Hindu Undivided Family (HUF)
What we will cover

• Introduction to a HUF
• Who can form a HUF
• Joining the HUF
• Income & Tax of HUF
• Smart moves
• Should you go in for a HUF
• Partition of HUF
• Quick pointers
"If you are paying too much tax and all possible deductions have been availed of, the only way to bring down the tax liability is by starting a Hindu Undivided Family (HUF). However, they can do so only after they marry."

- Says a Delhi-based CA
• HUF as another entity
• Entitled to the same exemptions as any other individual taxpayer
• Enjoys the same deductions as you and me
• Effectively gives the karta:
  ▪ an additional basic tax exemption of 1.8 lakh per year,
  ▪ an additional tax deduction under Sections 80C, 80CCF and 80D,
  ▪ the benefit of lower tax slabs.
• Karta of the HUF:
  - Gets a combined basic exemption of ₹ 3.6 lakh p.a.
  - Savings limit of ₹ 2.4 lakh p.a u/s 80C and 80CCF
  - Add another ₹ 30,000 u/s 80D
## HOW HUF CUTS TAX

<table>
<thead>
<tr>
<th>Total income</th>
<th>Individual</th>
<th>HUF</th>
<th>Individual</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>10,00,000</td>
<td>6,00,000</td>
<td>16,00,000</td>
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<tr>
<td><strong>Less</strong></td>
<td></td>
<td></td>
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<tr>
<td>80C</td>
<td>1,00,000</td>
<td>1,00,000</td>
<td>1,00,000</td>
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<tr>
<td>80CCF</td>
<td>20,000</td>
<td>20,000</td>
<td>20,000</td>
</tr>
<tr>
<td>80D</td>
<td>15,000</td>
<td>15,000</td>
<td>15,000</td>
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<td><strong>Taxable income</strong></td>
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<td><strong>4,65,000</strong></td>
<td><strong>14,65,000</strong></td>
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<tr>
<td><strong>Basic exemption</strong></td>
<td><strong>1,80,000</strong></td>
<td><strong>1,80,000</strong></td>
<td><strong>1,80,000</strong></td>
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<tr>
<td><strong>Tax payable</strong></td>
<td><strong>1,14,845</strong></td>
<td><strong>29,355</strong></td>
<td><strong>3,00,245</strong></td>
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</table>

By setting up the HUF, an individual divides his taxable income between two entities. This cuts his annual tax by ₹1.56 lakh.
WHO CAN FORM A HUF?
• Any Hindu, Sikh, Jain or Buddhist man can form an HUF - provided he is married
• Automatically constituted when a couple exchanges wedding vows
• Few simple formalities to be completed for the HUF to function as a legal entity
Minimum number of coparceners

• HUF can consist of just two members
  ▪ one of whom is a coparcener
  ▪ For tax purposes, the income of such an entity would not be taxed in the hands of the HUF; it would be taxed in the hands of the sole coparcener

• For an entity to be taxed as an HUF, it should have at least two coparceners
  ▪ The income of the HUF consisting of a husband and wife would not be taxed in the hands of the HUF
  ▪ Except where the husband has received funds on the partition of a larger HUF
Corpus for the HUF

- Any capital asset (property, gold, jewellery, securities, deposits) or cash
- Can't transfer just any asset
- Any personal funds or property given by an individual to the HUF
  - lead to clubbing provisions under Section 64 (2)
    - Income from these assets will be treated as that of the individual
    - defeating the very purpose for which the HUF was established

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With money received as gifts from relatives

- Tax implication
  - HUF does not enjoy exemption - no tax on gifts received by an individual from specified blood relatives
  - HUF is not an individual, so it has no relatives
  - Any money it gets will be treated as a gift from a stranger.
  - If the value of the assets received as gifts in a year exceeds ₹50,000, it will be deemed as income of the HUF and taxed accordingly
• With assets received as part of a will
  ▪ If the property is inherited by the individual, transferring it to the HUF will again lead to clubbing.
    • A person can give property and other assets to his son's HUF but it should be clearly specified that the asset is for setting up the HUF

• With funds received on the dissolution (or full partition) of a larger HUF
  ▪ If the Karta wants to divide the HUF property between the co-parceners
    • he can transfer the fund to a newly formed HUF

• If the ancestral property is sold, the proceeds received can also be transferred to the HUF
JOINING THE HUF
• All lineal descendants of the Karta, their spouses and children automatically become members
• Wives join the HUF as members
• Children join on birth as coparceners
• Even the unborn child of a member or co-parcener has an equal share in the HUF
• Till 2005:
  ▪ Daughter ceased to be a member in the HUF after her marriage
In 2005 the Hindu Succession Act was amended:

- Equal rights to daughters even after they were married
- Married women now have rights in two HUFs
  - Father's as a co-parcener
  - Husband's as a member
  - Cannot start a HUF on their own
  - Karta does not have male heirs
    - the HUF property will have to be partitioned among his daughters
- Mitakshara system - which is followed in most parts of the country, has accepted the change,
- Dayabhaga school - governs the HUFs in West Bengal and Assam, continues with the bias
Dayabhaga

• Father is the sole owner of the joint family property
• No other member can enforce the partition of the HUF as long as Karta is alive

Mitakshara

• Property belongs to the HUF, not to an individual
• Can be partitioned even during the lifetime of the Karta
• A husband and wife can form an HUF
  - but a wife can only be a member, not a co-parcener
  - The HUF income will not be assessed separately
  - A member has equal rights
  - Only a co-parcener can demand the partition of the HUF
  - Only the birth of a child will give the unit the status of an HUF for tax purposes
INCOME & TAX OF HUF
• Five basic heads of income:
  ▪ capital gains
  ▪ rent
  ▪ profit from business
  ▪ income from other sources
  ▪ salary
  • invest the initial corpus as well as the gifts received in subsequent years
  • Ancestral property can be let out
  • Start a business
  • Interest and royalty incomes
• Karta will have to maintain the books of accounts of the HUF and file tax returns on its behalf
• Date of filing tax returns and the tax rate are no different from that of individual taxpayers
• Need to invest to save tax under Section 80C and 80CCF
SMART MOVES
• Insure the family's health:
  ▪ Can get a group health insurance cover (in case of a large family of 20-25 people) at a low price

• Pay Karta for services:
  ▪ If the Karta does not have a high income, the HUF can pay him a salary for his services
  ▪ Salary will be taxed as his income
  ▪ Fully deductible from HUF income

• Use HUF income for expenses:
  ▪ income earned by the HUF can be used for the household expenses of the family
A co-parcener can take a larger home loan to reduce his personal tax liability because the HUF income is enough to take care of his living expenses.

- **Distribute income to co-parceners:**
  - Karta can gift money to the coparceners from the income earned by the HUF.
  - This income is tax-free in the hands of the co-parceners.
  - In this manner, a person with a high income will be able to get tax-free income.
• Give loan for business:
  ▪ HUF can also give loans to the Karta or coparceners for setting up a business
  ▪ The HUF can charge interest on the loan. Interest paid on any business loan is fully deductible.
  ▪ For the borrower, it will be like taking money from one pocket and putting it in another and getting tax deduction on the interest.
  ▪ A caveat here:
    • If the coparcener borrows money to start the same business in which the HUF is engaged, the tax authorities may raise an objection
    • Have been cases where income from businesses started by coparceners after borrowing funds from the HUF have been treated as HUF income
SHOULD YOU GO IN FOR A HUF
• Suits taxpayers who also have:
  ▪ income from ancestral property
  ▪ expect to inherit financial assets
  ▪ Will be able to divert the inheritance to the HUF
    • preventing their personal tax liability from shooting up
• Useful for taxpayers with a very high savings rate
  ▪ Whose Section 80C limit is quickly exhausted by the Provident Fund and children's school fee
  ▪ Will be able to get tax benefits on other investments, such as insurance premium, equity-linked saving schemes and fixed deposits
Partition of HUF

- To reduce tax liability
- The partition should result in separate independent taxable units
- Works best when members of the HUF have no other sources of income
• HUF is defined as consisting of a common ancestor and all his lineal male descendants together with their wives and unmarried daughters
• No formal action is required to create an HUF
• Family is a group of people related by blood or marriage
• Unmarried daughter and daughter in law is also member
• HUF continues even in the hands of females after the death of sole male member
• HUF need not consist of two male members- even one male member is enough
• Generally, the senior most male member of the family acts as Karta
• Any other male member can also act as Karta with the consent of the other member
• HUF Property:
  ▪ ancestral property
  ▪ property allotted on partition
  ▪ property acquired with the aid of joint family property
  ▪ separate property of a co-parcener blended with or thrown into a common family pool
• Female member cannot merge her separate property with joint family property, but she can make a gift of it to the HUF

• HUF can consist of several branches or sub-branches
  ▪ irrelevant whether the smaller HUFs hold any property
  ▪ Nucleus property can be acquired
    • partition of bigger HUF
    • gifts from any member of the family or a stranger
    • Will with intention of the donor or the testator that the said gift or bequest will form the HUF property of the donee
• HUF can safely receive gifts of up to Rs 3 lakh per year without incurring any tax liability
  - benefit of deduction of ₹ 1.2 lakh
  - basic exemption of ₹ 1.8 lakh
THANK YOU FOR YOUR TIME