

CHAPTER 7

Income under the head "Capital gains" and its computation

PROVISIONS IN BRIEF

Basis of charge	<p>Income under the head "Capital gains" is chargeable to tax if the following conditions are satisfied–</p> <ol style="list-style-type: none"> 1. There is a capital asset. 2. It is transferred during the previous year. 3. Capital gain is generated because of transfer. 4. Capital gain is not exempt from tax.
Meaning of "capital asset"	<p>"Capital asset" is defined by section 2(14).</p> <p>► <i>Positive list</i> - "Capital asset" means property of any kind, whether fixed or circulating, movable or immovable, tangible or intangible. Besides, it includes the following –</p> <ol style="list-style-type: none"> 1. Any rights in, or in relation to, an Indian company, including rights of management or control or any other rights whatsoever. 2. Property of any kind held by an assessee (whether or not connected with his business or profession). 3. Any securities held by a Foreign Institutional Investor which has invested in such securities in accordance with the regulations made under the SEBI Act. <p>► <i>Negative list</i> - The following assets are excluded from the definition of "capital assets" –</p> <ol style="list-style-type: none"> 1. Stock-in-trade (other than securities referred to in <i>point 3</i> above). 2. Personal effects. 3. Agricultural land in a rural area in India. 4. A few gold bonds and special bearer bonds (this point does not have any practical utility). 5. Gold Deposit Bonds issued under the Gold Deposit Scheme, 1999 or deposit certificates issued under the Gold Monetisation Scheme, 2015.
<i>Personal effects</i>	<p>Any movable property (including wearing apparel and furniture) held for personal use of the owner or for the use of any member of his family dependent upon him, is not a "capital asset" for the purpose of income under the head "Capital gains". However, the following are not "personal effects" (in other words, the following are "capital assets") even if these are for personal use—jewellery, archaeological collections, drawings, paintings, sculptures, or any work of art.</p>
<i>Agricultural land in a rural area in India</i>	<p>It should not be situated in <i>Area A</i> and <i>Area B</i>.</p> <p><i>Area A</i> - Any area within the jurisdiction of a municipality or a cantonment board having a population of 10,000 or more.</p> <p><i>Area B</i> - 2 kilometres (to be measured aially) from the local limits of municipality/ cantonment board (if population is above 10,000 but not more than 1 lakh) [it is 6 kilometres (if population is above 1 lakh but not more than 10 lakh) or it is 8 kilometres (if population is above 10 lakh)]</p>

<i>Types of capital assets</i>	<p>There are two types of capital assets – Short-term and long-term. If period of holding is more than 36 months, the capital asset is long-term, otherwise it is short-term.</p> <p>► However, in the following cases, the capital asset held for more than 12 months is treated as long-term capital assets – Listed equity/preference share in any company, Government securities, listed debentures, units of UTI, units of an equity oriented mutual fund and zero coupon bonds.</p> <p>► Moreover, equity/preference unlisted shares (from the assessment year 2017-18) and immovable property (being land/building) (from the assessment year 2018-19) held for more than 24 months are treated as long-term capital assets.</p>
Transfer	<p>Capital gains arises on transfer of a capital asset. If the asset transferred is not a capital asset, no capital gains will arise. Transfer includes sale, exchange or relinquishment of the asset; or the extinguishment of any rights therein; or the compulsory acquisition thereof under any law. However, the following are not treated as “transfer” (in other words, in the following cases, there is no capital gain) –</p> <ol style="list-style-type: none"> 1. Distribution of assets in kind by a company to its shareholders on its liquidation. 2. Any distribution of capital assets in kind by a Hindu undivided family to its members at the time of total or partial partition. 3. Any transfer of capital asset under a gift or a will or an irrevocable trust (exception – gift of ESOP shares is chargeable to tax and fair market value of the share on the date of gift is taken as sale consideration). 4. Transfer of capital asset between holding company and its 100 per cent subsidiary company, if the transferee-company is an Indian company. 5. Transfer of capital asset in the scheme of amalgamation/demerger, if the transferee-company is an Indian company. 6. Transfer of shares in amalgamating company/demerged company in lieu of allotment of shares in amalgamated company/resulting company in the above case. 7. Transfer of capital asset in a scheme of amalgamation of a banking company with a banking institution. 8. Transfer of shares in an Indian company held by a foreign company to another foreign company in a scheme of amalgamation/demerger of the two foreign companies, if a few conditions are satisfied. 9. Transfer of a capital asset by a non-resident of foreign currency convertible bonds or Global Depository Receipts to another non-resident if the transfer is made outside India and if a few conditions are satisfied. 10. Transfer by an individual of Sovereign Gold Bond (issued by RBI under the Sovereign Gold Bond Scheme, 2015) by way of redemption. 11. Transfer of any work of art, archaeological, scientific or art collection, book, manuscript, drawing, painting, photograph or print, to the Government or a University or the National Museum, National Art Gallery, National Archives or any other notified public museum or institution. 12. Any transfer by way of conversion of bonds or debentures, debenture-stock or deposit certificate in any form, of a company into shares or debentures of that company. 13. Transfer by way of conversion of preference shares of a company into equity shares of that company (applicable from the assessment year 2018-19). 14. Land transferred by a sick industrial company, if a few conditions are satisfied. 15. Transfer of a capital asset by a private company/unlisted public company to a limited liability partnership in the case of conversion of company into LLP. 16. Transfer of capital assets at the time of conversion of a firm/sole proprietary concern in a company, if a few conditions are satisfied. 17. Any transfer involved in a scheme for lending of any securities, if a few conditions are satisfied. 18. Any transfer of capital asset in a reverse mortgage.

	<p>19. Transfer of a capital asset (being a Government security carrying periodic payment of interest) made outside India through an intermediary dealing in settlement of securities by a non-resident to another non-resident.</p> <p>20. Transfer of a capital asset (being share of a special purpose vehicle) to a business trust in exchange of units allotted by that trust to the transferor.</p> <p>21. Any transfer by a unitholder of units held by him in the consolidating scheme of a mutual fund, made in consideration of the allotment to him of units in the consolidated scheme of the mutual fund, if the consolidation is of two or more schemes of equity oriented fund or of two or more schemes of a fund other than equity oriented fund.</p> <p>22. Transfer by a unitholder of units held by him in the consolidating plan of a mutual fund scheme, made in consideration of the allotment to him of units, in the consolidated plan of that scheme of the mutual fund.</p> <p>23. Transfer, made outside India, of a capital asset being rupee denominated bond of an Indian company issued outside India, by a non-resident to another non-resident (applicable from the assessment year 2018-19).</p>																																								
Computation of capital gain																																									
<i>Short-term capital gain</i>	It arises on transfer of short-term capital asset and it is calculated as follows— Full value of consideration <i>minus</i> cost of acquisition <i>minus</i> cost of improvement <i>minus</i> expenditure pertaining to transfer incurred by the transferor.																																								
<i>Long-term capital gain</i>	<p>It arises on transfer of long-term capital asset and it is calculated as follows— Full value of consideration <i>minus</i> indexed cost of acquisition <i>minus</i> indexed cost of improvement <i>minus</i> expenditure pertaining to transfer incurred by the transferor.</p> <p>► However, in the following cases the benefit of indexation is not available even if the capital asset is long-term capital asset—</p> <ol style="list-style-type: none">1. Bonds or debentures [other than (a) capital indexed bonds issued by the Government or (b) Sovereign Gold Bond issued by RBI under the Sovereign Gold Bond Scheme, 2015].2. Depreciable assets.3. Slump sale.4. Units/GDR/securities given in sections 115AB, 115AC, 115ACA and 115AD.5. Shares and debentures in Indian acquired by a non-resident in foreign currency, if a few conditions are satisfied.																																								
<i>Cost of improvement</i>	It does not include any expenditure on improvement incurred before April 1, 2001.																																								
<i>How to convert cost of acquisition into indexed cost of acquisition</i>	<p>Cost of acquisition × Cost inflation index (CII) of the year in which the capital asset is transferred ÷ CII of the year in which the asset was first held by the assessee [or previous owner, in cases covered by section 49(1)]. However, indexation benefit is available from 2001-02.</p> <p><i>Cost inflation index for different previous years—</i></p> <table><tr><td>2001-02</td><td>100</td><td>2006-07</td><td>122</td><td>2011-12</td><td>184</td><td>2016-17</td><td>264</td></tr><tr><td>2002-03</td><td>105</td><td>2007-08</td><td>129</td><td>2012-13</td><td>200</td><td>2017-18</td><td>272</td></tr><tr><td>2003-04</td><td>109</td><td>2008-09</td><td>137</td><td>2013-14</td><td>220</td><td>2018-19</td><td>NA</td></tr><tr><td>2004-05</td><td>113</td><td>2009-10</td><td>148</td><td>2014-15</td><td>240</td><td>2019-20</td><td>NA</td></tr><tr><td>2005-06</td><td>117</td><td>2010-11</td><td>167</td><td>2015-16</td><td>254</td><td>2020-21</td><td>NA</td></tr></table>	2001-02	100	2006-07	122	2011-12	184	2016-17	264	2002-03	105	2007-08	129	2012-13	200	2017-18	272	2003-04	109	2008-09	137	2013-14	220	2018-19	NA	2004-05	113	2009-10	148	2014-15	240	2019-20	NA	2005-06	117	2010-11	167	2015-16	254	2020-21	NA
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<i>How to convert cost of improvement into indexed cost of improvement</i>	Cost of improvement × Cost inflation index (CII) of the year in which the capital asset is transferred ÷ CII of the year in which improvement took place.																																								
<i>Exempt capital gains</i>	<p>In the following cases, capital gain is exempt under section 10—</p> <p>► Transfer of units of US64.</p> <p>► Compulsory acquisition of urban agricultural land in India owned by an individual or HUF, if the land was used for agricultural purposes by the owner (or any of his parents) during 2 years immediately prior to acquisition.</p>																																								

	<p>► Long-term capital gains on transfer of shares/ units or units of a business trust, if securities transactions tax is applicable (alternatively, the transaction is undertaken [during the previous year 2016-17 (or any subsequent year)] on a recognised stock exchange located in any International Financial Services Centre and the consideration for such transaction is paid or payable in foreign currency). With effect from the assessment year 2018-19, the aforesaid exemption shall be available in the case of transfer of equity shares (which were acquired on or after October 1, 2004), only if securities transaction tax is chargeable not only at the time of transfer but also at the time of acquisition of shares[†].</p> <p>► Capital gains which arise on conversion of an Indian branch of a foreign bank into an Indian subsidiary, if the conversion takes place in accordance with the scheme framed by RBI and subject to the conditions notified by the Central Government.</p> <p>► Capital gains which arise to a shareholder on “buy-back of shares” by a company if such shares are not listed.</p> <p>► Capital gain arising out of any award/ agreement under Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013.</p> <p>► Capital gain arising under Land Pooling Scheme of Andhra Pradesh Government pertaining to the following transactions –</p> <ul style="list-style-type: none"> - Transfer of capital asset (being land or building or both) under land pooling scheme. - Sale of land pooling ownership certificate issued under the above land pooling scheme (such certificate is given to the land owner in lieu of land transferred under the scheme). - Sale of reconstituted plot or land by said persons within 2 years from the end of the financial year in which the possession of such plot or land was handed over to the said persons.
<p>Computation of capital gains in special cases</p> <p><i>When cost of asset to the previous owner is taken into consideration</i></p>	<p>Special cases are –</p> <p>When an assessee acquired capital asset by any mode given in section 49, then at the time of its transfer, cost of acquisition to the previous owner is taken as cost of acquisition.</p> <p>► <i>Acquisition mode given under section 49</i> - In the following cases, cost of acquisition of asset to the previous owner is considered –</p> <ol style="list-style-type: none"> 1. Acquisition of a property by a member at the time of partition of Hindu undivided family. 2. Acquisition of a property by gift/Will or by succession, inheritance, etc. 3. Acquiring a capital asset by a holding company from its 100 per cent subsidiary company or <i>vice versa</i>, if the transferee-company is an Indian company.

[†] However, this restriction is not applicable if equity shares were acquired prior to October 1, 2004. Moreover, this restriction is not applicable in the case of transfer of mutual fund units (whether units were acquired before or after October 1, 2004). Moreover, if shares were acquired after October 1, 2004 in any of the following circumstances notified by the Government, the above restriction will not be available (in other words, exemption will be available even if at the time of acquisition, securities transaction tax was not paid) –

- Acquisition which has been approved by the Supreme Court, High Court, National Company Law Tribunal, SEBI or RBI.
- Acquisition by any non-resident in accordance with FDI guidelines of the Indian Government.
- Acquisition by an investment fund [referred to in sec. 115UB].
- Acquisition through preferential issue to which Chapter VII of SEBI (Issue of Capital and Disclosure) Regulations does not apply.
- Acquisition through an issue of share by a company.
- Acquisition by scheduled banks, reconstruction or securitisation companies or public financial institutions during their ordinary course of business.
- Acquisition under ESOP.
- Acquisition under SEBI (Substantial Acquisition of Shares and Takeovers) Regulations.
- Acquisition from the Government;
- Acquisition by mode of transfer (as per section 47/50B) if previous owner has acquired shares by any of the modes given in this list.

Barring the cases given above, if listed equity shares [which were acquired on or after October 1, 2004 (without paying securities transaction tax)] are transferred during the current year (even after paying securities transaction tax) capital gain exemption under section 10(38) will not be available.

	<p>4. Acquisition of a property in a scheme of amalgamation, if the transferee-company is an Indian company.</p> <p>5. Acquisition of property under a scheme of conversion of private company/unlisted company into LLP.</p> <p>6. Acquisition of property under a scheme of conversion of firm/sole-proprietary concern into company.</p> <p>► <i>Special points</i> - The following are special points–</p> <p>1. The benefit of indexation is available from the year in which the previous owner acquired the property*.</p> <p>2. To determine whether the asset is short-term or long-term, the period of holding by the previous owner is also considered.</p>
<i>Fair market value on April 1, 2001</i>	<p>If the capital asset was acquired by the assessee (or by the previous owner in the cases given above) before April 1, 2001, the fair market value of the capital asset on April 1, 2001 can be taken (at the option of the assessee) as cost of acquisition.</p> <p>► <i>Special points</i> - The following are special points–</p> <p>1. This rule is optional. The assessee may or may not adopt the fair market value on April 1, 2001 as cost of acquisition.</p> <p>2. The option is not available in the case of transfer of following capital assets - depreciable assets, goodwill of a business, trade-mark/brand name associated with a business, right to manufacture/produce an article, right to carry on business, route permits and loom hours.</p>
<i>Depreciable assets</i>	<p>If a depreciable assets is transferred, capital gain (loss) shall be calculated only in two cases–</p> <p>a. when the written down value of the block of assets on the last day of the previous year becomes zero.</p> <p>b. when the block of assets becomes empty on the last day of the previous year.</p> <p>Only in these two cases, capital gain (loss) arises on the transfer of a depreciable asset. Cost of acquisition in such case will be the depreciated value of the block of assets on the first day of the previous year <i>plus</i> actual cost of assets (falling in the same block of assets) acquired at any time during the previous year.</p> <p><i>Other points</i> - Capital gain or loss, which arises on transfer of depreciable assets, is always taken as short-term capital gain or loss.</p>
<i>Forfeiture of advance money</i>	<p>At the time of negotiating transfer of a capital asset, the transferor has forfeited any advance money. It is forfeited because the purchaser could not pay the balance consideration within the stipulated period (or it may be forfeited because of any other non-performance). The tax treatment of advance money so forfeited or retained by the assessee is as follows –</p> <p>► <i>If advance money is forfeited during the previous year 2013-14 (or any earlier previous year)</i> - It is not taxable in the hands of recipient till the capital asset (in respect of which advance money was received and forfeited) is transferred. If capital asset is not transferred during his lifetime, advance money forfeited by him will not be chargeable to tax. Conversely, if the capital asset is transferred during his lifetime, the advance money will be deducted from the cost for which the asset was acquired or the written down value or the fair market value, as the case may be, in computing the cost of acquisition.</p> <p>► <i>If advance money is forfeited during the previous year 2014-15 (or any subsequent previous year)</i> - It is taxable in the hands of recipient under section 56(2)(ix) under the head “Income from other sources” in the year in which advance money is</p>

*The Bombay High Court in *CIT v. Manjula J. Shah* [2012] 204 Taxman 691 held that indexed cost of acquisition has to be computed with reference to the year in which the previous owner first held the asset and not the year in which the current assessee became the owner of asset. Practical problems are solved in the book on the basis of this ruling of Bombay High Court.

	forfeited. Consequently, it will not be deducted from cost of acquisition when the capital asset is ultimately transferred.
<i>Conversion of capital asset into stock-in-trade</i>	<p>If capital asset is converted into stock-in-trade during a previous year relevant to the assessment year 1985-86 (or any subsequent year), the following special rules are applicable–</p> <ol style="list-style-type: none"> 1. It will be assumed that capital asset is transferred in the year in which conversion takes place. 2. Fair market value of the asset on the date of conversion will be taken as full value of consideration. 3. However, capital gain will not be taxable in the year of conversion. It will be taxable in the year in which stock-in-trade is transferred.
<i>Transfer of capital assets to a firm by way of capital contribution by a partner</i>	It is treated as transfer. The amount recorded in the books of account is taken as full value of consideration.
<i>Distribution of a capital asset by a firm to partners at the time of dissolution</i>	It is treated as transfer. Capital gain is taxable in the hands of the firm. Fair market value of the asset on the date of distribution is taken as full value of consideration.
<i>Compulsory acquisition of a capital asset</i>	<p>Initial compensation‡ is taken as full value of consideration. Capital gain is chargeable to tax in the year in which the initial compensation (or part thereof) is first received. Indexation benefit is, however, available up to the year in which the asset is compulsorily acquired.</p> <p>► <i>When additional compensation is received</i> - If a court/Tribunal/authority enhances compensation, it will be taxable in the year in which enhanced compensation or additional compensation is received. For this purpose cost of acquisition and cost of improvement are taken as <i>nil</i>. However, litigation expenses or incidental expenditure for obtaining additional compensation is deductible.</p>
<i>Capital gain on transfer of shares/debentures in the hands of non-residents</i>	If a non-resident acquires shares in, or debentures of, an Indian company by utilizing foreign currency, the gain will be calculated in the same foreign currency, which was initially utilized in acquiring shares/debentures. After calculating capital gain in foreign currency, it will be converted into Indian currency. This rule is not optional, it is compulsory. The benefit of indexation is not available.
<i>Self-generated assets</i>	<p>In the case of transfer of self-generated goodwill of a business, right to manufacture/produce an article/thing or right to carry on business, or profession, the cost of acquisition and cost of improvement are taken as <i>nil</i>. In the case of transfer of self-generated assets being tenancy right, route permit, loom hours, trade name or brand name, cost of acquisition is taken as <i>nil</i>. In these cases, the option of adopting fair market value on April 1, 2001 is not available. On transfer of any other self-generated asset, capital gain is always <i>zero</i>.</p> <p>If capital asset being goodwill of a business, right to manufacture/produce an article/thing or right to carry on business, is purchased, then at the time of its transfer, cost of improvement is taken as <i>nil</i>.</p>
<i>Bonus shares</i>	If bonus shares were allotted before April 1, 2001, cost of acquisition is the fair market value on April 1, 2001. If bonus shares are allotted after April 1, 2001, cost of acquisition is taken as <i>zero</i> .

‡However, the amount of compensation received in pursuance of an interim order of the court, Tribunal or other authority shall be chargeable to tax in the previous year in which the final order of such court, Tribunal or other authority is made.