

GIFTS AND LOANS — BY AND TO NON-RESIDENT INDIANS: PART I

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Editor's Note on NRI Series:

This is the 8th article in the ongoing NRI Series dealing with Income-tax and FEMA issues related to NRIs. This article is divided in two parts. The first part published here deals with important aspects of Gifts by and to NRIs. The second part will deal with important aspects of Loans by and to NRIs. Readers may refer to earlier issues of BCAJ covering various aspects of this Series: (1) NRI — Interplay of Tax and FEMA Issues — Residence of Individuals under the Income-tax Act — December 2023; (2) Residential Status of Individuals — Interplay with Tax Treaty — January 2024; (3) Decoding Residential Status under FEMA — March 2023; (4) Immovable Property Transactions: Direct Tax and FEMA issues for NRIs — April 2024; (5) Emigrating Residents and Returning NRIs Part I — June 2024; (6) Emigrating Residents and Returning NRIs Part II — August 2024; (7) Bank Accounts and Repatriation Facilities for Non-Residents — October 2024.

INTRODUCTION

The Foreign Exchange Management Act (FEMA) of 1999 is a significant piece of legislation in India that governs foreign exchange transactions aimed at facilitating external trade and payments while ensuring the orderly development of the foreign exchange market.

Enacted on 1st June, 2000, FEMA replaced the earlier, more restrictive Foreign Exchange Regulation Act (FERA) of 1973, reflecting a shift toward a more liberalized economic framework. The Act establishes a regulatory structure for managing foreign exchange and balancing payments, providing clear guidelines for individuals and businesses engaged in such transactions.

It designates banks as authorized dealers, allowing them to facilitate foreign exchange operations. FEMA distinguishes between current account transactions and capital account transactions. Current account transactions, which include trade in goods and services, remittances, and other day-to-day financial operations, are generally permitted without prior approval, reflecting a more open approach to international commerce. In contrast, capital account transactions, which encompass foreign investments and loans, are subject to specific regulations. Furthermore, the Act includes provisions for enforcement through the Directorate of Enforcement, establishing penalties for violations.

This article will delve into the provisions governing gifting and loans involving Non-Resident Indians (NRIs), including the relevant implications under the Income Tax Act, 1961 (ITA) as applicable. Understanding these provisions is crucial for NRIs, as they navigate financial transactions across borders while remaining compliant with Indian tax laws. Further, within the gifting and loan sections, respectively, we will first deal with the FEMA provisions and, after that, Income Tax provisions dealing with gifting or loans as the case may be.

To start, it's essential to understand the definition of NRIs. The term NRI has been defined in several notifications issued under the Foreign Exchange Management Act (FEMA), as outlined in the table below:

Definition	Regulations
NRI means a person resident outside India who is a citizen of India.	FEM (Borrowing and Lending) Regulations, 2018
	FEM (Deposits) Regulations, 2016
	FEM (Remittance of Assets) Regulations, 2016
NRI means an individual resident outside India who is a citizen of India.	FEM (Non-Debt Instruments) Rules, 2019
	FEM (Debt Instruments) Regulations, 2019

In essence, the term NRI is defined in several notifications issued under the Foreign Exchange Management Act (FEMA) to refer specifically to an individual who holds Indian citizenship but resides outside of India. This definition captures a broad range of individuals who may live abroad for various reasons, including employment, business pursuits, education, or family commitments.

Further, kindly note that we are not dealing with the provisions concerning the overseas citizen of India cardholder ('OCIs') in this article. Overseas Citizen of India means an individual resident outside India who is registered as an overseas citizen of India cardholder under section 7(A) of the Citizenship Act, 1955.

FEMA ASPECT OF GIFTING

A. Gifting to and from NRIs

Let us briefly delve into whether the gifting transaction is a capital or a current account transaction. A capital account transaction means a transaction that alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of persons resident outside India and includes transactions referred to in sub-section (3) of section 6¹. A current account transaction means a transaction other than a capital account transaction and includes certain specified transactions. In our view, gifting transactions can be classified as either capital or current account transactions, depending on the specific circumstances. For instance, when an Indian resident receives a gift as bank inward remittance from a non-resident, this transaction does not change the resident's assets or liabilities in any foreign jurisdiction nor alters the assets or liabilities of a non-resident in India. As a result, it can be viewed as a current account transaction, primarily affecting the resident's income without altering any existing financial obligations abroad. On the other hand, if an Indian resident gifts the sum of money in the NRO account in India of a non-resident, this situation will be categorized as a capital account transaction since this impacts the non-resident's assets in India.

Now that we have clarified the meaning of the term NRI, we can proceed to explore the provisions under FEMA related to gifting various assets by individuals residing in India to NRIs, whether those assets are located in India or abroad. Understanding these provisions is essential

for both residents and NRIs, as they outline the legal framework governing the transfer of gifts across borders. Under FEMA, certain guidelines specify how and what types of assets can be gifted, along with the necessary compliance requirements to ensure that these transactions adhere to regulatory standards.

A.1 FEMA Provisions — Gifting from PRI to NRI

a. Gifting of Equity Instruments of an Indian company

i. The expression equity instruments have been defined in Rule 2(k) of FEM (Non-debt Instruments) Rules, 2019 ('NDI Rules') as equity shares, compulsorily convertible preference shares, compulsorily convertible debentures, and share warrants issued by an Indian company.

ii. NDI Rules categorically include the provision concerning the transfer of equity instruments of an Indian company by or to a person resident outside India ('PROI')/ NRIs.

iii. Specifically, Rule 9(4) of NDI Rules provides that a person resident in India holding equity instruments of an Indian company is permitted to transfer the same by way of gift to PROI after seeking prior approval of RBI subject to the following conditions:

- The donee is eligible to hold such a security under the Schedules of these Rules;
- The gift does not exceed 5 per cent of the paid-up capital of the Indian company or each series of debentures or each mutual fund scheme [Paid-up capital is to be calculated basis the face value of shares of an Indian company.];
- The applicable sectoral cap in the Indian company is not breached;
- The donor and the donee shall be "relatives" within the meaning in clause (77) of section 2 of the Companies Act, 2013;
- The value of security to be transferred by the donor, together with any security transferred to any person residing outside India as a gift during the financial year, does not exceed the rupee equivalent of fifty thousand US Dollars [For the value of security, the fair value of an Indian company is required to be taken into consideration;]
- Such other conditions as considered necessary in the public interest by the Central Government.

¹ Though the definition refers to section 6(3) of FEMA, section 6(3) of FEMA is omitted as of the date of this article. Instead, Section 6(2) and Section 6(2A) are amended to cover the erstwhile provisions of Section 6(3) of FEMA.

iv. Consequently, it is clear that when a Person Resident in India (PRI) intends to gift equity instruments to a Non-Resident Indian (NRI), this action is permitted only after obtaining prior approval from the Reserve Bank of India (RBI) and subject to satisfaction of terms and conditions as mentioned in Rule 9(4) of NDI Rules.

v. This leads us to a critical question under FEMA: does gifting equity instruments on a non-repatriable basis also necessitate prior approval from the RBI, considering the fact that non-repatriable is akin to domestic investment?

- Rule 9(4) of the Non-Debt Instruments (NDI) Rules does not clearly specify whether prior approval from the Reserve Bank of India (RBI) is required for either repatriable or non-repatriable transfers of equity instruments. Hence, the first perspective is that since Rule 9(4) of NDI Rules does not distinguish between repatriable and non-repatriable investments, even gifting of shares on a non-repatriable basis should be subjected to the terms and conditions specified in Rule 9(4) of NDI Rules.

- The second perspective is that non-repatriable investments are viewed as analogous to domestic investments, suggesting that they operate similarly to transactions conducted between two resident Indians. In this light, the gifting of equity instruments of an Indian company should be permitted under the automatic route, thereby eliminating the need for prior RBI approval. This interpretation aligns with the notion that since the funds remain within India's borders and are not intended for repatriation, the transaction should not pose risks to the foreign exchange regulations.

vi. Additionally, it is to be noted that LRS provisions do not apply in the case of gifting of equity instruments of Indian companies by PRI to NRI.

b. Gifting of other securities such as units of mutual fund, ETFs, etc

i. Schedule III of the NDI Rules addresses the sale of units of domestic mutual funds, whereas the FEMA (Debt Instruments) Regulations, 2019, focuses specifically on the purchase, sale, and redemption of specified securities. Neither of these regulations explicitly mentions the gifting of such units or securities. Further, the term 'transfer' is also not used under these provisions to permit the gifting of such assets. As a result, a question arises regarding whether these securities can be gifted to Non-Resident Indians (NRIs) under the automatic route.

ii. Given that the rules and regulations do not explicitly outline the provisions for gifting, it is prudent to seek prior approval from the Reserve Bank of India (RBI) before proceeding with such transactions. This approach helps mitigate the risk of violating FEMA provisions, ensuring compliance and legal clarity in the transaction process.

c. Gifting of immovable property in India

i. Acquisition and transfer of immovable property in India by an NRI is governed by the provisions of the NDI Rules.

ii. Rule 24(b) of NDI Rules permits NRI to acquire any immovable property in India (other than agricultural land or farmhouse in India) by way of a gift from a person resident in India who is a relative as defined in section 2(77) of Companies Act, 2013. Thus, NRI cannot receive agricultural land or farm house by way of a gift from PRI even if it is from a relative.

iii. The relative definition of the Companies Act, 2013 covers the following persons:

Act of 2013
Relative, with reference to any person, means anyone related to another, if—
(i) they are members of HUF; or
(ii) they are husband and wife; or
(iii) one person is related to the other in such manner as may be prescribed.
Act of 2013 (as prescribed)
Father (including step-father)
Mother (including step-mother)
Son (including step-son)
Son's wife
Daughter
Daughter's husband
Brother (including step-brothers)
Sister (including step-sisters)

iv. As a consequence, gifting by only relatives as covered above is permitted in the case of immovable property in India. Thus, if the resident grandfather wishes to gift immovable property to his NRI grandson, such gifting will not be permitted under the contours of FEMA.

v. This limitation on gifting can have significant implications for families, particularly when it comes to

wealth transfer and estate planning. For instance, if the resident grandfather wants to ensure that his grandson benefits from the property, he will not be able to gift property to his grandson.

vi. Additionally, it is to be noted that LRS provisions do not apply in the case of gifting of immovable properties by PRI to NRI.

d. Gifting of immovable property outside India

i. The acquisition and transfer of immovable property outside India are governed by the provisions set forth in the Foreign Exchange Management (Overseas Investments) Rules, 2022 ('OI Rules').

ii. This brings up an important question: are resident individuals permitted to transfer immovable property outside India to Non-Resident Indians (NRIs)?

iii. Rule 21 of the OI Rules specifically addresses the provisions related to the acquisition or transfer of immovable property located outside India. Within this rule, Rule 21(2)(iv) explicitly states that a person resident in India can transfer immovable property outside the country as a gift only to someone who is also a resident of India. This means that the recipient of the gift must reside in India to qualify for such a transfer. Consequently, gifting immovable property outside India by a resident individual to an NRI is not permitted within the framework of FEMA regulations.

e. Gifting of foreign equity capital

i. To determine whether gifting of foreign equity capital from a PRI to an NRI is allowed, it is essential to consider the provisions outlined in the OI Rules and the Foreign Exchange Management (Overseas Investment) Regulations, 2022 ('OI Regulations'). Additionally, RBI has also issued Master Direction on Foreign Exchange Management (Overseas Investment) Directions, 2022, specifying/detailing certain provisions concerning overseas investments.

ii. Rule 2(e) of the OI Rules defines equity capital as equity shares, perpetual capital, or instruments that are irredeemable, as well as contributions to the non-debt capital of a foreign entity, specifically in the form of fully and compulsorily convertible instruments. Therefore, it primarily includes equity shares, compulsorily convertible preference shares, and compulsorily convertible debentures.

iii. Schedule III of the OI Rules addresses the provisions

related to the acquisition of assets through gifts or inheritance. However, it does not explicitly mention the scenario where a Person Resident in India (PRI) gifts foreign securities to a Non-Resident Indian (NRI). This implied that PRI is not permitted to gift foreign equity capital to NRI under the automatic route. This interpretation is also supported by the Master Direction, which clearly states that resident individuals are prohibited from transferring any overseas investments as gifts to individuals residing outside India. The definition of the term 'overseas investment' includes financial commitment made in foreign equity capital.

f. Gifting through bank / cash transfers

i. Master Direction on Liberalised Remittance Scheme ('LRS Master Direction') outlines the provisions concerning gifting by PRIs to NRIs through bank transfers.

ii. As per the LRS Master Direction, a resident individual is permitted to remit up to USD 250,000 per FY as a gift to NRIs. Whereas, for rupee gifts, a resident individual is permitted to make a rupee gift to an NRI who is a relative (as defined in section 2(77) of the Companies Act) by way of a crossed cheque/ electronic transfer. However, it is to be noted that the gift amount should only be credited to the NRO account of the non-resident.

iii. A significant question arises regarding whether a resident individual who has opened an overseas bank account under LRS is permitted to gift funds from that account to a person residing outside India. This question involves two differing interpretations of the regulations. One perspective posits that when a resident individual gifts money from an overseas LRS bank account, it alters their overseas assets. This change is seen as a capital account transaction, which is subject to stricter regulations under FEMA. Since gifting is not explicitly allowed under FEMA for capital account transactions, this view concludes that such gifts cannot be made. Additionally, the LRS Master Direction states that funds in the LRS bank account should remain available for the resident individual's use, suggesting that any transfer of those funds, including gifting, would not be permissible. Conversely, another view is that LRS intends to allow the utilization of funds for both permitted capital account transactions and current account transactions. Thus, gifting being a permitted transaction under LRS, it should be permitted from overseas bank accounts too. For example, since residents are allowed to use their overseas LRS bank accounts to cover travel expenses,

it stands to reason that gifting funds from these accounts should also be acceptable.

iv. Furthermore, concerning the gifting of cash to any person resident outside India by the PRI, it is crucial to that emphasize PRI is not permitted to give cash gifts to individuals residing outside India while the PROI is present in India or abroad. This prohibition stems from Section 3(a) of FEMA, which specifically forbids any person who is not an authorized person from engaging in transactions involving foreign exchange. The term 'transfer' under FEMA encompasses a wide range of transactions, including gifting. This means that any act of gifting cash or other forms of foreign exchange to a non-resident is treated as a transfer and is, therefore, subject to the same restrictions.

v. Thus, in a nutshell, while gifts in foreign currency can be sent to any person resident outside India, irrespective of their relationship with the donor, rupee gifts are strictly limited to those individuals defined as relatives. Also, cash gifting is prohibited.

g. Gifting of movable assets such as jewelry, paintings, cars, etc

i. Given that the FEMA regulations do not clearly outline provisions for gifting such movable assets located either in India or outside India, it is prudent to seek prior approval from the Reserve Bank of India (RBI) before proceeding with such transactions. This approach helps mitigate the risk of violating FEMA provisions while ensuring compliance at the same time.

A.2 FEMA Provisions — Gifting from NRI to PRI

a. Gifting of Equity Instruments of an Indian Company

i. Rule 13 of NDI Rules, which specifically covers the provisions concerning the transfer of equity instruments by NRIs, does not contain any specific provision wherein NRIs are permitted to transfer by way of gift equity instruments of Indian companies to a person resident in India. However, Rule 9 of NDI Rules, which covers the transfer of equity instruments of an Indian company by or to a person resident outside India, covers the provision concerning the transfer of equity instruments of an Indian company by way of a gift from a person resident outside India to a person resident in India. Since NRIs are categorized as a person residing outside India, Rule 9 can also be said to apply to the aforesaid situation.

ii. Specifically, Rule 9(2) of NDI Rules provides that a person resident outside India holding equity instruments of an Indian company is permitted to transfer the same by way of sale or gift to PRI under automatic route subject to fulfillment of certain conditions such as pricing guidelines, compliance if repatriable investment, SEBI norms as applicable, etc.

iii. As a consequence, NRI is freely permitted to transfer equity instruments of an Indian company by way of a gift to PRI in accordance with FEMA rules and regulations.

b. Gifting of other securities such as units of mutual fund, ETFs, etc

i. As discussed in paragraph A.1.b, Schedule III of NDI Rules, as well as FEMA (Debt Instruments) Regulations, 2019, do not clearly outline provisions for gifting of these instruments. Hence, it is advisable to seek prior approval from the Reserve Bank of India (RBI) before proceeding with such transactions.

c. Gifting of immovable property in India

i. The acquisition and transfer of immovable property in India by non-resident Indians (NRIs) are regulated by the NDI Rules.

ii. According to Rule 24(d) of these rules, NRIs can transfer any immovable property in India to a resident person or transfer non-agricultural land, farmhouses, or plantation properties to another NRI.

iii. However, an important point of consideration is that Rule 24(d) does not explicitly mention whether transfers can occur through sale or gift. This ambiguity necessitates a closer examination of the term 'transfer' to determine if it encompasses gifts.

iv. Although the term 'transfer' is not defined in Rule 2 of the NDI Rules, Rule 2(2) states that terms not defined in the rules will carry the meanings assigned to them in relevant Acts, rules, and regulations. Thus, we need to check if 'transfer' is defined in the Foreign Exchange Management Act (FEMA). Section 2(ze) of FEMA defines 'transfer' to encompass various forms, including sale, purchase, exchange, mortgage, pledge, gift, loan, and any other method of transferring rights, title, possession, or lien. Therefore, gifts are included within the definition of 'transfer' under FEMA.

v. As a result, NRIs are allowed to transfer immovable property in India to any resident person in accordance with Rule 24(d) of the NDI Rules, along with Rule 2(2) and Section 2(ze) of FEMA.

d. Gifting of immovable property outside India

i. The acquisition and transfer of immovable property outside India are governed by the Foreign Exchange Management (Overseas Investments) Rules, 2022 (referred to as the OI Rules).

ii. Rule 21 of the OI Rules specifically addresses the acquisition and transfer of immovable property outside India. Notably, Rule 21(2)(ii) permits PRIs to acquire immovable property outside India from persons resident outside India (PROIs). However, this rule does not explicitly allow for acquisition through gifting from NRIs; it only permits acquisition through inheritance, purchase using RFC funds, or under the Liberalized Remittance Scheme (LRS), among other methods. Rule 21(2)(i) allows PRIs to acquire immovable property by gift, but only from other PRIs.

iii. Thus, it emerges that PRIs are not permitted to receive immovable property as a gift from NRIs.

e. Gifting of foreign equity capital

i. To determine whether gifting foreign equity capital from a person resident in India (PRI) to a Non-Resident Indian (NRI) is allowed, it is essential to consider the provisions outlined in the OI Rules and the Foreign Exchange Management (Overseas Investment) Regulations, 2022 ('OI Regulations').

ii. Rule 2(e) of the OI Rules defines equity capital as equity shares, perpetual capital, or instruments that are irredeemable, as well as contributions to the non-debt capital of a foreign entity, specifically in the form of fully and compulsorily convertible instruments.

iii. Schedule III of the OI Rules outlines the provisions regarding how resident individuals can make overseas investments. It specifically allows resident individuals to acquire foreign securities as a gift from any person residing outside India. However, this acquisition is subject to the regulations established under the Foreign Contribution (Regulation) Act, 2010 (42 of 2010) and the associated rules and regulations.

iv. As a result, PRIs are permitted to receive foreign securities as a gift from NRIs.

f. Gifting through bank/ cash transfers

i. Under FEMA, there are no restrictions on receiving gifts via bank transfer by PRI from NRI. However, it is to be noted that PRI is not permitted to accept gifts from a person resident outside India/ NRI in their overseas bank account opened under the Liberalised Remittance Scheme since the LRS account can only be used for putting through all the transactions connected with or arising from remittances eligible under the LRS.

ii. Similar to what has been discussed in paragraph A.1.f.iv, gifting cash by NRI to PRI is not permitted.

g. Gifting of movable assets such as jewelry, paintings, cars, etc

i. Given that the FEMA regulations do not clearly outline provisions for gifting such movable assets located either in India or outside India, it is advisable to seek prior approval from the Reserve Bank of India (RBI) before proceeding with such transactions.

A.3 FEMA Provisions — Gifting between NRIs

a. Gifting of Equity Instruments of an Indian Company

i. Rule 13 of NDI Rules, which specifically covers the provisions concerning the transfer of equity instruments by NRIs, contains the provisions for gifting equity instruments to another NRI.

ii. Rule 13(3) of NDI Rules specifically permits NRI to transfer the equity instruments of an Indian Company to a person resident outside India (on a repatriable basis) by way of gift with prior RBI approval and subject to the following terms and conditions:

- The donee is eligible to hold such a security under the Schedules of these Rules;
- The gift does not exceed 5 per cent of the paid-up capital of the Indian company or each series of debentures or each mutual fund scheme [Paid-up capital is to be calculated basis the face value of shares of an Indian company.]
- The applicable sectoral cap in the Indian company is not breached;

- The donor and the donee shall be “relatives” within the meaning in clause (77) of section 2 of the Companies Act, 2013;

- The value of security to be transferred by the donor, together with any security transferred to any person residing outside India as a gift during the financial year, does not exceed the rupee equivalent of fifty thousand US Dollars [For the value of security, the fair value of an Indian company is required to be taken into consideration;]

- Such other conditions as considered necessary in the public interest by the Central Government.

iii. Further, as per Rule 13(4) of NDI Rules, NRI is permitted to transfer equity instruments of an Indian company to another NRI under the automatic route provided such NRI would hold shares on a non-repatriation basis.

iv. Hence, in a nutshell, for repatriable transfer of shares by way of gift, prior RBI approval is required whereas, in the case of non-repatriable transfers, RBI approval is not required.

b. Gifting of other securities such as units of mutual fund, ETFs, etc

i. As discussed in paragraph A.1.b, Schedule III of NDI Rules, as well as FEMA (Debt Instruments) Regulations, 2019, do not clearly outline provisions for gifting of these instruments. Hence, it is advisable to seek prior approval from the Reserve Bank of India (RBI) before proceeding with such transactions.

c. Gifting of immovable property in India

i. According to Rule 24(e) of NDI Rules, NRI is permitted to transfer any immovable property other than agricultural land or a farmhouse or plantation property to another NRI. However, an important point of consideration is that Rule 24(e) does not explicitly mention whether transfers can occur through sale or gift.

ii. As discussed in paragraph A.1.c, section 2(ze) of FEMA defines ‘transfer’ to encompass various forms, including sale, purchase, exchange, mortgage, pledge, gift, loan, and any other method of transferring rights, title, possession, or lien. Therefore, gifts are included within the definition of ‘transfer’ under FEMA.

iii. As a result, NRIs are allowed to transfer immovable property in India to another NRI in accordance with Rule 24(e) of the NDI Rules read with Rule 2(2) of NDI Rules and Section 2(ze) of FEMA. It is to be noted that the transfer of agricultural land or a farmhouse or plantation property by way of gift to another NRI is prohibited.

d. Gifting of immovable property outside India

i. This transaction falls outside the regulatory framework of FEMA, meaning it is not subject to its restrictions or requirements. As a result, it is permitted and can be carried out without any regulatory concerns or limitations imposed by FEMA.

e. Gifting of foreign equity capital

i. This transaction falls outside the regulatory framework of FEMA, meaning it is not subject to its restrictions or requirements. As a result, it is permitted and can be carried out without any regulatory concerns or limitations imposed by FEMA.

f. Gifting through bank/ cash transfers

i. Under FEMA, NRI can freely gift money from their NRO bank account to the NRO bank account of another NRI, as transfers between NRO accounts are considered permissible debits and credits. Similarly, gifting money from one NRE account to another NRE account belonging to another NRI is also allowed without restrictions.

ii. However, the question comes up regarding whether it is allowed to gift money from an NRO account to the NRE account of another NRI or from an NRE account to the NRO account of another NRI. In our view, this may not be permissible, as the regulations regarding permissible debits and credits for NRE and NRO accounts do not explicitly cover this type of gifting transaction and restrict it to the same category of accounts.

iii. Furthermore, concerning the gifting of cash to any person resident outside India, as discussed in paragraph A.1.f.iv, gifting cash by NRI to NRI is not permitted.

g. Gifting of movable assets such as jewelry, paintings, cars, etc

i. Given that the FEMA regulations do not clearly outline provisions for gifting such movable assets

situated in India, it is advisable to seek prior approval from the Reserve Bank of India (RBI) before proceeding with such transactions.

A.4 Applicability of the Foreign Contribution (Regulation) Act, 2010

The Foreign Contribution (Regulation) Act, 2010 ('FCRA') governs the acceptance and utilization of foreign contributions by individuals and organizations in India. As per the Foreign Contribution (Regulation) Act, 2010, foreign contribution means the donation, delivery, or transfer made by any foreign source of any article, currency (whether Indian or foreign), or any security as defined in Securities Contracts (Regulations) Act, 1956 as well as foreign security as defined in FEMA. Thus, receipt of the above assets by PRI from foreign sources will trigger the applicability of FCRA. Hence, it is pertinent to analyze the definition of the term 'foreign source' as specified in FCRA.

It is important to highlight here that NRIs are not classified as a 'foreign source' under the provisions of FCRA. This distinction is crucial because it implies that gifts received from NRIs are not subjected to the stringent regulations that govern foreign contributions. Consequently, PRIs can freely acquire such gifts without falling under the scrutiny of FCRA.

INCOME TAX ASPECTS OF GIFTING

A.5 Applicability of Section 56 of the Income Tax Act, 1961

The framework of Section 56:

Section 56 of the Income-tax Act, of 1961, is primarily concerned with income that does not fall under other heads of income, such as salaries, house property, or business income. This section covers "Income from Other Sources" and serves as a residual category for various types of income that cannot be specifically classified under other heads.

This section deals, inter alia, with the taxability of gifts and the transfer of property under specific "conditions. This section was introduced to prevent tax avoidance by transferring assets or property without proper consideration (gifting) as a method to evade taxes.

Applicability:

As per this section, **any person** who receives income from any individual or individuals on or after 1st April, 2017, will have that income chargeable to tax. The 'income' types are outlined in the table below:

Sub- Section	Type of Income/ Property	Condition	Threshold	Taxable Amount
(a)	Money Received	Without consideration	₹ 50,000 aggregate per financial year	The entire amount received is taxable
(b)*	Immovable property received	Without consideration: If stamp duty value exceeds ₹ 50,000	₹ 50,000 stamp duty value	Stamp duty value of the property
(b)*	Immovable property received	With consideration: If the consideration paid is less than the stamp duty value and the excess is more than the greater of ₹ 50,000 or 10 per cent of the consideration.	Greater than ₹ 50,000 or 10 per cent** of consideration	Excess of stamp duty value over the consideration paid
(c)	Movable Property Received	Without consideration: Fair market value exceeds ₹ 50,000	₹ 50,000 aggregate fair market value	Entire fair market value
(c)	Movable Property Received	With consideration: If the consideration paid is less than the fair market value and the difference exceeds ₹ 50,000.	₹ 50,000 difference	Excess of fair market value over consideration paid

*Proviso to section 56(2)(x)(b)

** The Finance Act 2018 introduced a safe harbor limit set at 5 per cent of the actual consideration. However, the Finance Act 2020 increased this limit to 10 per cent of the actual consideration.

Proviso	Details	Taxable Amount
1	If the date of agreement and registration are not the same, the stamp duty value on the date of the agreement can be taken, provided payment was made by account payee cheque, draft, electronic clearing system, or other prescribed electronic modes.	Stamp duty value on the agreement date is used if conditions are met.
2	If the stamp duty value is disputed, the Assessing Officer may refer it to a Valuation Officer. The provisions of Sections 50C and 155(15) will apply.	The value is determined by the Valuation Officer, if applicable.
3	In cases covered under Section 43CA(1) (for certain types of properties), the 10 per cent threshold is increased to 20 per cent.	The difference between the stamp duty value and consideration if it exceeds ₹ 50,000 or 20 per cent of the consideration.

Exemption:

Though the list of exemptions is exhaustive, we have included key exemptions that are specifically pertinent concerning the gifting aspects only.

1. Any sum of money or any property received from any relative

The term "relative" shall be construed in the same manner as defined in the explanation to clause (vii) of Section 56(2), which delineates the definition of "relative" as follows:

Relative means:

i. In the case of an individual—

(A) spouse of the individual;

(B) brother or sister of the individual;

(C) brother or sister of the spouse of the individual;

(D) brother or sister of either of the parents of the individual;

(E) any lineal ascendant or descendant of the individual;

(F) any lineal ascendant or descendant of the spouse of the individual;

(G) spouse of the person referred to in items (B) to (F); and

ii. in the case of a Hindu undivided family, any member thereof,

2. Any sum of money or any property received on the occasion of the marriage of the individual

a. **Scope of Exemption:** Money or property received by the individual on their marriage is exempt under Section 56(2)(x), excluding gifts to parents. Further, the gifting of money or property, etc. will eventually be subjected to FEMA applicability as well in cross-border transaction cases.

b. **No Monetary Limit:** No limits on the value of gifts.

c. **Sources of Gifts:** Gifts can come from anyone, not just relatives.

d. **Timing of Gifts:** Gifts received before or after the wedding are exempt if related to the marriage.

A.6 Applicability of Clubbing Provisions under the Income Tax Act, 1961

Section 64 of the Income Tax Act, 1961, (ITA) addresses the taxation of income that arises from the transfer of assets to certain relatives, specifically focusing on preventing tax avoidance strategies that involve shifting income-generating assets. It aims to ensure that income from such assets is ultimately taxed in the hands of the original owner, thereby maintaining fairness in the taxation system.

The provisions of Section 64 concerning the clubbing of income is summarised in the table below:

Particulars	Provisions
Income of Spouse	Transfer of Assets: If a non-resident individual (let's say Mr. A) transfers an asset such as an immovable property located outside India or equity shares of Apple Inc. to his Indian resident spouse (Mrs. A) without adequate compensation, any income generated from that asset — such as rental income from the house or dividends from shares — will be treated as Mr. A's income. Whether capital gains pre-exemption or post-exemption to be clubbed: The High Court of Kerala, in the case of Vasavan², while interpreting Section 64 of ITA, held that the assessing authority was bound to treat the 'capital gains' which, but for Section 64 should have been assessed in the hands of the wife, as the capital gains of the assessee was liable to be assessed in his hands in the same way in which the same would have been assessed in the hands of the wife". Therefore, based on the above judicial pronouncements, one may claim that the capital gain income first needs to be computed in the hands of the spouse, and thereafter, capital gain income remaining net of allowable exemptions under Section 54/ Section 54F needs to be clubbed in the hands of husband for computing his total income in India.
Income of Minor Child	Clubbing of Income: Any income earned by a minor child, including income from gifts received, will be clubbed with the income of the parent whose total income is higher. This applies to all minor children of the individual. Exemption: There is a specific exemption of up to ₹ 1,500 per child for income derived from the assets of the minor. If the income exceeds this limit, the excess amount is clubbed with the income of the parent.
Income of Disabled Child	Separate Assessment: If a minor child is physically or mentally disabled, their income is not subject to clubbing provisions, allowing the child's income to be assessed separately. This recognition acknowledges the unique circumstances and financial burdens that may arise from disability.
Income from Assets Transferred to Daughter-in-Law	If an individual transfers assets to his daughter-in-law, any income generated from those assets will also be clubbed with the income of the transferor.
Transfer of Assets and Adequate Consideration	The clubbing provisions apply specifically to transfers made without adequate consideration. If the transferor receives fair value in exchange for the asset (like selling an asset), the income generated from that asset will not be subject to clubbing.

2 [1992] 197 ITR 163 (Kerala)

A.7 Applicability of Section 9(i)(viii) of the Income Tax Act, 1961

1. Introduction:

Till AY 20–21, no provision in the Act covered income of the type mentioned in section 56(2)(x) if it did not accrue or arise in India (e.g. gifts given to a non-resident outside India). Such gifts, therefore, escaped tax in India. To plug this gap, the Finance (No. 2) Act, 2019 inserted section 9(1)(viii) with effect from the assessment year 2020–21 to provide that income of the nature referred to in section 2(24)(xviii) arising outside India from any sum of money paid, on or after 5th July, 2019, by a person resident in India to a non-resident or foreign company shall be deemed to accrue or arise in India.

2. Key Provisions:

a. Conditions for Deeming Income:

- There is a sum of money.
- The sum of money is paid on or after 5th July, 2019.
- The money is paid by a person resident in India.
- The money is paid to a non-resident³, not a company or to a foreign company.

b. Exclusions from Coverage:

- Gifts of property situated in India are expressly excluded from the purview of this section: Section 56(2) refers to the sum of money as well as property. However, section 9(1)(viii) reads as 'income ... being any sum of money referred to in sub-clause (xviii) of clause (24) of section 2'. Thus, it refers only to the sum of money. Hence, a gift of property is not covered by section 9(1)(viii).
- The provision does not apply to gifts received by relatives or those made on the occasion of marriage, as specified in the proviso to section 56(2)(x) of the Income Tax Act.
- Gift of the sum of money by NRI to another NRI.

c. Threshold Limit:

- Any monetary gift not exceeding ₹50,000 in a financial

3 We have not mentioned applicability to resident and not ordinarily resident since we are dealing with provisions concerning NRIs in this article.

year remains exempt from classification as income under section 9(1)(viii).

A.8 Applicability of Section 68 of the Income Tax Act, 1961

Section 68 of the Income Tax Act imposes a tax on any credit appearing in an assessee's books when the assessee fails to satisfactorily explain the nature and source of that credit. This provision operates as a deeming fiction, treating unexplained credits as income if the explanation provided is inadequate.

Under Section 68, the initial burden is on the assessee to demonstrate the nature and source of the credit. Judicial precedents have established that to satisfactorily explain a credited amount, the assessee must prove three key elements:

- **Identity of the payer:** The assessee must provide clear identification of the person or entity that made the payment. This includes details such as the payer's name, address, and any relevant identification numbers.
- **Payer's capacity to advance the money:** The assessee must show that the payer had the financial capacity to provide the funds. This could involve demonstrating that the payer had sufficient income, savings, or assets that would allow them to make such a payment.
- **Genuineness of the transaction:** Finally, the assessee needs to prove that the transaction was genuine and not a façade to disguise income. This could include providing documentation such as bank statements, agreements, or other relevant evidence supporting the legitimacy of the transaction.

It is also critical to understand that just because a transaction is taxable under Section 56(2)(x), it does not exempt it from consideration under Section 68. For

example, consider Mr. A, who receives a gift of Rs. 1 crore from his non-resident son. This amount will not be taxable under Section 56(2)(x) because it falls within the definition of a relative, exempting it from tax. However, Mr. A will still have an obligation to prove the identity, capacity, and genuineness of this gifting transaction under Section 68 to ensure compliance with tax regulations.

When it comes to taxation, there are significant differences between these sections. If an addition is made under Section 56(2)(x), the income will be taxed at the individual's applicable slab rate, allowing the taxpayer to claim deductions for any losses incurred as well as set-off of losses. In contrast, if the addition is made under Section 68, Section 115BBE applies, imposing a much higher tax rate of 60 per cent on the added income, with no allowance for any deductions or set-offs for losses.

A.9 Applicability of TCS Provision under the Income Tax Act, 1961

In order to widen and deepen the tax net, the Finance Act 2020 amended Section 206C and inserted Section 206(1G) to provide that an authorized dealer who is receiving an amount for remittance out of India from the buyer of foreign exchange, who is a person remitting such amount under LRS is required to collect tax at source ('TCS') as per the rates and threshold prescribed therein. Gifting to a person resident outside India either in foreign exchange or in Indian rupees is very well covered within the purview of LRS remittances.

As per the TCS provision as applicable currently, at the time of gift by PRI to NRI either in foreign exchange or in Indian rupees, the authorized dealer bank of PRI will collect the tax at source @ 20 per cent in case the gift amount is in excess of ₹7 lakh. The second part of this Article will deal with important aspects of "Loans by and to NRIs". ■

"Time is really the only capital that any human being has, and the only thing that he can't afford to lose."

— Thomas Edison