THE INHERITANCE AND GIFT TAXATION — CONSIDERATIONS ABOUT ITS NATURE

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1. THEMATIC FRAMEWORK

In this article, and following political movements and a growing public discussion evidenced on this subject, we address the inheritance and gift taxation in order to ascertain its place in the context of the Portuguese tax system. Aiming this goal, we will consider the Portuguese experience in this area, analyzing the legislative sequence and, where it proves useful, we will consider the adopted solutions within other fiscal systems. Once completed that objective, we will promote a brief analysis of the consequences that arise from such characterization — mainly at the level of its constitutional conformity.

2. THE RECENT INTEREST IN INHERITANCE AND GIFT TAXATION

The absence of alternatives capable of generating a revenue increase using the income and consumption taxation, due to the saturation of its tax bases and the obstacles that arise to the alteration of the existing taxation models and their respective rates, lead the governments to look for alternative solutions in order to raise tax revenues. At the same time, there is a growing concentration of the academic and political debate around aspects related to economic inequality and its combat through tax redistribution solutions and the need to adjust the fiscal system in

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order to make it more favourable to economic growth. In the context described, it will therefore not be surprising that the discussion on the inheritance and gift taxation has been rekindled.

In Portugal, the “Partido Socialista” electoral programme for the legislative elections of 2015 had a proposal to create a tax on high-value inheritances. Although this proposal has not been transposed into the text of the state budget laws for 2016 and 2017, the consideration of such as a possibility has determined an immediate reaction on the part of the opposition parties, social media and public opinion. The debate on the legitimacy, utility and merit of this taxation was launched.

Although it does not represent an innovation in the context of the Portuguese tax system, the taxation of gratuitous transmissions – for a fairly heterogeneous complex of motives – has never been explored among us in the full extent of its potential. About 15 years since the 2003 property taxation reform, which led to the “Imposto sobre as Sucessões e Doações” (ISD) elimination, and considering the recent discussion on the subject, it is now the time to deepen the discussion on gratuitous transfer taxation.

3. The Legislative Evolution of the Inheritance and Gift Taxation in the Portuguese Tax System

The taxation of gratuitous transfers in Portugal – by donation or inheritance – began in 1838, with the “Imposto sobre a Transmissão do Património”. This tax exempted, objectively, the transmission of movable property and, subjectively, the transmissions between relatives in the 1st grade. The taxable transmissions were graved with rates established according to the degree of affiliation between the parties involved.

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3 Approved by the Law of February 21st.
4 See BULHÔES, Miguel de, A Fazenda Pública de Portugal, Praticas Vigentes e Varias Utopias do Auctor, Imprensa Nacional, 1884, 44-45; and VALÉRIO, Nuno, and others, Os
In 1860, the referred tax was abolished and approved the "Contribuição de Registo". This new tax merged the above mentioned tax on gratuitous transmissions with the SISA – a tax on onerous transmissions. Within this new tax, the gratuitous transfer of movable and immovable property between ascendants, descendants and spouses was exempt. This option only changed in 1869, when the exemption was restricted to the transmissions from parents to children. It was kept the decision of setting different tax rates depending on the degree of affinity between the transferor and the beneficiary of the transmission.

Later on, in 1917, was introduced, in the "Contribution of the Registry", progressive rates on gratuitous transmissions, which began to vary according to the value of the assets, and not only according to the degrees of kinship. Notwithstanding the introduction of a progressive taxation and the high rates that were set, the "Contribuição do Registo" on gratuitous transmissions recorded levels of revenue collection much lower than expected.

In 1929, the "Contribuição do Registo" on the gratuitous transmissions was transformed into the ISD. This tax has suffered significant legal modifications until 1958, when it was approved the new ISD Code. Within the mentioned tax, the gratuitous transfers of movable and immovable property were taxed in the person of its beneficiaries. Without prejudice to other cases provided for in the code, it was considered that a transfer of assets to a minor descendant wasn’t a taxable event. Due to the provision of a wide range of exemptions, the taxation of gratuitous transfers would only

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Impostos no Parlamento Português, Sistemas Fiscais e Doutrinais Fiscais nos Séculos XIX e XX, Dom Quixote, 2006, 196-197.

5 Approved by the Law of June 30th.
6 By the Law of August 31st.
7 See the Decree of May 24th.
9 See the Decree No. 16731 of April 13th, with force of law.
10 The tax on successions and donations.
11 See Decree-Law No. 41969, of November 24th.
12 Sec. BULHÕES, Miguel de, A Fazenda Pública de Portugal..., cit., 45; e VALÉRIO, NUNO, and others, Os Impostos no Parlamento Português..., cit., 176-177.
occur when the transferred goods exceeded certain minimum value. In the case of the transfers between ascendants, descendents or spouses those values were higher.

The Portuguese Constitution, in its original version from 1976, stated in that the tax on inheritances and gifts should be progressive in order to contribute to equality among citizens and that it should take on account the transmission, by inheritance, of the benefits produced by labour. In 1982, the referred provision was amended and eliminated the mention to "inheritance of the fruits of labour". Within the constitutional revision carried out in 1997, the reference to the tax on inheritances and gifts was eliminated. Since then, the Constitution only requires that the taxation of property contributes to equality between citizens. The "deconstitutionalization" of the tax on donations and successions opened the door to its abolition by the 2003 tax reform.

Nowadays, the inheritance and gift taxation in the Portuguese legal system is integrated within the scope of the “Imposto do Selo” (IS) and the “Imposto sobre o Rendimento das Pessoas Coletivas” (IRC). Thus since 2003, when the ISD was abolished – in the context of the property taxation reform. This option was mainly due to two factors: (i) the decision not to tax situations the gratuitous transmissions in favour of the closest family (ii) and the decision to tax the gratuitous transfers of property to companies within the IRC. Due to the legislative options described, the ISD suffered great erosion on its tax base. Consequently, the lawmaker has considered that, from that moment on, there was no reason to keep a code only destined to tax the remaining taxable gratuitous transmissions.

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9 See article 107 (3).
10 See the Law No. 1/82, of September 30th.
11 See the Law No. 1/97, of September 20th.
12 In its article 104 (3).
14 See Resolution of the Council of Ministers 10/98, of January 23th – I, Série-B.
15 The stamp duty.
16 The corporate tax.
17 See article 31 (3) of the Decree-Law 287/2003, of November 12th.
18 See the IS Code preamble.
The solution was therefore to shift of the taxation of gratuitous transfers to the scope of the IS Code\textsuperscript{23}.

In view of the above, in the Portuguese tax system, this sort of taxation is currently promoted in two ways: (i) the IRC taxation of gratuitous transfers of property to companies\textsuperscript{24} – in such cases, the gratuitous transfers will positively affect the formation of taxable income\textsuperscript{25}; and (ii) the IS taxation of gratuitous transfers of property to individuals\textsuperscript{26}. In the latter case, the tax will be required of the subjects benefiting from the transfers: (i) in the case of transfers by death, the tax is due on the inheritance, represented by the head of household or the legatees, depending on the circumstances; (ii) in other gratuitous transfers, the tax is due by its beneficiaries\textsuperscript{27}.

Focusing our analysis on the IS, we see that these taxable persons will be charged with the payment of IS at a fixed rate of 10\% on the value of the transmitted goods\textsuperscript{28}. The scope of the tax under analysis is significantly restricted in view of the fact that the legitimate heirs (the spouse or unmarried partner, the descendants and the ascendants) are exempt from any taxation\textsuperscript{29}. Thus, because, on the one hand, the civil legislation disciplines the inheritance between the legitimate heirs by ensuring them a portion of the assets – by the way, the most significant part of them. On the other hand, the vast majority of the gratuitous transfers of assets carried out in the lifetime are addressed to the legitimate heirs. For these reasons, the said exemption has the concrete effect of exempting from the payment of IS the vast majority of inheritance and gifts. Taking all these factors into account, it's easily understood that the revenue

\textsuperscript{23} The IS has historically evolved in the sense of assuming a residual configuration. It is capable of embracing in its scope a fairly diversified tax realities. These include, for this purpose, the taxation of gratuitous transfers. About this tax taxable base, see LOBO, Carlos Batista, «As operações financeiras no Imposto do Selo: enquadramento constitucional e fiscal», Revista de Finanças Públicas e Direito Fiscal, n.º 1, Ano I, IDEF/Almedina, 2008, 76-79.
\textsuperscript{24} See article 21 (1 and 2) of the IRC Code.
\textsuperscript{25} See the IS Code preamble.
\textsuperscript{26} See article 5 (1, 3 and 5/e) and article 6 (e) of the IS Code and the point 1.2. of the IS Code general table.
\textsuperscript{27} See article 2 (2) of the IS Code.
\textsuperscript{28} See point 1.2 of the IS Code general table.
\textsuperscript{29} See articles 2156 and follow of the "Código Civil" (Civil Code).
obtained from the levying of this tax does not contributes in a significantly way to the formation of the overall tax revenue\textsuperscript{30}.

At the same time, for the closest relatives (the legitimate heirs) that are exempt from tax, the gratuitous transfers occurred between each other have the power to eliminate/reduce the taxable capital gain on a future onerous transfer. Therefore, it can influence the amount of personal income tax collected by tax administration\textsuperscript{31}. Through a gratuitous transfer, the acquisition value of the transferred assets for tax purposes is increased. Seen that the capital gain in the scope of the “Imposto sobre o Rendimento das Pessoas Singulares”(IRS)\textsuperscript{32} is calculated on the difference between the acquisition value and the sale value result, the capital gain on a future onerous transfer of the referred assets will be reduced\textsuperscript{33}. This results in a tax forgiveness for any capital gains accrued during the decedent’s lifetime.

4. DISCUSSION ON THE INHERITANCE AND GIFT TAXATION NATURE

The constitutional forecast of tax as a fundamental duty to contribute to public necessities in accordance with the criterion of the ability to pay, leads us to consider three autonomous parameters susceptible to reveal it: income, consumption and property\textsuperscript{34}. What is the relevant parameter when we talk about taxing inheritances and gifts?

The ability to pay is delimited by the fiscal lawmaker on the basis of the economic capacity of the taxpayers. In turn, this capacity shall be based on the set of assets, with patrimonial value, which integrate the legal sphere of the taxpayer, although considered in different dimensions: (i) the set of assets susceptible to pecuniary valuation which enter the legal sphere of the taxpayer in a given

\textsuperscript{30} Regarding the context of the European Union, this constitutes a common aspect between the different Member States tax systems. See EUROPEAN COMMISSION, Cross-country Review of Taxes on Wealth and Transfers of Wealth, October 2014, 2-3.


\textsuperscript{32} The personal income tax.

\textsuperscript{33} See article 45 (1 and 3/b) of IRS Code.

\textsuperscript{34} See article 104 of the Constitution and article 4 of the “Lei Geral Tributária”.
period of time (income taxation); (iii) the stock of assets belonging to the taxpayer or its transfer (property taxation); (iii) and the assets leaving the taxpayer legal sphere for the purpose of satisfying his needs (consumption taxation)\(^35\). In which hypothesis falls under the gratuitous transfer taxation?

Among us, and taking into consideration the specific outlines that it has been taking in our fiscal system, the predominant response of our doctrine goes in the sense of its qualification as a form of taxation of property, focusing on the increase of the value of the wealth of the transfer beneficiary\(^36\). It is, however, difficult to draw the borders between taxation of property and income in such situations, because the free transfer of goods will be an asset increment in the legal sphere of the beneficiary. The simple confrontation of the legal framework conferred to the gratuitous transfers taxation by the Portuguese lawmaker allows us to realize that it may fall under the IS (allegedly, property taxation) or the IRC (income taxation) scope depending on the nature of the taxpayer (an individual or a company, respectively). The same option was taken by the Spanish lawmaker, since the "Impuesto sobre Sucesiones y Donaciones" is only applied to gratuitous transfers benefiting individuals and the transfers benefiting companies are taxed within the "Impuesto sobre la Renta de las Personas Físicas"\(^37\).

In the light of the foregoing, the gratuitous transfers can be qualified as an asset increase and be taxed under an income tax, or be qualified as relevant assets transfers in the context of property taxation\(^38\). In a bolder perspective, there are also who support the

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\(^{35}\) See VASQUES, Sérgio, Capacidade Contributiva, Rendimento e Património, Fiscalidade n.\(^0\) 23, 40.


\(^{37}\) See article 3 (3) of the "Ley del Impuesto sobre Sucesiones y Donaciones" – Ley 29/1987, de 18 de diciembre.

\(^{38}\) On this problematic, see VILLAREJO, Avelino García, SÁNCHEZ, Javier Salinas, Manual de Hacienda Pública General y de España, Tecnos, 1995, 486-488.
possibility of integrating the gratuitous transmissions in the consumption taxation scope.

Concerning the established legislation, the framing of gratuitous transfers in one or another category of taxation has been due more to a political-legislative option, than to a consideration on its nature. In particular, the option to integrate the gratuitous transfers taxation in the stamp duty carries out serious difficulties in the level of its compatibility with the provisions of article 104 (1) of the Portuguese Constitution.

5. **Analysis of the Constitutional Conformity of Taxing Gratuitous Transfers in the IS Scope**

As stated, the main reasons for the ISD abolition were the exemption granted to the nearest family core and the legislative option to shift the taxation of gratuitous transfers benefiting companies to the IRC.

According to the legislator himself, the option to frame into the IRC scope the taxation of gratuitous transfers benefiting companies was due to the requirement to ensure coherence of the fiscal system in attention to the adoption of the principle of accrual income within that tax. If that was the reason, can we ask why the gratuitous transfers that benefit individuals were displaced into the IS scope, instead of the IRS?

The constitutional revision of 1977 implied a "deconstitutionalisation" of the ISD and the displacement of the goals that were associated with it (the promotion of equality among citizens) for the property taxation in general. Considering this new constitutional framework, the legislator, within the property taxation

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40 See the IS Code preamble.

41 That's, for example, what happens in Czech Republic where the inheritances and gifts are included in a provision of its personal income tax - although they are exempt from tax – see article 4 of the Act. No. 586/1992 Coll. ACT Czech National Council of 20 November 1992.
reform of 2003, has advanced in the direction of its abolition. Thus, with the (alleged) intention of integrating it into the taxation of property, in order to achieve a most efficient way of reducing inequalities in the system as a whole and among taxpayers who own property. Although it is clear that the solutions introduced by that reform do not lend themselves to major developments in this area, the truth is that, contrary to what happens with the IRS, the Constitution does not require progression in the field of taxation of assets. Provided that the progressive nature of taxation is a result of the combined composition of the taxes forming part of the overall tax system, the constitution grants the option to adopt it or not in the property taxation scope.

Focusing on our analysis on the taxation of gratuitous transmissions to natural persons, in synthesis, the heritage reform of 2003 has determined: (i) the ISD abolition; (ii) the exemption of gratuitous transfers that benefits ascendants, descendants and spouses; and (iii) the displacement of the tax facts which remained fiscally relevant into the IS or IRC scopes, on the basis of their respective recipients, in the context of which they are subject at fixed rates.

The inclusion of free transmissions in one or other type of taxation tend to be the outcome of a political consideration than the consideration of its legal nature. It will all depend on the way the legislator wishes to strike the object of taxation. As for the way that gratuitous transmissions are fiscally considered in the scope of the IS, we will tend to consider that they are seen as an asset increment in the legal sphere of the respective beneficiary. The same would not happen if the taxation was produced in the legal sphere of the

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42 This meant a clear sign of retreat from social concerns associated with fiscal policy – see VASQUES, Sérgio, Manual de Direito Fiscal, Almedina, 2013, 44.
43 See Resolution of the Council of Ministers 10/98, of January 23th – I, Série-B.
44 See NABAIS, José Casalla, Direito Fiscal, Almedina, 2015, 175.
45 See CANOTILHO, J. J. Gomes, MOREIRA, Vítor, Constituição da República Portuguesa Anotada, cit., 1101.
46 The IS Code preamble states that the transfers benefiting companies are taxed within IRC because of its nature of patrimonial increments and we see no grounds to qualify differently those transfers benefiting individuals. At the same time, we see that the beneficiaries of the transfers are liable to tax and bear the economic burden on the value of the assets entering their legal sphere (see article 1 (2), article 2 (2), article 3 (3/a) and point 1.2. of the IS Code general table).
transferor\textsuperscript{47}, as it happens in the United Kingdom ("Inheritance Tax") and in the in the United States of America ("Estate and Gift Taxes")\textsuperscript{48}.

There is a constitutional imposition in the sense that income tax has to be unique, personal and progressive. As result, there are grounds to question the constitutional conformity of the legislator’s option to shift this type of taxation into the scope of the IS, as described. As stated by XAVIER DE BASTO\textsuperscript{49}, the inheritances and donations are part of the concept of income that the fiscal theory has constructed for the purpose of measuring the taxpayers ability-to-pay, and the circumstance of not being taxed by personal income tax is not due to any hesitation theoretically founded on its nature, but on its irregular nature, with all the difficulties that arise from it in the scope of personal income tax, characterized by its progressive rates.

If we assume that the gratuitous transmissions integrates the concept of income, the assertion that they should be subtracted from personal tax by their irregular or occasional character should deserve some reservations. Thus, because the taxable income should correspond to the algebraic sum of the consumption of a particular individual, with the difference between the initial net assets and the final net assets, in a given period, thereby corresponding to the liquid enrichment of this individual\textsuperscript{50}. The personal income tax to summon the taxation of any patrimonial increments even if it assumes irregular or occasional nature. Consequently, the gratuitous

\textsuperscript{47} The question may be more problematic in the case of "mortis causa" transfers, as the article 2 (2/A) of the IS Code provides that the tax will be due by inheritance, represented by the representative of the beneficiaries. Nevertheless, taxation is not promoted in the legal sphere of the deceased. For fiscal reasons, the legislator recognizes tax personality to the inheritance, assuming it as taxpayer, but the lawmaker aim will nevertheless be taxing the beneficiaries of the gratuitous transfer – as the mentioned norm recognizes.

\textsuperscript{48} See article 1 of the Inheritance Tax Act 1984 of July 31st and Chapters 11 and 12, Subtitle B, Title 26, of the United States Code.

\textsuperscript{49} See BASTO, José Xavier de, As perspectivas actuais de revisão da tributação do rendimento e da tributação do património em Portugal, Boletim de Ciências Económicas da Universidade de Coimbra, Volume, XLI, 1998, 148.

\textsuperscript{50} The concept has evolved from a concept of income according to which should correspond to the flow of goods susceptible to pecuniary valuation which stem from a durable productive source during a certain period of time. About this subject, see RIBEIRO, João Sérgio, «Tributação Presuntiva do Rendimento, Um Contributo para Recuacionar os Métodos Indiretos de Determinação da Matéria Tributável», Almedina, 2014, 73.
transfers should be included with the taxable income concept. Otherwise, it would be easy for the ordinary lawmaker to evade the constitutional imperatives established in respect of each type of tax. To do so, it would be enough to requalify the taxable realities in a different kind of tax. The amount required to a taxpayer because of the fact that he had benefited from a gratuitous transmission focuses on the patrimonial increment recorded in its legal sphere. This does not change, because of the fact that we designate it by stamp duty.

While the Constitution expressly established the existence of an autonomous tax on inheritance and gifts, such a problem would not arise. However, once removed such provision, and assuming that we are faced with a patrimonial increments taxation, the option to maintaining its taxation outside the IRS and moving it to the IS arises as controversial in its constitutional conformity, considering the normative foresight of the article 104 (1) of the Constitution.

Such an option may conflict with the constitutional imperative of a global income taxation, which grounds the exclusion of selective taxes on income\(^5\). On the other hand, the mentioned solution may conflict with the constitutional imperative of progressive income taxation – seen that the gratuitous acquisitions will constitute patrimonial increments subject to a fixed rate of 10%\(^6\). Finally, the IS taxation does not consider the family income and its needs.

In the light of the foregoing and as a way to overcome the evidenced problem, we believe that the taxation of gratuitous transfers to individuals should be displaced into the IRS scope, contributing to the formation of its tax base. Thus, without prejudice to the possibility of subjecting them to the definitive or special rates because, in principle, as long as the IRS remains progressive as a

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\(^6\) The fact that the constitutional provision of article 104 (1) of the Constitution is addressed to the "personal income tax" as a whole, allows that certain realities which integrate its scope, not to be subject to a progressive taxation. From the referred provision won't result any constitutional disconformity if, in overall, the progressive nature of the tax is guaranteed. In this case, we can't sustain the same conclusion. Because if we admit that the lawmaker has separated a form of taxation of income under the IS, this "autonomous tax" will not respect the requirement of progressiveness.
whole, the taxation of certain revenues with flat rates won't be unconstitutional\textsuperscript{53}.

6. CONCLUSION

The nature of taxation of donations and successions is a problematic issue. It isn't easy to say, in general terms, if it should be framed into the taxation of income or property. It will all depend on concrete options assumed by the lawmaker on that matter. As regards the way the taxation of such transfers is disciplined in the Portuguese tax system, we have to conclude that the lawmaker considers them as manifestation of income.

This conclusion is sustained: (i) in positions assumed by the lawmaker himself; (ii) by the fact that the transmissions benefiting companies are taxed within the IRC; and (iii) in the legal discipline given to gratuitous transfers benefiting individuals under the IS, since its objective is to tax asset increments in the legal sphere of the respective beneficiary.

In this last case, such conclusion comes with relevant problems at the level of constitutional conformity of such an option, once considered the constitutional imperatives arising from article 104 of the Portuguese Republic Constitution. Such an option may conflict with the mentioned provision since: (i) it disrespects the constitutional imperative of a global income taxation – which grounds the exclusion of selective taxes on income; (ii) it disregards the constitutional imperative of progressive income taxation – once that the gratuitous acquisitions will constitute patrimonial increments subject to a fixed rate of 10%; and (iii) it does not consider the family income and its needs when taxing income arising from the gratuitous transfer.

\textsuperscript{53} As long as the IRS remains progressive in overall, it will not be unconstitutional the taxation of that certain revenues with flat rates.