ECONOMIC LAWS PRACTICE
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BUDGET BUZZ

REVAMP OF CAPITAL GAINS TAX REGIME

Budget Proposal

The Finance Bill 2024 has proposed simplifications on Capital gains taxation. The changes proposed to the capital gains tax regime will have several significant impacts on all category of investors, affecting their returns, investment strategies and market behaviour. A snapshot of new capital gains tax regime as compared to the old regime is given below:

Sr No	Category of investment	Period of holding for qualifying as long-term capital assets		Tax rate on short-term capital gains		Tax rate on long-term capital gains	
		Old provision	New provision	Old provision	New provision	Old provision	New provision
1.	Listed security being shares and equity oriented mutual funds	1 year	1 year	If Securities Transaction Tax (STT) paid – 15% IF STT not paid - At normal tax rate	If STT paid – 20% IF STT not paid - At normal tax rate	If STT paid – 10% (without indexation) IF STT not paid – 20% (with indexation) or 10% (without indexation)	12.5%[1] (without indexation)
2.	Listed security unit of business trust (REIT and Invit)	3 years	2 years	If STT paid – 15% IF STT not paid - At normal tax rate	If STT paid – 20% IF STT not paid - At normal tax rate	If STT paid – 10% (without indexation) IF STT not paid – 20% (with indexation) or 10% (without indexation)	12.5%[1] (without indexation)
3.	Listed debentures and bonds (other than zero coupon bonds)	3 years	1 year	At normal tax rate	At normal tax rate	10% (without indexation)	12.5% (without indexation)
4.	Market linked debentures and Specified mutual funds[2]	Deemed to be short term	Deemed to be short term	At normal tax rate	At normal tax rate	N.A.	N.A.
5.	Other listed security	3 years	1 year	At normal tax rate	At normal tax rate	20% (with indexation benefit) or 10% (without indexation)	12.5% (without indexation)

[1] The exemption on long term capital gains on listed shares on which STT is paid is increased from INR 1,00,000 to INR 1,25,000

[2] Specified mutual funds include a mutual fund which invests 65% or more of the proceeds in debt and money market instruments. Further, the funds which invests 65% or more of the proceeds in above funds will also be classified as specified mutual funds.

6.	Zero coupon bonds	1 year	1 year	At normal tax rate	At normal tax rate	10% (without indexation)	12.5% (without indexation)
7.	Unlisted bond or debentures	3 years	Deemed to be short term	At normal tax rate	At normal tax rate	20% (without indexation)	N.A.
8.	Unlisted shares	2 years	2 years	At normal tax rate	At normal tax rate	Resident - 20% (with indexation) Non-resident – 10% (without indexation)	12.5% (without indexation)
9.	Land and building	2 years	2 years	At normal tax rate	At normal tax rate	20% (with indexation)	12.5% (without indexation)
10.	Other assets	3 years	2 years	At normal tax rate	At normal tax rate	20% (with indexation)	12.5% (without indexation)

Impact

- **Higher Tax Outflow on Listed Shares and Securities** - The increase in tax rate for long-term capital gains on listed shares and securities from 10% to 12.5% and for short-term gains from 15% to 20% will result in higher tax liabilities for investors and directly reduces the net returns from these investments. For example, if an investor had taxable long-term capital gains of INR 100,000 from listed shares, the tax liability would increase from INR 10,000 to INR 12,500. For short-term gains of INR 100,000 from listed shares, the tax would rise from INR 15,000 to INR 20,000.

- **Reduced Tax Rate on Long-Term Other Assets but Removal of Indexation Benefit** - The tax rate on other long-term assets has been reduced from 20% to 12.5%. While this seems to be beneficial at first glance, the removal of the indexation benefit can significantly impact the taxpayers. Indexation adjusts the purchase price of an asset to account for inflation, thereby reducing the taxable capital gain. Without indexation, the entire gain becomes taxable, which can be a substantial burden, especially in a case where the return on investment is less than 2.6 times the inflation rate.

- **Increased Tax on Long-Term Unlisted Shares for Non-Residents** - The tax rate on long-term unlisted shares for non-residents has increased from 10% to 12.5% which raises the tax burden on non-resident investors. This change could impact return on investment made in Indian unlisted shares by foreign investors.

ELP's Insights

Investors will need to carefully evaluate their portfolios and possibly seek professional advice to optimize their investment strategies in light of these tax changes. The proposed changes in capital gains taxation could lead to shifts in market behaviour. Moreover, sectors heavily reliant on long-term investments, such as startups, infrastructure and real estate, might find it more challenging to attract the necessary capital especially due to removal of indexation benefit, potentially slowing growth in such sectors.

In a nutshell, while the simplification of the capital gains tax regime might bring some clarity, the increased tax rates and removal of indexation benefits are likely to have a mixed impact on investors.