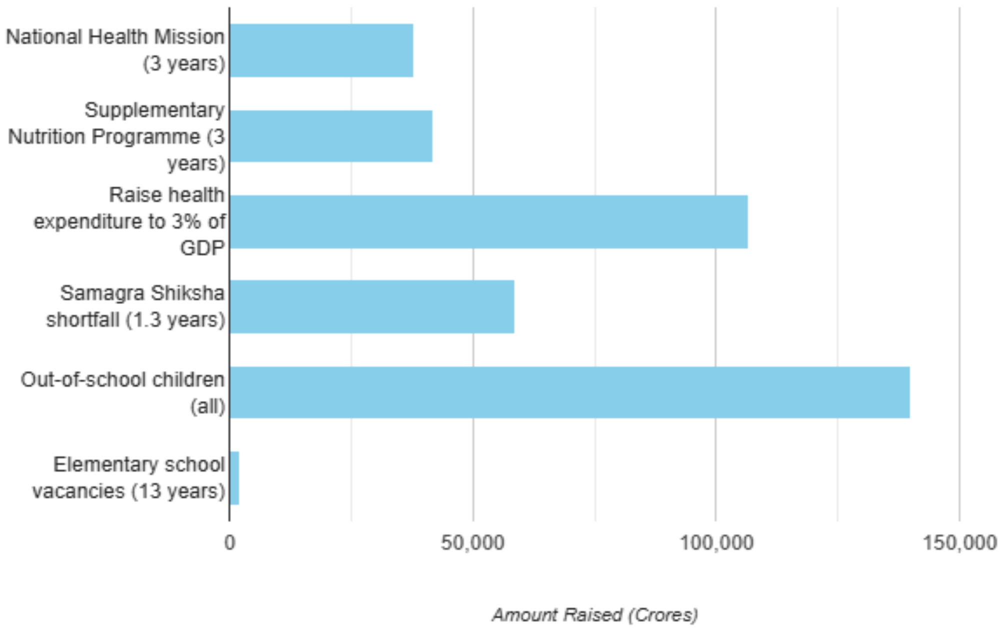


Image - 3

The X axis depicts the amount generated from the tax collected by billionaires, depicting how even such a small percentage, can make a huge contribution for a long time, correspondingly shown on the Y axis.

This data is another factor which proves that implementing inheritance tax in the present society can actually contribute a huge chunk to the system.

However, these taxes can also be a hurdle. While they may reduce wealth inequality, they could also discourage the wealthy from investing or diversifying their assets. This is because accumulating more wealth could simply mean a larger tax bill for their heirs. This disincentive to invest could potentially stifle economic growth.

[21] *supra* note 1, at 8.

6. CASE STUDIES

Let us analyze and understand the economic outcomes of Inheritance tax, by studying about its implications from case studies in other nations around the globe.

6.1 Japan

Japan, one of the largest economies in the world, is also known to impose an Inheritance tax - a record high of up to 55% of inheritance tax on the beneficiaries on inheriting any kind of assets.[22] This redistribution has helped in generating a significant amount of revenue for funding public services and social programs, that too in a nation with one of the highest old age population. This tax has helped in covering costs associated with healthcare, pensions and other services to support the elderly. The Inheritance tax has contributed to the overall fiscal growth of the government. During economic downturns, such as the prolonged recessions that Japan faced in the 1990s, inheritance tax revenue provided a buffer that helped maintain public spending levels without exacerbating the fiscal deficit.[23]

6.2 South Korea

But the other side of the story is seen in the case of South Korea. The maximum tax imposed in this nation is a whopping 50%, which seems to have promoted the majority of the Korean Chaebols to emigrate more.[24] Based on Henley & Partners survey, it is being said that South Korea can be ranked No.1 if the survey focused on the number of rich emigrants to the total population, indicating the high rates of emigration. Majority of the population is dissatisfied with the inheritance tax and are of the strong opinion to get it abolished.[25] Even though the revenue generated by the Inheritance tax in the nation has drastically increased in a decade to has high as 7.6 trillion won,[26] it is still seen as a hurdle by the business moguls. The hefty inheritance tax has become unavoidable, as evidenced by the Samsung heir embroiled in a bribery scandal, resulting in one of the largest global tax payments.[27] This is an indicator of the ramification of the Inheritance tax, if the nation doesn't take any further actions, then investors

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[22] Hiromitsu Ishi, *Effects Of Taxation On The Distribution Of Income And Wealth In Japan*, 21, HITOTSUBASHI JOURNAL OF ECONOMICS, 27, 27-47, 1980.
[23] *Id.*
[24] Yi Whan-woo, *High inheritance tax prompts more wealthy Koreans to emigrate*, KOREA TIMES (Jun. 4, 2024, 7:06 PM), https://www.koreatimes.co.kr/www/biz/2024/05/602_365692.html.
[25] *Id.*
[26] Statista, *Total revenue from inheritance taxes in South Korea from 2012 to 2022* (Jun. 4, 2024, 7:06 PM), https://www.statista.com/statistics/1231479/south-korea-inheritance-tax-revenue/.
[27] BBC, *Samsung heirs to pay record inheritance tax* (Jun. 4, 2024, 7:08 PM), https://www.bbc.com/news/business-56911094.

will reduce their expansions and investments, which might hit the country's economy in the long run.

6.3 The OECD nations

The Organisation for Economic Co-operation and Development, (OECD) is a group of 38 member nations who are committed to stimulate economic progress, trade, and policy coordination amongst these nations.[28] Of them, we have already discussed Japan and South Korea, but moving West, it is seen that the United States stands at the 4th place, with tax rates going as high as 40% tied along with the UK. But even such a high percentage seems to be doing no good, as the revenue generated from them Estate Taxes declined from $38 Billion in 2001 to $20 Billion in 2015.[29]

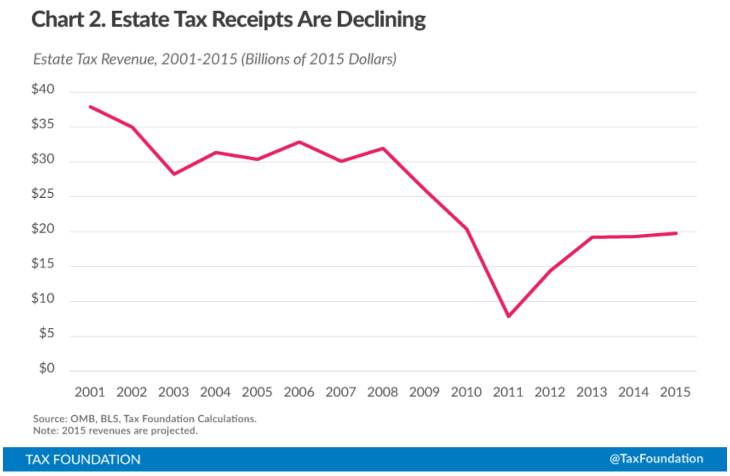

Image 4 - Graph of estate tax receipts declining[30]

But on the contrary, the last 15 nations in OECD do not levy any sort of taxes on property passed to lineal heirs and this list contains some of the richest nations like Luxembourg, Norway and Sweden. In fact eliminating Inheritance tax, turned out to be successful when in 2013, IKEA founder Ingvar Kamprad returned to his home country, who was away for 4 decades for tax reasons.[31]

7. LEARNINGS FOR INDIA

The above mentioned nations expose us to the bright and dark sides of Inheritance and Estate

[28] OECD, https://www.oecd.org/about/members-and-partners/ (last visited Jun. 5, 2024).
[29] Alan Cole, *Estate and Inheritance Taxes around the World,* TAX FOUNDATION (Jun. 4, 2024, 7:38 PM), https://taxfoundation.org/research/all/federal/estate-and-inheritance-taxes-around-world/.
[30] *Id.*
[31] *supra* note 30.

tax. Considering the high wealth inequality in India implementing an Inheritance tax on Uber rich seems to be a viable option. Also, it is seen that High Inheritance taxes motivate the rich to donate more into charity. Infact, the UK government provides a tax benefit, where If 10% or more of the estate is left to charity, the Inheritance tax rate drops from 40% to 36%. [32] Also it is seen that administration of these taxes is cost-effective when compared to other annual wealth taxes.[33] All in all with proper implementation and certain foolproof exemptions, this tax can be a great step in the progressive system.

An inference can be drawn from these nations that the economic gains from the implementation of Inheritance tax, is not cosmic in nature, but every penny does make a difference. Some factors, where India won't face the inaccuracies which were faced by the above nations are primarily that regarding cost of living. Since, India does not have a very high cost of living,[34] even a small contribution towards the state funds will actually make a significant difference supporting this argument are the survey reports mentioned above. As a result it can be said India can benefit from implementing an inheritance tax to address its issues.

However, careful consideration of tax rates and exemptions is crucial to avoid discouraging investment and prompting capital flight. A well-balanced inheritance tax can play a major and impactful role in India's economic landscape. The trend of ultra rich emigrating from South Korea in response to high taxes suggests that India too possibly can face a similar issue. It is necessary to implement this scheme without any flaws and loopholes.

While on the economic front, these taxes do not seem to be a game changer either, the meager revenue that they ended up generating in the West or the 0.5% that they have contributed to the revenue in the OECD nations,[35] makes this more of a liability than an asset.

Another major disadvantage from the enactment of this tax will be the lack of investment. If Investors are forced to pay a tax, once they meet a certain threshold, they will prevent reaching this level, by limiting their investment and by not expanding their business. This inturn will vigorously hit the economy. Additionally, some investors may find or exploit loopholes present in the system by transferring assets while alive to circumvent tax obligations on their heirs.

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[32] Will Norton, *How can giving to charity reduce an Inheritance Tax bill?*, KEYSTONE LAW (Jun. 5, 2024, 7:16 PM), https://www.keystonelaw.com/keynotes/inheritance-tax.
[33] OECD, *Inheritance taxation in OECD countries* (Jun. 5, 2024, 7:18 PM), https://www.oecd.org/tax/tax-policy/inheritance-taxation-in-oecd-countries-brochure.pdf.
[34] EXPATISTAN, *Cost of Living Ranking by Country* (Jun. 4, 2024, 7:45 PM), https://www.expatistan.com/cost-of-living/country/ranking.
[35] OECD, *Inheritance Taxation in OECD Countries*, OECD TAX POLICY STUDIES, 2021.

This way not only will investment stagnate, there won't be any financial contributions in the name of law towards the society. This way implementation of Inheritance tax is far from being foolproof at this stage.

8. CONCLUSION

As much as Inheritance tax sounds appealing to the society with the intention of wealth redistribution it comes with its own set of complexities too. Reintroduction of Inheritance tax in the nation, in the present day circumstances looks like a credible option but it is necessary to ensure it is not filled with loopholes, as this will be another failure in the nation.

Historically, though inheritance tax was abolished in 1985, the current economic climate, characterized by severe wealth inequality, suggests that there may be a renewed need for such a tax. Economically, from the perspective of a successive society inheritance tax can potentially generate revenue to fund public services and reduce inequality, as demonstrated by nations like Japan. However, on the contrary the challenges faced by countries like South Korea, where high inheritance tax rates have led to capital flight and disinvestment, highlight the potential side effects of this tax. Overall, the success rate of Inheritance tax in nations around the world, doesn't seem to be absolutely triumphant.

In the case of India, the reintroduction of inheritance tax must be carefully assessed and calculated by balancing the need for revenue and wealth redistribution against the risk of discouraging investment and economic growth. A well-structured progressive tax rate, coupled with some strategic exemptions and a solid administrative system in place, could mitigate some of these risks. Encouraging charitable donations through tax benefits, as seen in the UK, could also enhance the positive impact of the tax.

In conclusion, while the inheritance tax alone may not be the ultimate remedy for solving India's economic disparities, it could be an esteemed component of a broader progressive taxation strategy. Proper implementation along with no leeways, can make this an economy booster. Ultimately, the success of such a tax will depend on its design and the broader context of India's fiscal and economic policies.

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