LTCG Tax on Equity is Only Logical

What is the issue?

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- 10% LTCG tax has caused angst among many investors and has also contributed to the recent share market weakness.
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- But this move is justified as there is no need to accord preferential treatment for share capital as opposed to debt instruments.
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Why should LTCG on Equity be taxed?

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- The recent budget slapped a 10% tax on long-term capital gains above Rs. 1 lakh on listed equity shares and equity mutual funds.
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- There is little logic in why equity instruments should be tax exempted, when debt instruments such as bank fixed deposits, don’t have exemptions.
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- Notably, the latter is what forms the mainstay of the population.
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- Also, equity has been delivering massive gains to investors over the past few years, even as debt investors are staring at whittled-down returns.
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- Further, the finance minister noted that tax returns filed in 2017-18 indicate that LTCG tax could significantly boost revenues.
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On what grounds is concept of LTCG on equity opposed?

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- Some vouch that equity has higher risks and hence deserves tax exemptions.

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- Further, some reason that tax breaks will help in promoting equity instruments, which are currently still very restricted in India.
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- But investors ought to know what they are getting into and align their return expectations accordingly.
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- While the introduction of LTCG Tax has caused disturbance in the short-term, things will slowly but surely adjust to the new-normal.
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What are some of the teething issues with the current proposal?

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- **STT -** One major complain from investors is that while LTCG tax has been re-introduced, the securities transaction tax (STT) still remains.
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- Notably, STT was introduced in 2004 in tandem to replace the tax on LTCG and hence should ideally be retracted now.
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- In any case, STT revenue was quite small, at less than Rs. 10,000 crores a year.
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- **Inflation Indexing -** LTCG on equity is taxed at 10%, which is much lower than the 20% LTCG tax on other asset - like gold, real estate and debt funds.
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- But these other assets are inflation indexed, which helps them to adjust gains by accounting for inflation effects, which helps in reducing taxes.
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- As cost indexation is a fair principle that results in taxing only real, inflation-adjusted returns, LTCG on equity too needs to be inflation indexed.
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- This will protect investors against high inflation risks and needs to be considered even if it means increasing the tax rate.
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- **STCG Tax -** “Short-Term Capital Gains Tax” on equity (which covers stocks held for 12 months or less), is still being taxed at a mere 15%.
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- This too is much lower than the tax on short-term gains on many other asset classes and hence needs to be hiked.
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- **Anomalies -** While the LTCGs on equity are now taxed, capital gains on

“Insurance-cum-Investment Products” continue to be exempted.
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- As this would give the latter an unfair advantage and could distort the capital market patterns, it needs to be corrected.
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Source: Business Line

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