Heads of Income: Capital Gains & Exemptions

Understanding Capital Assets and Tax Reliefs

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What is Capital Gain? (Sec. 45)

- Any profit or gain arising from the transfer of a capital asset is chargeable to tax under the head 'Capital Gains'.
- Capital Asset (Sec. 2(14)): Property of any kind held by an assessee, whether connected with a business or not.
- Examples: Land, building, shares, mutual funds, gold, jewellery, etc.
- Exclusions: Stock-in-trade, personal effects (except jewellery, drawings, etc.), rural agricultural land.

Types of Capital Gains

- Capital gains are classified based on the holding period of the asset.
- Short-Term Capital Asset (STCA): An asset held for a period of less than 36 months (or 12/24 months in specific cases).
- Short-Term Capital Gain (STCG): Profit from the sale of an STCA.
- Long-Term Capital Asset (LTCA): An asset held for a period of more than 36 months (or 12/24 months in specific cases).
- Long-Term Capital Gain (LTCG): Profit from the sale of an LTCA.
- Holding Period Exceptions:
- 12 months: Listed shares/securities, units of equity-oriented funds.
- 24 months: Immovable property (land/building), unlisted shares.

Computation of Capital Gains

- Particulars STCG LTCG
- Full Value of Consideration XXX XXX
- Less: Expenditure on Transfer (XXX) (XXX)
- Net Consideration XXX XXX
- Less: Cost of Acquisition (XXX) -
- Less: Indexed Cost of Acquisition - (XXX)
- Less: Cost of Improvement (XXX) -
- Less: Indexed Cost of Improvement - (XXX)
- Gross Capital Gain XXX XXX
- Less: Exemptions (XXX) (XXX)
- Taxable Capital Gain XXX XXX

- Indexation: A mechanism to adjust the cost of acquisition and improvement for inflation, reducing the taxable gain. It is only available for LTCG.

Tax Exemptions on Capital Gains (Sections 54, 54EC, etc.)

- To encourage reinvestment, the Act provides exemptions from tax on capital gains if the proceeds are reinvested in specified assets.
- Section 54: LTCG from the sale of a residential house property is exempt if the entire gain is reinvested in the purchase/construction of another residential house property within a specified time frame.
- Section 54EC: LTCG from the sale of any long-term capital asset (e.g., land, building) is exempt if the gain is invested in specific bonds (e.g., NHAI, REC) within 6 months from the date of transfer. The maximum investment is ₹ 50 Lakhs.
- Section 54F: LTCG from the sale of any long-term capital asset other than a residential house is exempt if the net consideration is reinvested in a residential house property within a specified time.

Tax Rates for Capital Gains

- Short-Term Capital Gain (STCG):
- Generally, taxed at the individual's normal slab rates.
- STCG on listed equity shares (Sec. 111A): Taxed at a flat rate of 15%.

- Long-Term Capital Gain (LTCG):
- LTCG on listed equity shares (Sec. 112A): Exempt up to ₹ 1 Lakh. Gain exceeding ₹ 1 Lakh is taxed at 10% without indexation benefit.
- LTCG on other assets (Sec. 112): Taxed at 20% with the benefit of indexation.

Example of Capital Gains Calculation

- Scenario: Mr. P sold a residential house on 10th June 2024 for ₹ 80 Lakhs. He purchased it on 1st May 2012 for ₹ 20 Lakhs. He bought another residential house on 1st March 2025 for ₹ 35 Lakhs.
- Analysis: The house was held for more than 24 months, so it is a LTCA.

- Calculation:
- Sale Consideration: ₹ 80,00,000
- Indexed Cost of Acquisition: (₹ 20,00,000 x 348) / 206 = ₹ 33,78,641 (using CII for AY 2025-26 and AY 2013-14)
- LTCG before exemption: ₹ 80,00,000 - ₹ 33,78,641 = ₹ 46,21,359

- Exemption u/s 54:
- He invested ₹ 35 Lakhs in a new house. The entire gain up to the amount of investment is exempt.
- Exempt LTCG = ₹ 35,00,000
- Taxable LTCG: ₹ 46,21,359 - ₹ 35,00,000 = ₹ 11,21,359

Summary of Key Concepts

- Capital Gain is a profit from the sale of a capital asset.
- It can be Short-Term (STCG) or Long-Term (LTCG) depending on the holding period.
- LTCG on most assets is eligible for indexation, which adjusts the cost for inflation, lowering your tax.
- The tax rates for capital gains are specific and often different from normal slab rates.
- You can claim tax exemptions by reinvesting your capital gains in a new asset, like a house or specific bonds.