
[2024] 164 taxmann.com 652 (Article)

[2024] 164 taxmann.com 652 (Article)©

Date of Publishing: July 27, 2024

Is dropping of rate of tax on capital gain to 12.5% a bait to bury cost indexation benefits**RAJI NATHANI**

FCMA, Advocate

**GOPAL NATHANI**

FCA

What is capital gain?

Capital gain is the profit earned on the sale of an asset which has increased in value over the holding period. Interest rates directly impact the cost of borrowing for developers and homebuyers. Lower interest rates make borrowing cheaper, encouraging developers to undertake new projects and homebuyers to invest in properties. It stimulates demand in the real estate market, leading to increased sales and development activity. Thus the real estate sector has played a significant role in India's economy and added significantly to the country's Gross Domestic Product (GDP) through various channels. Post 2001 the Government has prompted taxpayers to invest into land and building assets directly or indirectly essentially to boost infrastructure in the nation building. Likewise, the prices of the property have also risen due to low interest rates offered by banks on home loans coupled with low interest rates on savings and inflation.

Thus Indexation is a proactive solution to "bracket creep" and helps taxpayers maintain their same purchasing power and avoid higher tax rates brought on by inflation year on year basis of holding asset based on index factor announced by the Government. It is essentially used to adjust the numbers so that the value of our assets keep up with inflation. Even the bankers would take into account the indexation to make assessment of property value. Approved valuers provide estimates of valuation also considering the inflation. Indexation allowance is thus interwoven in any given transaction for transfer of long term capital asset because the value of money declines as the years go by. The same is also provided under sec 48 of the Income Tax Act, 1961

Long Term Capital gains**Indexation Allowance/Mode of computation. (sec 48)**

48. The income chargeable under the head "Capital gains" shall be computed, by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, namely:—

- (i) expenditure incurred wholly and exclusively in connection with such transfer;
- (ii) the cost of acquisition of the asset and the cost of any improvement thereto

Provided further that where long-term capital gain arises from the transfer of a long-term capital asset, other

than capital gain arising to a non-resident from the transfer of shares in, or debentures of, an Indian company referred to in the first proviso, the provisions of clause (ii) shall have effect as if for the words "cost of acquisition" and "cost of any improvement", the words "indexed cost of acquisition" and "indexed cost of any improvement" had respectively been substituted:

- (iii) "indexed cost of acquisition" means an amount which bears to the cost of acquisition the same proportion as Cost Inflation Index for the year in which the asset is transferred bears to the Cost Inflation Index for the first year in which the asset was held by the assessee or for the year beginning on the 1st day of April, 2001, whichever is later;

Proposal Rationale (Budget' 24)

The budget memorandum reads that indexation available under second proviso to section 48 is proposed to be removed for calculation of any long-term capital gains which is presently available for property, gold and other unlisted assets. **This will ease computation of capital gains for the taxpayer and the tax administration.** The proposal is proposed to be given effect immediately i.e. with effect from the 23rd of July, 2024.

Effect

By this amendment therefore any transaction of transfer of these three kind of assets on or after July 23, 2024 would be chargeable at flat rate of 12.5% on the difference of the sale price and cost of purchase without the indexation allowance benefit hitherto available under the law.

Aftermath's:

In limine, this amendment is patently wrong for the following reasons but first look at this simple calculation:

Particulars	INR	INR
Sale Consideration	1000	1000
Cost of Acquisition	200	200
Indexed cost	728	0
Capital Gains	272	800
Tax	54	100
Increase in Tax		84%

1. Reduction in tax Rate to 12.5% is actually an increase in tax by 84% without indexation.
2. The amendment if approved will be retrospective in nature as much as it aims to take away indexation benefit to counteract the effects of inflation presently available under the law on assets acquired and held between April 1, 2001 till July 23, 2024;
3. It is a settled law that tax should not operate retrospectively on gains in the value of the asset which had already taken place prior to the introduction of this new computation procedure; and
4. The amendment would mean essentially comparing purchases of one time-period with given cost index and value for money with another different time period altogether thus comparing apples with oranges as it proposes to tax the unindexed gain;
5. It is a common fact that the rate of increase/inflation in value of property is far greater after 2001 then earlier to that date and if the indexation benefit were only to operate for period of acquisitions prior to April 1, 2001 it would result in unfair treatment to one class of taxpayers.
6. Increase in black money transactions with an intend to reduce capital gains. This Irregular revision of provision of withdrawal of indexation benefit does the entire system more harm than is visible at the outset.

Way forward

1. The amendment should be made to take effect only prospectively for any transaction of sale of capital asset

acquired on or after July 23, 2024 for more rational simplification.

2. Indexation or NO Indexation shall be left at the option of the taxpayer.
3. Both buyer and seller take into consideration the indexation allowance before signing any transaction for transfer of long term capital asset in the nature of an immovable property. There would be many such transactions that may have been under pipeline /being planned or under execution as with this sudden amendment it would impact their negotiation. In the last alternate course the amendment may be deferred to September month like other amendments in the budget.

Even the circle rate is calculated by multiplying the property's built-up area by the applicable rate per square meter or square foot, factoring in the **property's age**. Then how can the law makers deprive the taxpayer of this benefit on old purchase.

Short Term Capital Gains

Proposal Statement

It is stated in the budget memorandum that the rate for short-term capital gain under provisions of section [111A](#) of the Act on STT paid equity shares, units of equity oriented mutual fund and unit of a business trust is proposed to be increased to 20% from the present rate of 15% as the present rate is too low and the benefit from such low rate is flowing largely to high net worth individuals. Other short-term capital gains shall continue to be taxed at applicable rate.

Falsity

Sundararaman Ramamurthy, MD & CEO, Bombay Stock Exchange while speaking at the 28th Annual General Meeting of Asia Securities Forum (ASF), hosted by Bombay Stock Exchange Brokers' Forum (BBF) in Mumbai informed that "eighty-three percent of the new investors registered in the last three years are below the age of 40 years, and are in their income earning age. Breaking down the number further, Ramamurthy said that nearly half of these new investors are in age of 30-40 years. Among the total number of investors trading in the market, around 60 percent got registered in the last 3 years. Out of this, 14 percent of the total are 18 to 20 years old. The next 22% is 20 to 30 years." Thus in his assessment stock market prospects are bright as young investors enter with active income.

If this is what it is and given these numbers, the perception held by the few bureaucrats in proposing this amendment is blatantly wrong and just an intellectual trickery.

In fact, for a large section of the small and medium class investors short term market gains are their bread and butter/livelihood so that to impose higher tax upon them does not truly reflect a rational decision.

Way forward

If the true rationale for the increase in rate is withdrawal of benefit from high net worth individuals then simply, the basic exemption of Rs. 1.25 lacs as applicable to long term capital gains may be extended to small/medium taxpayer's class only.

In the light of avowed objective of this government, Just and fair provisions of law shall always remain a cherry atop the confection of the rule of law. Such unfounded and ungrounded withdrawal of Indexation is certainly a call in question and shall be revoked with immediate effect.

■ ■