CAPITAL GAINS ON TRANSFER OF SHARES/UNITS ETC SECTION 112A/55(2)(AC)

Explain taxability of Capital Gains.

Answer: If any capital asset has been transferred like land, building, gold etc. profit shall be called capital gains and if the asset has been transferred within a period of three years, capital gains shall be short term and shall be taxable at the normal rate and if asset is sold after 3 years, it will be long term capital gain and as per section 112, it shall be taxable @ 20% and also deductions under section 80C to 80U i.e. Chapter VI-A, shall not be allowed from long term capital gains.

In case of listed shares or units of equity oriented mutual fund etc., period of three years shall be taken as one year.

If any person has transferred listed equity shares or listed units of equity oriented mutual funds or listed units of a business trust and has paid securities transaction tax, in such cases long term capital gain shall be taxable @ 10% u/s 112A but only amount in excess of ₹1,00,000 and short term capital gains shall be covered under section 111A and shall be taxable @ 15% and deductions under section 80C to 80U i.e. Chapter VI-A, shall not be allowed from such short term capital gains.

Equity oriented mutual fund means such mutual funds in which more than 65% of the total proceeds have been invested in the equity shares of the domestic company.

Rebate u/s 87A shall be allowed from tax on LTCG or STCG 111A. (No Rebate u/s 87A from LTCG 112A)

Special provision for resident individual

In case of a resident individual if total income excluding long term capital gains and short term capital gain covered under section 111A, LTCG u/s 112A and casual income is below the amount which is exempt from income tax (i.e.2,50,000/3,00,000/5,00,000), in such cases deficiency in the exemption shall be allowed from long term capital gains or short term capital gain under section 111A or long term capital gains under section 112A as the case may be. Such benefit is not allowed to a non-resident.

Cost of Acquisition in case of Capital Gains u/s 112A

As per section 55(2) (ac),

In case of equity shares or units of equity oriented mutual funds or units of business trust which have been sold wef 01.04.2018 onwards, cost of acquisition shall be higher of

1. Cost of acquisition

2. Lower of

(a) Fair market value of such asset on 31.01.2018

(b) Actual sale value

Example

Mr. X purchased equity shares on 01.10.2015 for ₹ 1,00,000 and market value on 31.01.2018 is ₹ 5,00,000 and shares have been sold for ₹ 9,00,000 on 10.04.2018, in this case capital gains shall be computed in the manner given below:

Full value of consideration		9,00,000
Cost of acquisition		(5,00,000)
Higher of		
1. Cost of acquisition	1,00,000	
2. Lower of		
(a) Fair market value of such asset on 31.01.2018	5,00,000	

(b) Actual sale value	9,00,000	
LTCG u/s 112A		4,00,000
Tax Liability shall be		
Tax on LTCG u/s 112A (4,00,000 – 1,00,000 = 3,00,000)		
(3,00,000 – 2,50,000) x 10%		5,000
Rebate u/s 87A is not allowed		
Add: HEC @ 4%		200
Tax Liability		5,200

The purpose is not to tax capital gains accrued upto 31.01.2018

Presume in the above question the shares have been sold for ₹ 3,00,000, in this case tax treatment shall be

Full value of consideration		3,00,000
Cost of acquisition		(3,00,000)
Higher of		
1. Cost of acquisition	1,00,000	
2. Lower of		
(a) Fair market value of such asset on 31.01.2018	5,00,000	
(b) Actual sale value	3,00,000	
LTCG u/s 112A		Nil
Tax Liability shall be		Nil

The purpose is not to compute any loss if there is decrease in value after 31.01.2018

Presume in the above case shares have been sold for ₹ 40,000, tax treatment shall be

Full value of consideration		40,000
Cost of acquisition		(1,00,000)
Higher of		
1. Cost of acquisition	1,00,000	
2. Lower of		
(a) Fair market value of such asset on 31.01.2018	5,00,000	
(b) Actual sale value	40,000	

Loss u/s 112A	(60,000)
Tax Liability shall be	Nil

The purpose is to allow loss with regard to original cost.

Write a note on computation of capital gains in case of transfer of shares.
Answer: <u>Capital gains in case of transfer of shares</u>
In case of original shares, cost of acquisition shall be the amount for which the asset was purchased but if it was purchased before 2001, cost of acquisition shall be the amount for which it was purchased or its market value as on 01.04.2001 whichever is higher. In case of bonus shares, cost of acquisition shall be nil but if bonus shares are issued before 01.04.2001, cost of acquisition shall be the market value as on 01.04.2001.
In case of right shares, cost of acquisition shall be the amount for which such shares have been purchased. If right to purchase right shares has been renounced, amount received shall be considered to be short term capital gains. Cost of acquisition for the right renouncee shall be the amount paid to the person renouncing the right and amount paid to the company.
In case of long term equity shares or long term units of equity oriented mutual funds or units of business trust, capital gains shall be computed as per section 112A provided securities transaction tax has been paid, such capital gains shall be taxed @ 10% in excess of ₹ 1,00,000
In case of short term equity shares or the units, capital gains shall be computed but as per section 111A, such capital gains shall be taxed @ 15%.

<u>Illustration 1:</u> Mr. X purchased 100 equity shares in ABC Ltd. on 01.10.1995 @ ₹10 per share. The company has issued 100 bonus shares on 01.10.1998 and market value of the shares on 01.04.2001 was ₹7 per share. The company has again issued 100 bonus shares on 01.10.2012.
The company has offered 100 right shares on 01.04.2018 @ ₹140 per share though the market value is ₹250 per share. Mr. X purchased half of the shares and remaining half were renounced by him in favour of his friend Mr. Y. He has charged ₹20 per share from Mr. Y for renouncing the right.
All the shares were sold by Mr. X and Mr. Y @ ₹300 per share on 01.01.2019 and securities transaction tax has been paid. (market value on 31-01-2018 is ₹200 per share)
Mr. X has income under the head house property ₹2,20,000 and has causal income ₹50,000 and has invested ₹1,00,000 in NSC.
Mr. Y has income under the head house property ₹3,50,000 and has invested ₹30,000 in NSC.
Compute tax liability of Mr. X and Mr. Y.
(b) Presume in the above STT is not Paid.

<u>Solution:</u>	₹
***Computation of Capital Gains of* Mr. X**	
<u>Original Shares</u>	
Full value of consideration (100 x 300)	30,000.00
Less: Cost of Acquisition (100 x 200)	(20,000.00)
Long Term Capital Gain u/s 112A	10,000.00
<u>1st Bonus Shares</u>	
Full value of consideration (100 x 300)	30,000.00
Less: Cost of Acquisition (100 x 200)	(20,000.00)
Long Term Capital Gain u/s 112A	10,000.00
<u>2nd Bonus Shares</u>	
Full value of consideration (100 x 300)	30,000.00

Less: Cost of Acquisition (100 x 200)	(20,000.00)
Long Term Capital Gain u/s 112A	10,000.00
Right Shares	
Full value of consideration (50 x 300)	15,000.00
Less: Cost of Acquisition (50 x 140)	(7,000.00)
Short Term Capital Gain u/s 111A	8,000.00
Renouncing of right to purchase shares	
Full value of consideration	1,000.00
Less: Cost of acquisition	Nil
Short Term Capital Gain	1,000.00
Computation of Total Income	
Income under the head House Property	2,20,000.00
Income under the head Capital Gains	
Long term capital gains 112A (30,000-30,000)	Nil
Short term capital gains 111A	8,000.00
Short term capital gains	1,000.00
Income under the head Capital Gains	9,000.00
Income under the head Other Sources	50,000.00
Gross Total Income	2,79,000.00
Less: Deduction u/s 80C	(1,00,000.00)
Total Income	1,79,000.00
Computation of Tax Liability	
Tax on casual income ₹50,000 @ 30%	15,000
Tax on (8,000 – 8,000) @ 15% u/s 111A	Nil
Tax on normal income ₹1,21,000 at slab rate	Nil
Less: Rebate u/s 87A	(2,500)
Tax before health & education cess	12,500
Add: HEC @ 4%	500
Tax Liability	13,000

Mr. Y	
Full value of consideration	15,000.00
Less: Cost of acquisition (50 x 160)	(8,000.00)
Short Term Capital Gain u/s 111A	7,000.00
Computation of Total Income	
Income under the head House Property	3,50,000.00
Income under the head Capital Gains	7,000.00
Gross Total Income	3,57,000.00
Less: Deduction u/s 80C	(30,000.00)
Total Income	3,27,000.00
Computation of Tax Liability	
Tax on ₹7,000 @ 15% u/s 111A	1,050.00
Tax on ₹3,20,000 at slab rate	3,500.00
Less: Rebate u/s 87A	(2,500.00)
Tax before health & education cess	2,050.00
Add: HEC @ 4%	82.00
Tax Liability	2,132.00
Rounded off u/s 288B	2,130.00

Solution (b):	₹
***Computation of Capital Gains of* Mr. X**	
Original Shares	
Full value of consideration (100 x 300)	30,000.00
Less: Indexed Cost of Acquisition (100 x 10)/100 x 280	(2,800.00)
Long Term Capital Gain	27,200.00
1st Bonus Shares	
Full value of consideration (100 x 300)	30,000.00
Less: Indexed Cost of Acquisition (100 x 7)/100 x 280	(1,960.00)
Long Term Capital Gain	28,040.00
2nd Bonus Shares	
Full value of consideration (100 x 300)	30,000.00
Less: Indexed Cost of Acquisition	Nil
Long Term Capital Gain	30,000.00
Right Shares	
Full value of consideration (50 x 300)	15,000.00
Less: Cost of Acquisition (50 x 140)	(7,000.00)
Short Term Capital Gain	8,000.00
Renouncing of right to purchase shares	
Full value of consideration	1,000.00
Less: Cost of acquisition	Nil
Short Term Capital Gain	1,000.00
Computation of Total Income	
Income under the head House Property	2,20,000.00
Income under the head Capital Gains	
Long Term Capital Gain	85,240.00
Short Term Capital Gain	9000.00
Income under the head Other Sources	50,000.00
Gross Total Income	3,64,240.00
Less: Deduction u/s 80C	(1,00,000.00)
Total Income	2,64,240.00
Computation of Tax Liability	
Tax on casual income ₹50,000 @ 30%	15,000.00
Tax on (85,240 – 85,240) @ 20% u/s 112	Nil
Tax on ₹1,29,000 at slab rate	Nil
Less: Rebate u/s 87A	(2,500.00)
Tax before health & education cess	12,500.00
Add: HEC @ 4%	500.00
Tax Liability	13,000.00

Mr. Y	
Full value of consideration	15,000.00
Less: Cost of acquisition (50 x 160)	(8,000.00)
Short Term Capital Gain	7,000.00
Computation of Total Income	
Income under the head House Property	3,50,000.00

Income under the head Capital Gains	7,000.00
Gross Total Income	3,57,000.00
Less: Deduction u/s 80C	(30,000.00)
Total Income	3,27,000.00

Computation of Tax Liability

Tax on ₹3,27,000 at slab rate	3,850.00
Less: Rebate u/s 87A	(2,500.00)
Tax before health & education cess	1,350.00
Add: HEC @ 4%	54.00
Tax Liability	1,404.00
Rounded off u/s 288B	1,400.00

<u>Illustration 2:</u> Mr X has income under the head house property ₹3,50,000 and LTCG 112A ₹1,00,000. Compute tax payable.

Answer:
We have two options
<u>Option 1:</u>
Computation of Total Income

Income under the head House Property	3,50,000.00
Income under the head Capital Gains (₹1,00,000-₹1,00,000)	Nil
Gross Total Income	3,50,000.00
Less: Deduction u/s 80C	Nil
Total Income	3,50,000.00

Computation of Tax Liability

Tax on ₹3,50,000 at slab rate	5,000.00
Less: Rebate u/s 87A	(2,500.00)
Tax before health & education cess	2,500.00
Add: HEC @ 4%	100.00
Tax Liability	2,600.00

<u>Option 2:</u>

Computation of Total Income

Income under the head House Property	3,50,000.00
Income under the head Capital Gains	1,00,000.00
Gross Total Income	4,50,000.00
Less: Deduction u/s 80C	Nil
Total Income	4,50,000.00

Computation of Tax Liability

Tax on ₹3,50,000 at slab rate	5,000.00
Tax on Nil (₹1,00,000- ₹1,00,000) u/s LTCG 112A	Nil
Less: Rebate u/s 87A (Note)	Nil
Tax before health & education cess	5,000.00
Add: HEC @ 4%	200.00
Tax Liability	5,200.00

Note: Whether Rebate allowed or not is not clear , assuming not allowed as total income is more than ₹3,50,000.

<u>Illustration 3:</u> Mr X has income under the head house property ₹100,00,000 and LTCG 112A ₹1,00,000.

Compute tax payable.

We have two options

Option 1:

Computation of Total Income

Income under the head House Property	100,00,000.00
Income under the head Capital Gains (₹1,00,000-₹1,00,000)	Nil
Gross Total Income	100,00,000.00
Less: Deduction u/s 80C	Nil
Total Income	100,00,000.00

Computation of Tax Liability

Tax on ₹100,00,000 at slab rate	28,12,500.00
Add: Surcharge @ 10%	2,81,250.00
Tax before health & education cess	30,93,750.00
Add: HEC @ 4%	1,23,750.00
Tax Liability	32,17,500.00

Option 2:

Computation of Total Income

Income under the head House Property	100,00,000.00
Income under the head Capital Gains	1,00,000.00
Gross Total Income	101,00,000.00
Less: Deduction u/s 80C	Nil
Total Income	101,00,000.00

Computation of Tax Liability

Tax on ₹100,00,000 at slab rate	28,12,500.00
Tax on Nil (₹1,00,000-1,00,000)	Nil
Add: Surcharge @ 15%	4,21,875.00
Tax before marginal relief	32,34,375.00
Less: Marginal Relief	(40,625.00)

Working Note:	
Tax + surcharge @15% on income of ₹101,00,000	32,34,375
Tax + surcharge @10% on income of ₹100,00,000	(30,93,750)
Increase in tax	1,40,625
Increase in income	1,00,000
Marginal Relief (1,40,625 – 1,00,000)	40,625

Tax after marginal relief	31,93,750.00
Add: HEC @ 4%	1,27,750.00
Tax Liability	33,21,500.00

Note: Whether Surcharge is chargeable @ 10% or 15% is not clear. Assuming amount is exceeding ₹1,00,00,000 surcharge charged @ 15%

Illustration 4: Mr X has income under the head house property ₹5,00,000 and LTCG112A ₹1,00,000. Compute tax payable.

Answer:

Option1:

Computation of Total Income

Income under the head House Property	5,00,000.00

Income under the head Capital Gains (₹1,00,000-₹1,00,000)	Nil
Gross Total Income	5,00,000.00
Less: Deduction u/s 80C	Nil
Total Income	5,00,000.00

Computation of Tax Liability

Tax on ₹5,00,000 at slab rate	12,500.00
Tax before health & education cess	12,500.00
Add: HEC @ 4%	500.00
Tax Liability	13,000.00

Option2:

Computation of Total Income

Income under the head House Property	5,00,000.00
Income under the head Capital Gains	1,00,000.00
Gross Total Income	6,00,000.00
Less: Deduction u/s 80C	Nil
Total Income	6,00,000.00

Computation of Tax Liability

Tax on ₹5,00,000 at slab rate	12,500.00
Tax on Nil (₹1,00,000-₹1,00,000)	Nil
Tax before health & education cess	12,500.00
Add: HEC @ 4%	500.00
Tax Liability	13,000.00

Note: In both the option answer is same.

Illustration 5: Mr. X holds 500 shares of ABC Ltd. which were allotted to him on 22.04.2001 @ ₹30 per share. On 22.07.2018 ABC Ltd. made right issue to the existing shareholders at the rate of one share for every five shares held @ ₹20 per share. Mr. X instead of exercising his rights to obtain right shares, has exercised his right of renouncement by renouncing the said right entitlement in favour of Mr. Y @ ₹13 per right share entitlement on 04.08.2018.

(a) Determine the nature and amount of capital gain, if any, taxable in the hands of Mr. X.

(b) What will be the cost of acquisition of shares purchased by Mr. Y?

Solution: ₹

Computation of Capital Gains in the hands of Mr. X

Full value of consideration (100 x 13)	1,300
Less: Cost of acquisition	Nil
Short Term Capital Gain	1,300

Cost of acquisition of shares purchased by Mr. Y = ₹33 x 100 = ₹3,300

Illustration 6: Mr. X is a shareholder of ABC Ltd. holding 1,000 shares of the face value of ₹10 each. The company made a right issue in the ratio of 1:1 on 01.01.2019 at a premium of ₹50 per share. He renounced it in favour of Mr. Y at a price of ₹10 per share.

What is the capital gain chargeable in the hands of Mr. X? What will be the cost of the shares in the hands of Mr. Y?

Solution: ₹

Computation of Capital Gains in the hands of Mr. X

Full value of consideration (1,000 x 10)	10,000
Less: Cost of acquisition	Nil
Short Term Capital Gain	10,000

Cost of the shares in the hands of Mr. Y is ₹70 per share.

Illustration 7: Mrs. X purchases 1,000 equity shares in X Ltd. at a cost of ₹ 15 per share (brokerage 1%) in January 1998. She gets 100 bonus shares in August 2000. She again gets 1100 bonus shares by virtue of her holding on February 2005. Fair market value of the shares of X Ltd. On April 1, 2001 is ₹ 25. In January 2019, she transfers all her shares @ ₹ 120 per share (brokerage 2%). (market value on 31-01-2018 is ₹70 per share) Compute the capital gains taxable in the hands of Mrs. X for the A.Y. 2019-20 assuming:
(a) X Ltd. is an unlisted company and securities transaction tax was not applicable at the time of sale.
(b) X Ltd. is a listed company and the shares are sold in a recognised stock exchange and securities transaction tax was paid at the time of sale.

Solution:

(a) Computation of capital gains for the A.Y. 2019-20

Particulars	**₹**
1000 Original shares	
Sale proceeds (1000 × ₹ 120)	1,20,000
Less : Indexed cost of acquisition [₹ 25 × 1000 × 280/100]	(70,000)
Less : Brokerage paid (2% of ₹ 1,20,000)	(2,400)
Long term capital gain	**47,600**
100 Bonus shares	
Sale proceeds (100 × ₹ 120)	12,000
Less : Indexed cost of acquisition [₹ 25 × 100 × 280/100] [note]	(7,000)
Less : Brokerage paid (2% of ₹ 12,000)	(240)
Long term capital gain	4,760
1100 Bonus shares	
Sale proceeds (1100 × ₹ 120)	1,32,000
Less: Cost of acquisition	NIL
Less: Brokerage paid (2% of ₹ 1,32,000)	(2,640)
Long term capital gain	1,29,360
Long term capital gain	1,81,720

Note: Cost of acquisition of bonus shares acquired before 01.04.2001 is the FMV as on 01.04.2001 (being the higher of the cost or the FMV as on 01.04.2001).

(b) The long-term capital gains on transfer of equity shares through a recognized stock exchange on which securities transaction tax is paid is taxable in excess of ₹1,00,000 u/s 112A @ 10% and Indexation shall not be applicable.

Particulars	**₹**
1000 Original shares	
Sale proceeds (1000 × ₹ 120)	1,20,000
*Less : C*ost of acquisition [₹ 70 × 1000]	(70,000)
Less : Brokerage paid (2% of ₹ 1,20,000)	(2,400)
Long term capital gain u/s 112A	47,600
100 Bonus shares	
Sale proceeds (100 × ₹ 120)	12,000
Less : cost of acquisition [₹ 70 × 100]	(7,000)
Less : Brokerage paid (2% of ₹ 12,000)	(240)
Long term capital gain u/s 112A	4,760
1100 Bonus shares	
Sale proceeds (1100 × ₹ 120)	1,32,000
Less: Cost of acquisition (1100 x ₹70)	77,000
Less: Brokerage paid (2% of ₹ 1,32,000)	(2,640)
Long term capital gain u/s 112A	52,360
Long term capital gain u/s 112A	1,04,720