Monthly Missive for September, 2024

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Taxation on Capital Gain

The Union Budget 2024-25 brings significant changes to the taxation of capital gains, aimed at simplifying the tax structure and providing relief to taxpayers. The budget introduces new tax rates for both short-term and long-term capital gains, impacting a wide range of financial and non-financial assets. These revisions reflect the government's commitment to making the tax system more equitable and less burdensome for taxpayers, particularly benefiting the lower and middle-income classes.

Key changes to income under the head Capital Gains:

The thresholds for classifying assets as long-term have been simplified. For listed securities (such as equity shares, equity-oriented mutual funds1, units of business trust listed in India), it is 12 months and for all the other assets, it is 24 months. In the case of shares listed outside India, the period of holding is at 24 months for it to qualify as long-term asset. In case of Debt Mutual Funds, the holding period to qualify as long-term asset is now reduced from 36 months to 24 months.

Short Term Capital Gains:

Short-term capital gains on specified financial assets shall be taxed at a rate of 20% instead of the previous rate of 15%. All other financial assets and non-financial assets will continue to be taxed at their applicable tax rates, maintaining consistency in the broader tax framework.

Long-Term Capital Gains:

Long-term gains on all financial and non-financial assets will attract a tax rate of flat 12.5% without indexation, except for land and building acquired before 23rd July 2024.

To benefit the lower and middle-income classes, increasing the limit of exemption of capital gains on certain financial assets from ₹1 lakh to ₹1.25 lakh per year has been proposed. This increased exemption limit will apply for FY 2024-25 and subsequent years.

The rate for other long-term capital gains on all assets has been rationalized to 12.5% without indexation (Section 112). Previously, this rate was 20% with indexation. This change aims to simplify the taxation of capital gains and facilitate their easy computation.

Impact of Change in LTCG Rate and Removal of Indexation:

Example:

A. Test Period: 5 years
B. Cost of Acquisition: Rs.200
C. CII for FY 2024-25 = 363 and for FY 2014-15 = 240
D. Indexation Factor= 363/240 = 1.51
E. Indexed Cost of Acquisition: Rs.200*1.51= Rs.251

Let's assume three cases for sale consideration

Cases	Sale Consideration	Capital Gains with Indexed Cost of acquisition	Taxation (Old) @20%	Capital Gain without Indexed Cost of acquisition	Taxation (new) @12.5%	Tax Difference (New-Old)
Case 1	500	249	49.8	300	37.5	(12.3)
Case 2	400	149	29.8	200	25	(4.80)
Case 3	300	49	9.8	100	12.5	2.7

Impact Analysis:

The reduction in the rate will benefit all categories of assets, substantially benefiting taxpayers in most cases. However, where the gain is limited relative to inflation, the benefit may be limited or absent in a few cases. Nonetheless, the new structure is expected to make the taxation process more straightforward and less burdensome for taxpayers.

Amendment in Finance Bill:

After considerable debate on social media and input from various real estate industry participants, the Union government has unveiled two tax options for homeowners when selling their properties to minimize their tax liability:

1. Calculate the tax on long-term capital gains at 20% after applying the indexation benefit.
2. Calculate the tax on long-term capital gains at 12.5% without considering the indexation benefit.

Eligibility for the options:

Individuals or Hindu Undivided Families (HUFs) who purchased properties before July 23, 2024, are eligible to select their preferred long-term capital gains (LTCG) tax regime.

Conclusion:

The Union Budget 2024-25 marks a significant step towards a more streamlined and taxpayer friendly tax system in India. Changes to capital gains taxation are set to simplify calculations and offer substantial benefits to a wide range of asset holders. Together, these reforms are designed to boost economic growth, attract investment, and create a fairer tax system for everyone.