Paying tax on capital gains and the paperwork involved

Capital gains accrue when an investor sells an asset for profit. The income tax laws define capital assets and mandate that investors pay the applicable tax on short- or long-term gains. The holding period for the capital asset is used to determine the classification. The investor has to account for all such gains in a given financial year and pay the applicable tax before filing his income tax return.

Liability: Capital gains tax is payable on the sale of a capital asset, depending on the tax rate and minimum holding period for the asset. If the sale results in gain, there is a tax liability.

Multiple sales: All transactions in a financial year have to be taken into account to ascertain tax liability. If there are multiple transactions, the first-in, first-out rule is applied: what was acquired first is assumed to be sold first.

Payment: In case of individuals who have to get their accounts audited for tax purposes, any applicable tax on capital gains has to be paid as part of advance taxes. In other cases, it is paid as a self-assessment tax, before the filing of income tax return.

Setting off losses: Capital losses can be set off against gains if the investor has filed the returns on time. Delayed filing means he can't avail of the benefit.

STT: In cases where the securities transaction tax (STT) has been paid, the tax rate is nil or low. Investors should keep the proof of STT payment.

Points to note

Failing to pay tax on capital gains amounts to tax evasion. Since transactions are tracked by the Tax Information Network, the IT Department can send notices for proof of payment.

The gains accruing from frequent trading in shares or derivatives are also subject to tax. It is a good practice to account for these before filing returns.

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