

# Direct Tax Amendments

FINANCE (NO. 2) BILL, 2024



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# Rationalization and Simplification of Taxation of Capital Gains

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# Rationalization and Simplification of Taxation of Capital Gains

- Rationalization of periods of holding:
  - **Old Law:** Three categories i.e. 12 M (listed securities), 24 M (immovable property), 36 M (others)
  - **New Law:** Two categories i.e., 12 M (listed security) and 24 M (others) – Slump Sale?
- Rationalization of capital gains tax rates:

Particular	Old Law	New law (w.e.f. 23.07.2024)
Short-term capital gains (STCG) on capital assets which are subject to STT	15%	20%
Other STCG	Normal Tax Rates	Normal Tax Rates
Long-term capital gains (LTCG) on capital assets which are subject to STT	10% (No indexation)	12.5% (No indexation)
LTCG on unlisted shares by non-residents	10% (without indexation and foreign currency translation benefits)	12.5% (without indexation but <u>subject to foreign exchange translation benefits</u> )
Other LTCG	20% (With Indexation)	12.5% ( <u>No indexation</u> )

# Taxability on Sale of Immovable Property

Particulars	Purchase of Immovable property in FY 1989-90	Purchase of immovable property in FY 2009-10	Purchase of Immovable property in FY 2016-17
Cost of Acquisition / FMV as on April 01, 2001	15,00,000	29,50,727	47,38,223
Cost of Acquisition after CII	54,45,000	72,37,256	65,15,056
Sales Consideration	1,00,00,000	1,00,00,000	1,00,00,000
Tax on gains as existing provisions	9,11,000	5,52,549	6,96,989
Tax on gains as proposed amendment	10,62,500	8,81,159	6,57,722
Difference	-1,51,500	-3,28,610	39,267



# Buy-Back of shares

# Background on buy back of shares (1/2)

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- From 1939 to 1955
  - Sec. 2(22)(d) introduced - Consideration paid on capital reduction deemed as dividend in the hands of share holder - Punjab Distilling Industries [1965] 57 ITR 1 (SC)
- From 1955 to 2000
  - Sec. 45 introduced - Consideration received on 'capital reduction' (cancellation of shares/ reduction of FV of shares) taxable as capital gains., to the extent not taxable u/s 2(22)(d) - Kartikeya Sarabhai [1997] 228 ITR 163 / G Narasimhan [1999] 236 ITR 327
- From 2000 to 2013
  - Profits on Buy back: Taxable in the hands of shareholders as capital gains. (Sec 46A)



# Background on buy back of shares (2/2)

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- From 2013 to July 2019
  - Buy back of unlisted shares – Taxed in the hands of company @ 20% of distributed income (Sec 115QA)
    - Exempt in the hands of shareholders [S. 10(34A)]
    - Distributed income → Buyback price less issue price of share
  - Buyback of listed shares continued to be taxed under section 46A
- From July 2019
  - 115QA extended to listed companies

# Buy-back of shares- Proposed Amendment

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- Proposed Amendment
  - No tax in hands on company buying back shares on or after 1 October 2024
  - Buyback proceed taxable in the hands of shareholders as deemed dividend
    - No expenses allowed
    - Chargeable to tax at applicable rates
  - Cost of acquisition of share to be allowed as capital loss
- Issues
  - What will be the treatment of income on buy-back of share of a non-resident investor?
  - Categorization of buyback under treaty- Dividend or capital gains?
    - If dividend- whether capital loss also available?
    - If capital gains - benefit of capped treaty rates not available





# Gifts by Corporates

# Section 47(iii) – Gifts between Corporates taxable

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- Present position
  - Transfer of capital asset under a gift or will or an irrevocable trust: Exempt from capital gains
  - Whether gift by corporates covered?- Exemption granted by judicial forums
    - *Prakriya Pharmachem and Ors. v. Income-tax Officer, Ward -7, [2016] 66 taxmann.com 149 (Gujarat)*
    - *Nivi Trading Ltd. v. Union of India [2015] 64 taxmann.com 92 (Bombay)*
    - *Asian Satellite Broadcast (P) Ltd. v. Income Tax Officer, Circle 6(1)(3) [2020] 119 taxmann.com 481 (Bombay)]*
  - Cross border gifts between related parties: Since income is exempt, TP provisions not applicable [*refer Amiantit International Holding Ltd, [2010] 322 ITR 678 (AAR)*]

# Section 47(iii) – Gifts between Corporates taxable

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- Proposed amendment (effective from FY 2024-25)
  - Exemption available only in case of 'transfer of capital asset by an individual or HUF' under a gift, will or irrevocable trust
  - Gift by corporates: Not exempt
  - Intention of amendment → Curb practices of tax avoidance
- Points to ponder
  - Provision may have limited application to assets where sale consideration is deemed as FMV (such as shares and immovable property)
  - In case of cross-border gifting between AEs, whether transfer pricing provisions apply?



# Sale of Shares in OFS

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## 55(2)(ac) – Present Position

- Cost of acquisition of assets covered under section 112A to be, higher of
  - i. Actual cost of acquisition (first limb)
  - ii. And lower of;
    - ❖ Fair market value (second limb) and
    - ❖ Full value of consideration (third limb)
- The existing provisions failed to capture what would be the “fair market value” of an equity share (long-term asset) offloaded in an OFS process.
- “Fair value” in such cases thus became indeterminate

Proposed Amendment – The “fair value” (second limb) of such shares sold via OFS route would be the indexed cost of acquisition by considering FY 2017-18 to be the base year for computation of indexation benefit





# Other critical amendments

# Withdrawal of Equalisation Levy 2.0

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- Present position

- EQL at 2% was introduced by Finance Act 2020 ('EQL 2.0') to levy tax on consideration received by a non-resident e-commerce operator from e-commerce supply or services made or facilitated
- A corresponding exemption was provided under section 10(50) the IT Act for income arising from e-commerce supply or services which were liable to EQL

- Proposed amendment

- EQL 2.0 proposed to be withdrawn with effect from 1 August 2024
- Reason → provisions of EQL ambiguous and leads to compliance burden
- Exemption under section 10(50) of the IT Act withdrawn with effect from 1 August 2024
- Amendment appears to be also driven by Pillar 1 solution in pipeline

- Issues

- Can income of e-commerce operators be taxed by invoking SEP provision?



# Annexure

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## India – US Tax Treaty – Dividends and Capital Gains Article

- The term "dividends" as used in this Article means income from shares or other rights, not being debt-claims, participating in profits, income from other corporate rights which are subjected to the same taxation treatment as income from shares by the taxation laws of the State of which the company making the distribution is a resident ; and income from arrangements, including debt obligations, carrying the right to participate in profits, to the extent so characterised under the laws of the Contracting State in which the income arises
- Except as provided in Article 8 (Shipping and Air Transport) of this Convention, each Contracting State may tax capital gains in accordance with the provisions of its domestic law.

## India – Netherlands Tax Treaty – Capital Gains Article

5. Gains from the alienation of any property other than that referred to in paragraphs 1, 2, 3 and 4 shall be taxable only in the State of which the alienator is a resident.



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