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Is estate tax a social leveller?

Absence Of Impost Alone Might Not Attract Tax Tourists To India

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IS it a good idea for a tax consultant to nudge someone like Bernard Arnault, French businessman and the richest person in France, to adopt Indian nationality to escape paying tax duty?

Fifty-eight-year-old Arnault, ranked as the seventh-richest man in the world by Forbes in 2007, has assets valued at around $26 billion. He owns 47.5% of LMVH along with Christian Dior SA and is the chair-man of both companies.

It perhaps make sense for a tax consultant to advice Arnault as France charges an inheritance tax, which is levied on the worldwide assets of the deceased resident, subject to treaty provisions. The rates vary depending on the recipient's relationship with the deceased person. There are a few exemptions—works of art if offered to the state are spared from inheritance tax.

Some tax experts, however, reckon that it may be tough to convince Arnault to adopt Indian nationality due to a host of reasons. "One, India still does not have full capital account convertibility and this may be a hindrance for movement of forex capital in and out. Two, getting an Indian nationality through naturalisation may be too time consuming. Three, some of the developed countries that do not levy estate duty may provide a better alternative," says Ernst and Young tax partner Jayesh Sanghvi.

Australia, Russia, China, Malaysia, Sweden, New Zealand, Mexico and Hong Kong feature in the list of countries that do not levy an estate tax. Countries such as the US, the UK, Japan and Singapore, in contrast, tax the estate left behind by wealthy citizens/tax residents (residents who are liable to tax, regardless of citizenship).

US charges a tax on estates, after an exemption of $2 million. The tax is charged on the estate of the deceased US citizen, regardless of the location of the asset.

Like France, the UK levies an inheritance tax on the value of the accumulated assets of the deceased person. The jurisdiction of the tax hinges on the status of domicile. If the deceased person was a domicile of the UK, the tax would be charged on the value of his worldwide assets. In other cases, inheritance tax is levied only on the assets located in the UK.

"The levy of estate duty is devoid of nationality. It is imposed on citizens and tax residents, even if they are foreigners if the asset is located in a country that levies the duty," according to BMR Associates head direct tax practice Mukesh Bhutani.

A person (a foreigner), who stays for 182 days or more in a year is treated as a resident under the Indian tax laws. Or he is treated as a tax resident if he stays for 60 days in a year and 365 days in the preceding four years.

Irrespective of this criteria, a foreigner or an NRI has to pay tax on any income that he receives from India or income which is deemed to accrue or arise in India.

The UK has entered inheritance tax treaties with India, the US, Sweden, Switzerland, France and a few others to prevent double taxation. Inheritance tax treaties are few in number compared to bilateral tax treaties to prevent double taxation of income.

"While planning for succession, citizens should consider various tax and non-tax benefits of using trusts . The most important non-tax reason for using trusts is to avoid probate of a will in a given jurisdiction. Trusts can also be used to maximize exclusions, exemptions, credits and deductions allowed by law. Marital trusts can also defer tax. Consideration could also be given to more sophisticated estate planning techniques that use trusts including family limited partnerships, grantor trusts, dynasty trusts and charitable trusts. In many cases two or more would be advisable," says international tax expert **Nishith Desai**.

A person who renounces a US citizenship can set up foreign trusts with US citizens as beneficiaries. A foreign trust is considered a "non-resident alien individual" under the US

Internal Revenue Code. Neither the foreign trust nor the trustee is required to file a US tax return. The assets held in trust also escape probate on the estate of the grantor.

Individuals relinquishing their US citizenship are spared paying an estate tax, besides income tax and gift tax. However, the going may not be easy for those who renounce US citizenship with the primary motive of tax avoidance: They may still have to pay estate taxes, subject to certain norms.

Like estate duty, the incidence of the levy on capital gains is the location of the asset. “But one has to distinguish between the two levies. If estate duty is levied on an immovable property, the citus and location is clear”, holds Mukesh Bhutani.

Votaries of an estate tax say that it levels the playing field between the rich and the poor. The counter argument is that it discourages capital formation. India introduced estate duty in 1953, but scrapped it in 1985.

Can India attract tax tourists from the US or other high estate tax countries? The absence of estate duty in India may not constitute sufficient compensation for a wealthy foreigner to adopt Indian nationality, argues Jayesh Sanghvi.

Echoing a similar view, Anish Thacker, a chartered accountant says “if such a choice were to be made, the preference may be towards countries where there is a complete absence or a minimal incidence of taxation rather than a country with moderate income-tax rates but no estate tax.”

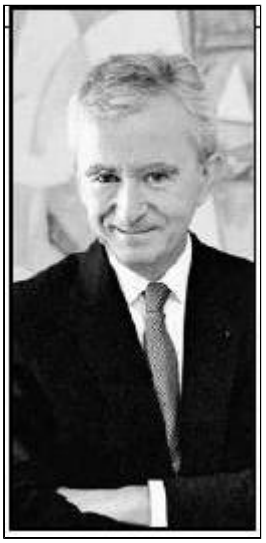
India’s maximum marginal personal income-tax rate is 30%. The corporate tax rate is 33.99%, but the effective rate is 17-19% due to various exemptions. The effective tax rate will rise when exemptions are phased out.

The corporate tax rate in Germany is lower at 26.4%, but this offset by the 30-50% estate tax. India appears to be an attractive destination for tax tourists from the US, which levies estate duties ranging between 18% and 46% and a corporate tax of 35%. So is the case for Japan.

“As India does not have citizenship based income, gift or estate taxes, it is a great place to live, make a gift and to die.” sums up **Nishith Desai**.

TAXING ISSUE

NIL ESTATE TAX IN INDIA
40%
ESTATE TAX IN THE UK
30-50%
ESTATE TAX IN GERMANY
18-46%
ESTATE TAX IN THE US
5-40%
ESTATE TAX IN FRANCE
10-50%
ESTATE TAX IN JAPAN WITH 20% SURTAX



WHERE WILL HE GO: Bernard Arnault