

# Mode of Computation [Full Value Ofconsideration] With Reference To Capital Gain Taxation under Income Tax Act, 1961.

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**ABSTRACT:** This research paper is about the computation of full value of consideration in case of transfers with a reference to capital gain taxation under Income Tax Act, 1961. Full value of consideration has different meaning for different types of transfers of capital assets under several different situations. Further this paper discusses about the possible and permissible deductions and exclusions of certain expenditures from the full value of consideration in case of transfer of different capital assets. Further the way in which indexation is done during deduction of cost of acquisition and cost of improvement has also been discussed with and without giving indexation benefits based on cost inflation index for year of acquisition and year of transfer. References of various case studies are cited for the purpose of explaining the judicial standing of provisions related to computation of full value of consideration and deduction of expenditure from it to find out net Capital Gain or Capital Loss with under section 48 of Income Tax Act, 1961.

**KEYWORDS:** Consideration, Indexation, Expenditure, CII, Transfer, Capital Gain, Acquisition.

## I. INTRODUCTION

“The income chargeable under the head “Capital gains” shall be computed, by deducting from the full value of the consideration received or accruing as a result of the transfer of the capital asset the following amounts, namely: —

1. expenditure incurred wholly and exclusively in connection with such transfer;
2. the cost of acquisition of the asset and the cost of any improvement thereto:

PROVIDED that in the case of an assessee, who is a non-resident, capital gains arising from the transfer of a capital asset being shares in, or debentures of, an Indian company shall be computed by converting the cost of acquisition, expenditure incurred wholly and

exclusively in connection with such transfer and the full value of the consideration received or accruing as a result of the transfer of the capital asset into the same foreign currency as was initially utilised in the purchase of the shares or debentures, and the capital gains so computed in such foreign currency shall be reconverted into Indian currency, so, however, that the aforesaid manner of computation of capital gains shall be applicable in respect of capital gains accruing or arising from every reinvestment thereafter in, and sale of, shares in, or debentures of, an Indian company:

PROVIDED FURTHER that where long-term capital gain arises from the transfer of a long-term capital asset, other than capital gain arising to a non-resident from the transfer of shares in, or debentures of, an Indian company referred to in the first proviso, the provisions of clause (ii) shall have effect as if for the words “cost of acquisition” and “cost of any improvement”, the words “indexed cost of acquisition” and “indexed cost of any improvement” had respectively been substituted:

PROVIDED ALSO that nothing contained in the first and second provisos shall apply to the capital gains arising from the transfer of a long-term capital asset being an equity share in a company or a unit of an equity-oriented fund or a unit of a business trust referred to in section 112A:

PROVIDED ALSO that nothing contained in the second proviso shall apply to the long-term capital gain arising from the transfer of a long-term capital asset, being bond or debenture other than— capital indexed bonds issued by the Government; or

Sovereign Gold Bond issued by the Reserve Bank of India under the Sovereign Gold Bond Scheme, 2015:

PROVIDED ALSO that in case of an assessee being a non-resident, any gains arising on account of appreciation of rupee against a foreign currency at the time of redemption of rupee denominated bond of an Indian company held by

him, shall be ignored for the purposes of computation of full value of consideration under this section:

PROVIDED ALSO that where shares, debentures or warrants referred to in the proviso to clause (iii) of section 47 are transferred under a gift or an irrevocable trust, the market value on the date of such transfer shall be deemed to be the full value of consideration received or accruing as a result of transfer for the purposes of this section:

PROVIDED ALSO that no deduction shall be allowed in computing the income chargeable under the head "Capital gains" in respect of any sum paid on account of securities transaction tax under Chapter VII of the Finance (No. 2) Act, 2004.

For the purposes of this section, —

- (i) "foreign currency" and "Indian currency" shall have the meanings respectively assigned to them in section 2 of the Foreign Exchange Regulation Act, 1973 (46 of 1973);
- (ii) the conversion of Indian currency into foreign currency and the reconversion of foreign currency into Indian currency shall be at the rate of exchange prescribed in this behalf;
- (iii) "indexed cost of acquisition" means an amount which bears to the cost of acquisition the same proportion as Cost Inflation Index for the year in which the asset is transferred bears to the Cost Inflation Index for the first year in which the asset was held by the assessee or for the year beginning on the 1st day of April, [2001], whichever is later; [With effect from A.Y. 2018-19, figures "1981" substituted by "2001"]
- (iv) "indexed cost of any improvement" means an amount which bears to the cost of improvement the same proportion as Cost Inflation Index for the year in which the asset is transferred bears to the Cost Inflation Index for the year in which the improvement to the asset took place;

"Cost Inflation Index" in respect of previous year, means such Index as the Central Government may, having regard to seventy-five per cent of average rise in the Consumer Price Index for the immediately preceding previous year to such previous year, by notification in the Official Gazette, specify, in this behalf."

KEY NOTE: - The dictionary meaning of the word "full" is "whole or entire, or complete". The word "full" has been used in this section in contrast to "a part of the price". The expression "full value" means the whole price without any deduction whatsoever and it cannot refer to the adequacy or inadequacy of the price bargained for.

Nor has it any reference to the market value of the capital asset which is the subject-matter of the transfer. The consideration for the transfer of the capital asset is what the transferor receives in lieu of the asset he parts with, namely money or money's worth

## II Method of Computing Capital Gain [Section 48]

Section 48 - Short term capital gains	
(i)	Full value of consideration
(ii)	Less: Cost of Acquisition
(iii)	Less: Cost of Improvement
(iv)	Less: Expenses on transfer
(v)	Short Term Capital Gains

Section 48 - Long term capital gains	
(i)	Full value of consideration 100
(ii)	Less: Cost of Acquisition
(iii)	Less: Cost of Improvement
(iv)	Less: Expenses on transfer
(v)	Long Term Capital Gains

<b>Formula for Indexation</b>	
Indexed Cost of Acquisition:	
Cost of acquisition x $\frac{\text{Cost Inflation Index for the year of transfer}}{\text{Cost Inflation Index for the year of acquisition}}$	
Indexed Cost of Improvement:	
Cost of Improvement x $\frac{\text{Cost Inflation Index for the year of transfer}}{\text{Cost Inflation Index for the year of improvement}}$	

### KEY NOTE

1. No Indexation bonds or debentures even if LTCG (Proviso 3 to section 48)
2. However, indexation shall be done for Sovereign Gold Bond

<b>Section 48: Full Value of Consideration</b>		
General cases	Consideration in cash	Amount received or receivable
	Consideration in kind	Fair Market Value of asset
Special Cases	45(1A)	Insurance claim
	45(2)	Fair Market Value on date of conversion of asset into SIT
	45(3)	Admission of partner. Amount recorded in books of

		accounts
	45(4)	Dissolution of Firm. Fair Market Value as on date of distribution
	45(5)	Initial compensation
	50C	Land & Building: Higher of Stamp value or consideration

Following are the bases where full value of consideration is determined on notional basis:

- 1) Capital gain generated by a non-resident at the time of redemption of rupee denominated bonds of an Indian company held by him [Fourth proviso to section 48]

**AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - The following amount shall be excluded from full value of consideration: - Amount equivalent to appreciation of rupee between the date of issue and the date of redemption against the foreign currency in which the investment is made (applicable from the assessment year 2017-18)

- 2) Share/debenture/warrants/allotted by an employer to an employee under notified Employees Stock Option Plan/Scheme and such shares, etc., are gifted by the concerned employee to any person (Fifth proviso to section 48]

**AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Market value at the time of gift

- 3) Money or other asset received under any insurance from an insurer due to damage or destruction of a capital asset [Section 45(1A)]  
**AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Value of money or the fair market value of the asset (on the date of receipt)
- 4) Conversion of capital asset into stock in trade (Section 45(2)). **AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Fair market value of the capital asset on the date of conversion.
- 5) Transfer of capital asset by a partner/member to firm/association of persons/ body of individuals as his capital contribution (Section 45(3)). **AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Amount recorded in the books of account of

- the firm/association of persons/body of individuals as the value of the capital asset.
- 6) Distribution of capital asset by firm/association of persons/body of individuals to its partners/members on its dissolution. [Section 45(4)]. **AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Fair market value of such asset on the date of transfer.
- 7) Transfer by an individual/HUF (i.e. owner) of land /building under a "specified agreement" i.e. a joint development agreement) to a developer. [Section 45(5A)]. **AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** -Stamp duty value (on the date of issue of completion certificate) of share of the owner in the developed property as increased by cash consideration, if any [applicable from the assessment year 2018-19]
- 8) Money or other assets received by shareholders at the time of liquidation of the company. [Section 46(2)].**AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Total amount plus market value of assets received on the date of distribution less amount assessed as deemed dividend under section 2(22)(c).
- 9) In case of transfer of land or building when sale consideration declared in the conveyance deed is less than the value adopted for the purpose of stamp duty by Stamp Valuation Authority of the State Government (Section 50C). **AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - The value adopted by the Stamp Valuation Authority of the State Government.
- 10) Transfer of unlisted shares in a company at less than fair market value [Section 50CA].**AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Fair market value of such shares (to be determined as prescribed) (applicable from assessment year 2018-19).
- 11) Where the consideration received or accruing as a result of the transfer is not ascertainable or cannot be determined. [Section 50D].**AMOUNT WHICH IS TAKEN AS FULL VALUE OF CONSIDERATION:** - Fair market value of the said asset on the date of transfer (applicable from assessment year 2013-14).

### III.Allowable expenses on transfer of capital assets

There are some expenses that are incurred in the process of selling a capital asset. You are

allowed to deduct expenses from sale proceeds from a capital asset, that wholly & directly relate to the sale or transfer of the capital asset. In other words, in computing capital gains, any expenditure incurred wholly and exclusively in connection with transfer shall be allowed as deduction. These are the expenses which are necessary to affect the transfer. These are deductible from full value of consideration.

#### IV. Wholly and exclusively

The main condition that any expenditure has to fulfill for the purpose of being allowed as a deduction is that this has to be wholly in connection with the transfer. It cannot be that there is a small element that is related to the transfer and this leads to the whole amount being considered for the deduction. There has to be an exclusive element of the end use which has to be the transfer of the capital asset. So if there are some vague claims saying that these are incurred for the purpose of the transfer then they are likely to be disallowed. Since the basic conditions are known it is important that there is a proper look at all the conditions to see that they are in line with the requirements.

#### V. Deduction of expenditure

Section 48 makes it clear what can be deducted under section 48(i) is expenses incurred wholly and exclusively in connection with the transfer.

##### 1) In case of sale of a house property

Following expenses are deductible from the total sale price of capital asset: —

- a) **BROKERAGE OR COMMISSION PAID FOR SECURING A PURCHASER:** This is one of the most common expenses that is incurred at the time of the transfer due to the fact that in many cases it is not possible to sell the property or the capital asset without the help of a broker or an intermediary. There would have to be some payment of fees to the broker at the time of the transfer of the asset and hence this would be a part of the total receipt that would have to be reduced in order to arrive at the final figure. It was held that expenditure incurred on payment of legal fees, brokerage, commission, etc. in connection with the transfer was allowable as deduction under section 48(1)(a)(i). — (Sah RoopNarain V. CIT (1987) 32 Taxman 453 (Raj))
- b) **COST OF STAMP PAPERS OR REGISTRATION FEES BORNE BY THE VENDER (SELLER):** There are different ways in which the sale agreement could be

structured. At the time of the transfer of the property there would have to be stamp duty or registration fees that have to be paid to the government for the change of name and other details in the property. When this is the case then the next thing to look at is who is going to bear these charges. It could be that the seller is bearing the charges in which case the amount can actually be claimed as a reduction from the amount of the total receipts. Amounts spent on stamp duty and registration charges for transfer were held deductible entirely, as expenditure incurred in connection with the transfer. — [Abdul Qayume v. CIT (1990) 184 ITR 404 (All)]

- c) **Travelling Expenses In Connection With Transfer (Sale):** It could also be that the individual who holds the property is living at some other place and hence would have to travel to the place where the property is located for the purpose of completing the requirements of sale. This would ensure that there are some amounts that are actually spent here which would actually be for the purpose of the transfer process. If this is the case then it would be considered as an amount that is spent for the property and this can be reduced from the amount received in the process of calculation of the gains.

**KEY NOTE:** Travelling expenses in connection with transfer may also be incurred after the transfer has been affected.

- d) **Litigation Expenses For Claiming Enhancement In Compensation:** There are different kinds of expenses that are incurred in the entire process of completing the sale of the property and there are situations where there might be some expenses incurred as litigation expenses. This could be for a property where there is a compulsory acquisition so there is some dispute about the valuation and this has been incurred in the process of getting a better compensation or for highlighting a point that has been missed in the calculation. This might also happen in case there is some dispute over the property valuation with the buyer and hence this reason has to be taken carefully into consideration. The whole idea is that the amount should have been spent as a part of the whole process of transfer.
- e) **Where property has been inherited,** expenditure incurred with respect to procedures associated with the will and inheritance, obtaining succession certificate, costs of executor, may also be allowed.

- f) Advertisement cost incurred by the seller to get buyer.
- 2) **In case of sale of jewellery:** - Where jewellery is sold and a broker's services were involved in **VI Expenditure allowed under other heads of income**

The expenses that you deduct from the sale price of assets for calculating capital gains are not allowed as deduction under any other head of the Income Tax, these can be claimed only once. In other words, any expenditure allowed as deduction under any other heads of income, i.e. Income from House Property, Profits and Gains of Business or Profession or Income from Other Sources cannot be allowed as deduction from the sale price of assets for calculating capital gains

#### **VII Amount paid to tenants to get the land vacant.**

Amount paid to tenant for vacating the property is an expenditure incurred wholly and exclusively in connection with the agreement of sale which preceded the transfer and in fulfillment of a condition of sale. Therefore, the same will be treated as expenditure under section 48(i). — [CIT v. A. Venkataraman (1982) 10 Taxman 298 (Mad.). See also Seventh ITO v. L.K.M. Hussain Beevi (1988) 26 ITD 17 (Mad)]

The assessee, owner of certain land, which was in possession of two tenants, entered into an agreement for sale to a third party who insisted on getting vacant possession of the land. Consequently, the assessee paid certain amounts to the tenants to get the land vacated. It was held that the amount paid to tenants was allowable as deduction in computing capital gains under section 48(1). — [CIT v. Venkataraman (A) (1982) 137 ITR 846 (Mad); CIT v. Shakuntala Rajeshwar (1986) 160 ITR 840 (Del)].

**CONTRARY VIEW** It was held that the amount paid by the landlord to the tenants for surrendering their tenancy rights in order to enable the landlord to receive full compensation in case of compulsory acquisition will not be deductible as there was no obligation in this case to hand over the vacant possession of the land to the Government. — [CIT v. R. Ranja Setty (1986) 159 ITR 797 (Karn)]. It was held that the amount paid to mother having right of residence in the property, for obtaining relinquishment of such right was deductible under section 48(1). — [CIT v. Soundararajan (CV) (1984) 150 ITR 80 (Mad)]. It was held that expenditure incurred in conducting land acquisition reference case before the Civil Court for enhanced compensation is expenditure incurred wholly and exclusively in connection with

securing a buyer, the cost of these services can be deducted.

the transfer of capital asset and is an allowable deduction. — [CIT v. M. Subaida Beevi (1986) 160 ITR 557 (Ker)]

#### **IX Need not be prior to transfer**

It is not necessary that the expenditure must have been incurred prior to the passing of the title. It is immaterial whether it was incurred prior or subsequent to the transfer. What is important is, it must be incurred and exclusively in connection with or in relation to the transfer. — [CIT v. Dr. P. Rajendran (1981) 127 ITR 810 (Ker)]

#### **X Expenditure incurred on payment of legal fees, brokerage, commission, etc.**

It was held that expenditure incurred on payment of legal fees, brokerage, commission, etc. in connection with the transfer was allowable as deduction under section 48(1)(a)(i). — [Sah Roop Narain v. CIT (1987) 32 Taxman 453 (Raj)]

#### **XI Expenditure for getting no objection certificate (NOC) for sale of flat.**

Assessee sold a flat in a housing co-operative society. It was held that payment of Rs. 4,00,000 (which included Rs. 25,000 as transfer charges and balance Rs. 3,75,000 as voluntary contribution to the society) made by the assessee to the society for getting No Objection Certificate (NOC) for sale of flat shall be treated as expenses of transfer as entire amount of Rs. 4,00,000 is necessary expenditure for transfer of flat. — [Damodar G. Nagalia v. ACIT (2007) 12 SOT 599 (Mum-Trib.)]

#### **XII Conclusion**

Looking back on this project, the overall outcome of results to be observed. This can be evaluated by looking at how well our objectives were met. Our first objective was to figure out the full value of consideration net of all allowable expenses in case of transfer of different capital assets on different occasions. Our next objective was to compute short term capital gains, long term capital gains, indexed cost of acquisition and indexed cost of improvement and expenditure allowed to be adjusted or deducted against the full value of consideration. Our subsequent objective was to determine the amount of full value of consideration in case of transfer of different type of capital assets. Finally we can say that computing of full value of consideration and allowable

expenditure to find out amount of capital gain is not uniform for all kind of transfers of several capital assets and we are in a position to comfortably conclude that section 48 is a very a comprehensive section which deals with computation of full value of consideration in case of capital gain taxation under Income Tax Act. 1961.

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