**Taxability of Long Term Capital Gains**

**-Implications & clarification**

1 Background

The Finance Bill 2018 has proposed certain amendments in regard to scheme of taxing Long Term Capital Gain arising on transfer of listed equity shares and units of mutual funds. Under the existing tax regime, Long Term Capital Gain arising from transfer of long term capital asset on which STT is paid is exempt from the income tax u/s 10(38) of the Income Tax Act. However, the present tax exemption was misused and abused as a tool of tax evasion. Even certain manufacturing units had reduced manufacturing activities and diverted its funds to the financial market for earning exempt income i.e. long term capital gain. Therefore the proposed amendment is brought to tax Long Term Capital Gain to avoid conversion of taxable income into exempt income and also to stop its misuse.

The CBDT has clarified the legal position vide circular no.370149/20/2018 dated 04.02.2018.

2 What is Proposed Amendment?

Under the proposed amendment the existing Section 10(38) which exempt Long Term Capital Gain is withdrawn and new section 112A is introduced which provide that Long Term Capital Gain arising from transfer of certain long term capital asset exceeding Rs.1,00,000 will be taxed at concessional rate of 10%.

3 What are Long Term capital asset?

1. Equity Shares in a company listed on a recognised stock exchange;

 (b) Unit of an equity oriented fund; and

 (c) Unit of a business trust.

Further, the above assets must be held for more than minimum period of 12 months from the date acquisition and STT is paid at the time of transfer and also paid at the time of acquisition if the shares are acquired after 1/10/2014. The holding period will be counted from the date of acquisition.

4 Year of applicability?

The new provision is applicable from the assessment year 2019-2020 i.e. transfer of long term capital asset takes place on or after 1/4/2018. Thus, if someone sales listed share before 31st March 2018, the entire capital gain is exempt u/s 10(38) of the Income Tax Act.

5 Working of long term capital gains

The Long Term Capital Gain will be computed by deducting cost of acquisition from the full value of consideration on transfer of long term capital asset.

Cost of acquisition for long term capital assets acquire on or before 31/1/2018 will be the actual cost. However, if the actual cost is less than the fair market value of such asset as on 31st of January 2018, then such fair market value i.e. 31/1/2018 will be deemed to the cost of acquisition.

6 Fair market value

 In case of a **listed equity share or unit**, the fair market value means the highest price of such share or unit quoted on a recognized stock exchange on 31st of January, 2018.

However, if there is no trading on 31st January, 2018, the fair market value will be the highest price quoted on a date immediately preceding 31st of January, 2018, on which it has been traded.

In the case of **unlisted unit**, the net asset value of such unit on 31st of January, 2018 will be the fair market value.

7 Applicability of TDS provisions.

No TDS to be deducted if the Long Term Capital Gain pertains to resident tax payer. In case of a non resident Provision of Section 195 will be applicable and accordingly TDS would be deducted. In case of FII, no TDS will be deducted.

8 Whether Long term capital loss can be set off

Under the new provisions since Long Term Capital Gain is taxable from the financial year 2018-19, the net long term capital loss incurred after 1/4/2018 shall be entitled to set-off against Long Term Capital Gain and if net Long Term Capital Gain exceed Rs.1,00,000, the tax will be paid at 10%.

Further long term capital gain can also be set off against the other capital losses pertains to other capital assets.

9 Some illustrations in light of the above clarification

 Shares acquired on 1.12.2016 for Rs.1,00,000/-

 Shares sold for Rs.5,00,000/-

 FMV of shares on 31.01.2018 is Rs.2,00,000/-

 Other Capital losses Rs.3,00,000/-

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| --- | --- | --- | --- |
| Particulars | If transfer before 31.03.2018 | If transfer after 31.03.2018 | If transfer after 31.03.2018 (taking sale consideration of Rs.7,00,000) |
| Cost (a) | 1,00,000 | 1,00,000 | 1,00,000 |
| FMV (b)  | 2,00,000 | 2,00,000 | 2,00,000 |
| Sale consideration (c) | 5,00,000 | 5,00,000 | 7,00,000 |
| Long term capital gain | 4,00,000 (c-a) | 3,00,000(c-b) | 5,00,000(c-b) |
| Set off other capital losses | Nil | 3,00,000 | 3,00,000 |
| Long term capital gain exempt u/s 10(38) | 4,00,000 | Not applicable | Not applicable |
| Exemption limit | Nil | Nil | 1,00,000 |
| Long term capital gain tax @ 10% | Nil | Nil | 2,00,000 |
| Tax payable u/s 112A | Nil | Nil | 20,000 |