# IMPORTANT ISSUES UNDER CAPITAL GAINS



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# We are proposing to deliberate upon following topics

Recent changes and development in the taxation of capital gains on transfer of shares and securities

- Taxation on buy back of shares
- Debenture a capital asset or a debt (S.50AA)
- Exemptions u/s 54 and 54F
- important decisions dealing with issues under capital gains
- Some other relevant issues

## Period of holding of a capital asset

- S. 2(42A) A Capital Asset held by an assesse for more than 24 months preceding immediately the date of transfer.
- Vide Finance (no. 2) Act 2024, the word '24 months' has been substituted for the word 36 months w.r.e.f 23.07.2025.
- 1st proviso to S.2(42A) In case of a security listed in a recognized stock exchange in India or unit of the unit Trust of India established under the Unit Trust of India Act, 1963 or a Unit of an equity oriented fund or zero coupon bond, the provision of this clause shall have effect as if for the word 24 months, the word 12 months had been substituted.

# Taxation on buy back of shares in the hands of company and shareholder

- S. 2(22)(iv) provided that any payment made by a company on purchase of its own shares from shareholder in accordance with S. 77A of the Companies Act, 1956 was not to be treated as dividend. [introduced in Finance Act 1999 w.e.f 01.04.2000]
- S. 46A was introduced to provide the mechanism for computation of capital gains in the hands of the shareholder. As per S.46A, the difference between the cost of acquisition and the value of consideration received by shareholder on buy back of shares shall be treated as capital gains subject to the provisions of section 48. [introduced in Finance Act 1999 w.e.f 01.04.2000]
- Thus, the shareholders were liable to pay the capital gain tax as per S.46A on buy back of shares

S.10(34A) was introduced in the Finance Act, 2013 w.e.f 01.04.2014 by which any income arising to an assesse being a shareholder, on account of buy back of shares not being listed in a recognized stock exchange by the company as referred to in s.115QA

[The highlighted words were omitted by the Finance Act, 2019 w.r.e.f 05.07.2019]

- S. 115QA Notwithstanding anything contained under the Act, a domestic company, shall be liable to pay the additional income tax at the rate of 20% on the amount of distributed income by the company on buy back of shares from the shareholder
- Distributed income means the consideration paid by the company on buyback of shares as reduced by the amount which was received by the company for issue of such shares, determined in the manner as may be prescribed.

[with effect from 01.04.2014, the company was liable to pay the tax on distributed amount at 20% on account of buy back of shares. Thus, the same was tax free in the hands of shareholder in view of S.10(34A)]

- The Finance (No.2) Act, 2024, made S.115QA inoperative w.e.f 01.10.2024 and introduced clause (f) to section 2(22) of the Act.
- As per section 2(22)(f), any payment received by a shareholder from the Company on purchase of its own shares as per the provisions of section 68 of the Companies Act, 2013, then, the said payment shall be treated as a dividend income in the hands of a shareholder which will be taxed at the regular rates. [inserted in Finance Act, 2024 w.e.f 01.10.2024]
- Further, a proviso has been inserted in S.46A which provides that if a shareholder receives any consideration from a company on buy back of shares as referred to in section 2(22)(f) after 01.10.2024, then, for the purpose of section 46A, the value of consideration received will be treated as Nil. Effect to this, a capital loss will be generated in the hands of a shareholder which is allowable to set off as per section 74 of the Act.
- Vora Financial Services (P) Ltd. vs. ACIT [2018] 171 ITD 646 − S. 56(2)(via) cannot be attracted in the hands of the company recipient on buy back of shares.

## **Debenture – A Capital Asset or debt**

- S.2(h) of Securities contract Regulation Act, 1956 defined the word "securities" which includes (i) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;
- The 1<sup>st</sup> proviso to clause (iii) of S.47 recognizes the debentures as a capital asset
- The provisos to S.48 also recognize the debenture as a capital asset.
- Intention of the legislature is to treat the debenture as a capital asset.

- S.50AA, a newly inserted section in the Finance Act 2023 w.e.f 01.04.2024, provides for a mechanism to compute the capital gains of Market Linked Debenture.
- S. 50AA Notwithstanding anything contained in section 2(42A) or 48 of the Act where the capital asset is
  - i. a unit of a Specified Mutual Fund acquired on or after the 1st day of April, 2023 or a Market Linked Debenture; or
  - ii. is an unlisted bond or an unlisted debenture which is transferred or redeemed or matures on or after the 23<sup>rd</sup> July, 2024

the full value of consideration received or accruing as a result of the **transfer** or **redemption** or **maturity** of such debenture or unit as reduced by

- a. the cost of acquisition of the debenture or unit; and
- b. the expenditure incurred wholly and exclusively in connection with such transfer or redemption or maturity

shall be deemed to be the capital gains arising from the transfer of a short-term capital asset

- No deduction shall be allowed in computing the income chargeable under the head "Capital gains" in respect of any sum paid on account of securities transaction tax under the provisions of Chapter VII of the Finance (No. 2) Act, 2004 (23 of 2004).
   "Market Linked Debenture" means a security by whatever name called, which has an underlying
  - "Market Linked Debenture" means a security by whatever name called, which has an underlying principal component in the form of a debt security and where the returns are linked to market returns on other underlying securities or indices and include any security classified or regulated as a market linked debenture by the Securities and Exchange Board of India
  - "Specified Mutual Fund" means a Mutual Fund by whatever name called, where not more than thirty five per cent of its total proceeds is invested in the equity shares of domestic companies.

The clause (ii) explaining Specified Mutual Fund substituted with following vide Finance (No.2) Act, 2024 w.e.f 01.04.2026

#### **Specified Mutual Fund means**

- a. A Mutual Fund by whatever name called, which invests more than sixty-five per cent of its total proceeds in debt and money market instruments; or
- b. a fund which invests sixty-five per cent or more of its total proceeds in units of a fund referred to in sub-clause (a)

#### Points for discussion:

- Can the assessee claim the benefit u/s 54F against the STCG declared u/s 50AA as in like manner it
  is claimed against the STCG u/s 50
- What is the implication when the debentures are held as a stock in trade?

# Summary of exemption provisions u/s. 54 & 54F

Exemption	U/s. 54	U/s. 54F
Who can claim exemption	Individual /HUF	Individual/HUF
Eligible assets sold	A residential House property (minimum holding period 3 year)	Any long-term capital asset (other than a residential house property)  provided on the date of transfer the taxpayer does not own more than one residential house property from the assessment year 2001-02 (except the new house)

Assets to be acquired for exemption	Residential house property	Residential house property
Time limit for acquiring the new assets	Purchase: 1 year back or 2 years forward  Construction: 3 years forward	Purchase :1 year back or 2 year forward,  Construction: 3 year forward
Exemption Amount		Investment in the new assets / Net Sale consideration X capital gain subjected the cost of new asset upto Rs. 10 cr.
Whether "Capital gain deposit account scheme" applicable	Yes	Yes

# **Exemption from Capital Gains on Transfer of a Residential House - Section 54**

- Exemption available to Individual / Hindu Undivided Family
- It should be a long-term capital asset being residential house buildings or lands appurtenant thereto
- Income from such capital asset should be chargeable under the head "Income from House Property"
- The assessee has within a period of one year before or 2 years after the date of such transfer purchased or within a period of three years constructed <u>one</u> residential house <u>in India</u> ('a' has been replaced w.e.f 01.04.2015)
- If new asset sold within 3 years then the cost will be NIL or reduced by capital gain exempted earlier as the case may be.
- Exemption Amount: Equal to the amount so utilized or the amount of capital gain, whichever is less.
   With an upper cap of Rs. 10 cr.

- First proviso to section 54(1) provides that, where the amount of capital gains does not exceed two crore rupees, the assessee at his option, purchase or construct two residential houses in India.
- ➤ Second proviso to section 54(1) provides that where in any assessment year, the assessee has exercised above option, he shall not be subsequently entitled to exercise the option for the same or any other assessment

#### The above provisos inserted in Finance Act 2020 w.e.f 01.04.2020

- ➤ Third proviso to section 54(1) provides that where cost of new asset exceeds 10 crore rupees, the amount exceeding ten crore rupees shall not be taken into account for the purpose of section 54. [inserted in Finance Act, 2023 w.e.f 01.04.2024]
- ➤ Section 54(2) provides that if the amount of capital gains not appropriated by the assessee towards purchase or construction of the new asset before the date of furnishing the return of income under section 139(1) in a capital gain account as specified.

### S. 54(2) - Deposit into Capital Gains Account

#### **Section 139 (1) vs. Section 139 (4)**

- Rasiklal M Parikh vs. CIT [2017] 393 ITR 536 (Bom)
- CIT v. Rajesh Kumar Jalan [2006] 157 Taxman 398/286 ITR 274 (Gau.)

#### **Property purchased in Joint name**

- Smt. Tejal Kaushal Shah vs. ITO [2025] 173 taxmann.com 844 (Mumbai Trib.)/[2025] 212 ITD 397 (Mumbai Trib.)[17-04-2025]
- Abdul Nayab Shaikh VS. ITO [2024] 167 taxmann.com 381 (Mumbai Trib.)

#### Property purchased in other's name

- Prakash vs. ITO [2009] 312 ITR 40 (Bom.), property purchased in the name of Adopted son
- Colathur N. Ram vs. ACIT [2024] 168 taxmann.com 565 (Mumbai Trib.)[17-09-2024] For qualifying the
  exemption under section 54, it is necessary to make investments in residential house in the name of
  assessee only.

#### Source of fund irrelevant.

- ACIT vs. Dr. P.S. Pasricha [2008] 20 SOT 468 (Mum)
- Reji Easow vs. ITO [2022] 194 ITD 384 (Mumbai Trib.)

# The cost of a new residential house plus cost of land would be eligible for exemption u/s 54(1)

 C. Aryama Sundaram vs. CIT [2018] 407 ITR 1 (Madras) [SLP of the department dismissed by SC]

#### Capital gains on Sale of more than one residential house invested in one flat -

- DCIT vs. Ranjit Vithaldas, reported in [2012] 23 taxmann.com 226 (Mumbai)
- Sanjeev Behl vs. ITO [ITA 5345/Mum/2024]

## **Exemption Conditions Under Section 54F**

- Exemption available to Individual / Hindu Undivided Family
- Available on Transfer of any Long-Term Capital Asset other than residential house
- Capital Gains exempt if the whole of the net consideration is utilized within a period of 1 year before or 2 years after the transfer, or within 3 years in construction of new residential house
- To avail the benefit u/s 54F, the assessee should not own more than one residential house, other than the new asset on the date of transfer of the original asset
- Benefit u/s 54F is not allowable where the assessee purchases any residential house, other than the new asset, within a period of one year after the date of transfer of original asset
- The amount of net consideration not utilized to purchase or construct a new residential house prior to filing a return u/s 139(1) should be deposited under capital gain account as specified u/s 54F(4)
- The net consideration in excess of 10 crore shall not be taken into account for the purpose of section 54F

## Investment in multiple houses exemption u/s. 54/54F

- Whether only one will qualify or all will qualify
- Interpretation of "a residential house"
- Whether "a" means single unit
- or "a" means that house shall be "residential" in nature
- Interpretation of 'One residential house in India' introduced vide Finance Act, 2013 w.e.f 1-4-2015
- Krishnagopal B. Nangpal vs. DCIT [2025] 176 taxmann.com 752 (Bombay)[22-07-2025] (A.Y. 1995-96) Before amendment
- CIT vs. Gita Duggal (2013) 357 ITR 153 (Del.)
- CIT vs. Raman Kumar Suri (2013) 255 CTR 257 (Bom.)
- Nakul Aggarwal vs. ACIT [2024] 167 taxmann.com 540 (Mumbai Trib.)/[2024] 209 ITD 342 (Mumbai Trib.)[14-10-2024] (Followed the decision of Bombay High Court in case of CIT vs. Devidas Naik [2014] 366 ITR 12 (Bombay))

#### When New house is purchased / constructed

- Meaning of Purchase payment in kind or adjustment towards a debt CIT vs. T. N. Arvinda Reddy
   [1979] 120 ITR 46 (SC)
- CIT vs. Smt Beena K Jain [1996] 217 ITR 363 (Bom)

The exemption u/s 54 of the Act depend on the date of acquisition of the property and not on the date of payment

M. George Joseph vs. DCIT [2022] 440 ITR 589 (Karnataka)

#### ➤ Whether the benefit of S.54F is allowable on purchase of tenancy rights?

- Yogesh Sunderlal Shah vs. ACIT [2012] 139 ITD 194 (Mumbai)/[2013] 154 TTJ 309 (Mumbai)

(An adverse view taken by ITAT. The appeal is admitted by the High Court and pending for final hearing)

- A favourable view has been taken in the case of M/s. Archana Parasrampuria vs ITO [ITA 1196/Mum/2009]
- ACIT vs. Asha Ashok Boob [2015] 69 SOT 321 (Pune-Trib)

#### **Booking a house under construction project – Purchase or Construction**

- CIT vs. Mrs. Hilla J. B. Wadia [1995] 216 ITR 376 (Bom) Co-operative society
- Mustansir I Tehsildar vs. ITO [2018] 168 ITD 523 (Mumbai)

#### Period of holding -

- PCIT vs. Vembu Vaidyanathan [2019] 413 ITR 248 (Bom) For computing capital gain tax, the period of holding should be reckoned from the date of allotment.
- The SLP filed by the department against the ruling of High Court is dismissed by the Supreme Court [2019] 265 Taxman 535 (SC)[19-07-2019]
- Minakshi Mahesh Pawani vs ITO [ITA 4380/Mum/2023] [2024] 164 taxmann.com 255 (Mumbai Trib.)[28-06-2024]

### Some other relevant issues

- ➤ Transfer (Development Agreement) Section 2(47) r.w.s S.53A of TP Act, 1882
- Prithvi Consultants Pvt Ltd. vs DCIT [2025] 172 taxmann.com 780 (Bombay)[05-09-2023] Unregistered agreement shall have no effect in law for purposes of S 53A of Transfer of Property Act, 1882.

  (Considered and followed \* CIT vs. Balbir Singh Maini [2017] 398 ITR 531 (SC) \* Chaturbhuj Dwarkadas Kapadia of Bombay v. CIT [2003] 260 ITR 491 (Bombay)
- Cost of acquisition in case of inherited property / period of holding Section 49
- ➤ -Rohon Developers (P.) Ltd. vs. ITO [2022] 42 ITR 404 (Bom) cost of acquisition is a cost incurred by the previous owner For computing the period of holding, the period of holding of the previous owner to be included for ascertaining the nature of the property.

(Considered and followed \* CIT vs. Manjula J Shah [2013] 355 ITR 474 (Bom)

# **THANK YOU**

Note: I thank my colleague Ms. Neha Pranjape, Advocate for preparing this presentation.