

An Overview of Real Estate Transactions Under Income Tax Act, 1961



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INTRODUCTION

The topic of taxation of capital gains on real estate transaction under the income tax act is live and ever interesting topic from point of view of all concerned with such taxation. This is one set of provisions in the Act which has raised maximum number of issues of interpretation. In the recent years several amendments have been brought about in the income tax act relating to computation and chargeability of capital gain. Frequent changes have only added to the complexity of an already complicated subject.

REAL ESTATE TRANSACTION

Capital gain on real estate transaction is a broad topic, the term real estate itself is a vast term but same is briefly categorized as under:

1. Sales of Land
2. Sales of Building.
3. Sales of Inherited/Gifted Property.
4. Property compulsorily acquired by the Government.

EXPLANATION OF IMPORTANT TERMS:

1. Long-term and Short-term capital asset:

- Capital asset is a asset defined under **section 2(14) of the Act**, which says it to be property of any kind held by an assessee, whether or not connected with his business or profession.
- For the purpose of computing capital gains , the capital asset is bifurcated into two categories on the basis of the duration for which they have been held by the assessee, namely:

i) Short-term Capital Asset

ii) Long-term Capital Asset



- Generally, Short-term Capital Asset means capital asset held by the assessee for less than 36 months immediately before the date of transfer, Thus Long-term Capital Asset means a capital asset held for more than 36 months.
- Profits arising on a transfer of short-term capital asset are liable to tax as any other income. On the other hand; gains arising on transfer of long-term capital asset are entitled to a concessional treatment. Thus classification of an asset as a long-term or short-term asset is therefore of considerable importance.

2. Cost of Acquisition (COA):

- Cost of Acquisition of an asset is the value for which it was acquired by the assessee. Expenses of capital nature for completing or acquiring the title to the property are includible in the cost of acquisition.
- Section 55 of Act states that where the capital asset becomes the property of the assessee before 01-04-1981, the assessee has the option to either take the actual cost of acquisition or fair market value as on 01-04-1981, whichever is more beneficial to the assessee as the cost of the asset for computation of capital gains. Where the capital asset becomes the property of the assessee by way of inheritance or gift and the previous owner of the property has acquired the same before 01-04-1981, then the Cost of Acquisition for computation of capital gains will be either the cost to the previous owner or the **fair market value of the asset as on 01-04-1981**, at the option of the assessee.
- For the following flowchart please consider the following
 - Cost of inflation index (CII) of the year in which property is transferred (F.Y. 2011-12) —785.
 - In case where the property is inherited or gifted then Cost of inflation index (CII) of the year in which property was first held by the assessee (F.Y. 2007-08)— 551.
 - In case where the property is not inherited or gifted but the same is purchased by the assessee (F.Y. 2006-07) CII— 519.



**In case of transfer of a long-term capital asset, the cost of acquisition is required to be enhanced by a factor of Cost of Inflation Index. A Large portion of gains on sale of capital asset is on account of inflation and does not represent a real profit. The benefit of indexation is given in order to mitigate this hardship.*

3. Cost of Improvement:

- Cost of improvement is a capital expenditure incurred by the assessee in making any additions/improvement or adding/increasing the value of the asset.
- For calculation of indexed Cost of improvement, CII is to be taken of the year in which improvement has taken place by the assessee or the previous owner. But in case the assessee exercises the option of substituting the FMV as on 01-04-1981 as the COA, then the expenses incurred for improvement will be added to the COA only to extent such expenses are incurred after 01-04-1981.

4. Full value of Consideration

- The starting point of computing the capital gains is ascertaining the full value of consideration received or accrued. Where the transfer is strictly for money there may not be any problem in determining the full value of consideration. However, difficulties may arise in cases where consideration is received partly in cash and partly in kind. In case consideration is partly or fully in kind, the market value of the asset received as consideration together with cash amount received will be full value of consideration.
- According to section 50C of the Act, where Sale consideration is received on transfer of land or building whether short-term or long-term is less than the Value adopted by any authority of a state government for the purpose of payment of stamp duty than the Value adopted by Stamp Duty authority is to be taken as Full value of consideration.
- When transfer of a capital asset is by way of Compulsory Acquisition under any law then Initial Compensation received from the Legal body is taken as the full value of consideration. Here one important thing to take note of is that normally capital gain is taxed in the year in



which asset is transferred but the case here is different because capital gain will be chargeable to tax in the year in which compensation is received which can be different from the year in which property is compulsorily taken over by legal body.

EXEMPTIONS

The Income tax Act grants total or partial exemptions of Capital Gains, but amount of exemption cannot exceed the quantum of capital gain. For the purpose of real estate transaction the sections which can help us to get a exemption in respect of Capital gains are 54, 54EC and 54F. The following table represents the conditions to be fulfilled in order to get the exemption.

<u>Particulars</u>	<u>Section 54</u>	<u>Section 54EC</u>	<u>Section 54F</u>
Which asset is eligible?	A residential house property.	Any Long-term Capital asset.	Any Long-term Capital asset other than residential house property.
Which asset is to be acquired to get exemption?	Another residential house property.	Bonds of NHAI or REC.	One residential house property
Time period for acquiring the above said asset?	Purchase asset within 1 year before transfer or 2 years after transfer* <u>OR</u> Construct residential house within 3 years from transfer*.	Acquire bonds within 6 months from transfer	Purchase asset within 1 year before the transfer or 2 years after the transfer* <u>OR</u> Construct residential house within 3 years from transfer*.
Revocation of Exemption.	If the said acquired asset for the purpose of exemption is transferred within 3 years from its	If the said bonds are transferred, converted into money or any loan is availed	<u>See the Foot note.</u>



	acquisition.	against such bonds within 3 years from its acquisition.	
Remarks.	If the assessee is not able to invest the whole/partial amount of capital gain for the purchase or construction then he can invest the same in "Capital gain deposit scheme account" before the due date of filing of Return of income. But the assessee has to use the said amount deposited for purchase or construction within the said period.	1.) The "Capital gain deposit scheme" is not available. 2.) Maximum amount that can be done in bonds is 50,00,000/-	1.) On the date of transfer the assessee does not own more than one residential property. 2.) The "Capital gain deposit scheme" is available.

*In case of compulsory acquisition from the date of receipt of initial compensation.

Foot note:

Revocation u/s 54F is done when,

1. Asset acquired is transferred within 3 years from its acquisition.
2. The assessee acquires another residential house property within 2 years from the date of original asset.
3. The assessee completes the construction of another residential house property within 3 years from the date of original asset.



TAXABILITY

Almost everything use for personal or investment purposes is a capital asset. When a capital asset is sold, the difference between the cost of the asset and the amount it is sold for is a capital gain or a capital loss. However, not all capital gains are treated equally. The tax rate can vary dramatically between short-term and long-term gain.

a) Long Term Capital Gain to be taxed at Flat Rate or Special Rate of 20 %.

b) Short Term Capital Gain to be taxed as any other income depending upon the slab on income in which the assessee falls.

- In case of Long-term capital gain Deduction of u/s 80C to 80U is not available.
- Further the benefit of the exemption limit i.e. maximum amount not chargeable to tax is available to long-term capital gain, only if the said limit is not being exhausted by other income other than long term capital gain i.e. other income including short-term capital gain.

SET-OFF AND CARRY FORWARD OF LOSSES

- Loss from transfer of a Short-term Capital Asset can be set off against gain from transfer of any other capital asset (Long Term or Short Term) in the same year. Loss from transfer of a Long- term Capital Asset can be set off against gain from transfer of any other long term Capital Asset only in the same year.
- If there is a net loss under the head “Capital Gains” for an assessment year, the same cannot be set off against any other head of income viz., Salaries, House Property, Business or Profession or other sources. It has to be separated into Short term Capital Loss (STCL) and long term capital loss (LTCL) and carried forward to next assessment year. In the next year, the STCL can be set off against any gains from transfer of any capital asset (Long term or Short term) and the LTCL can be set off against gains from transfer of long term capital asset only. Any unabsorbed loss after such set off can be further carried forward to next assessment year.
- Capital loss computed in an assessment year can be carried forward for eight assessment years and set off as above.



Insertion of Section 194-IA by Finance Act, 2013

The Finance Bill 2013 has introduced a new section **194-IA** “TDS on Immovable property”.

- It provides that any person, being a transferee, responsible for paying to a resident transferor any sum by way of consideration for transfer of any immovable property (other than agricultural land) shall deduct an amount equal to one per cent. of such sum as income-tax at the time of credit of such sum to the account of the transferor or at the time of payment of such sum in cash or by issue of cheque or draft or by any other mode, whichever is earlier.
- It is further provides that no deduction shall be made where consideration for the transfer of an immovable property is less than 50,00,000/-.
- Here” immovable property” means any land (other than agricultural land) or any building or part of a building
- The Tax so deducted is to be has to be deposited within 7 days from the end of the month in which the tax was deducted. Tax is to be accompanied by a challan-cum-statement in **Form 26QB**, electronically, within the specified time.
- Every person responsible for deduction of tax u/s 194IA shall furnish a certificate of TDS in Form **16B** to the payee within 15-days from the due date for furnishing the challan-cum-statement in form 26QB (i.e. within 22days of the end of the month in which the tax was deducted)
- No TDS return is required to be filled.
- This amendment will take effect from 1st June, 2013.

CONCLUSION

Capital Gain is one of the heads of income where maximum tax planning can be done especially for such real estate transactions, in order to minimize the gain to the maximum possible extent. But it is also one of areas of income tax where interpretations relating to sections differ a lot and thus support of judicial pronouncements and decisions should be taken.

