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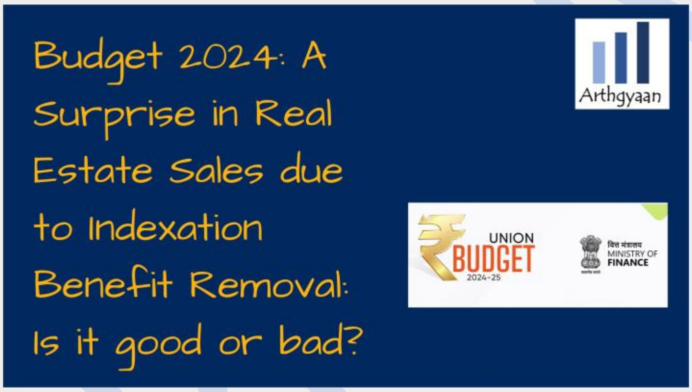
1. What is indexation in calculating long term capital gains tax? Does the removal of indexation benefit in the Budget mean you will pay more tax?

Why in News?

The changes in the long-term capital gains (LTCG) tax regime, particularly the withdrawal of the indexation benefit, has emerged as one of the most contentious decisions announced in the Union Budget for 2024-25. The announcement initially led to confusion and trepidation among various sections, prompting the government to issue a string of clarifications and explanations, claiming that it will be beneficial in most cases.

What is the concept of indexation, and what could be the consequences of the removal of indexation benefit from LTCG computation and related changes in the taxation regime?



What is indexation?

Indexation is the process of adjusting the original purchase price of an asset or investment in order to neutralise the impact of inflation on it. Put simply, it involves revising upward the cost of acquisition of an asset based on the inflation over the period for which it was held.

Inflation reduces the value of money over time, and therefore, when an asset is sold or an investment is redeemed, indexation helps in arriving at the cost of acquisition with the impact of inflation over the holding period factored in.

The cost of acquisition thus arrived at, is called the indexed cost of acquisition. It resets the base for calculation of gains or losses from the sale or redemption. The returns calculated on the indexed cost of acquisition are generally seen as more realistic than absolute gains calculated on the basis of the actual price at the time of purchase.

Without indexation, particularly in cases where the asset was held for an extended period, the gains may appear extremely high, but they may not paint a realistic picture. This is mainly because the inflationary impact on the asset’s value was not taken into account. Now, if the gains accrued on the sale of assets or redemption of investments are taxed, the absence of the indexation benefit would increase the tax outgo, assuming that the rate of tax stays the same.

What has the government done now?
The new LTCG regime proposed in the Union Budget for 2024-25 presented earlier this week by Finance Minister Nirmala Sitharaman does away with the indexation benefit available for calculation of LTCG on property, gold, and other unlisted assets, while reducing the LTCG tax rate to 12.5% from 20%.

For properties and other assets purchased prior to 2001, the fair market value as on April 1, 2001 would be considered as the cost of acquisition. According to the government, this exception has been made as even in the old LTCG tax regime, the same principle was used to determine the acquisition cost for such assets. This specific measure, the government argues, will ensure that inherited ancestral property and property bought decades ago is not subject to supernormal tax.

The government has justified its decision saying that it would simplify the capital gains tax structure without causing a loss to most taxpayers. This simplification, which removes the differential tax rates for various classes of assets, would help both taxpayers and tax authorities, the government has said.

What made people nervous, and nudged the government to make efforts to calm frayed nerves?
There was confusion and apprehension, especially with regard to the residential real estate sector. The big fear was that the changes would result in a large increase in the LTCG tax liability for those who were looking to sell property. Sensing the anxiety, the Finance Ministry and Income Tax Department started issuing clarifications.

According to the government, the new LTCG tax regime, even without the benefit of indexation, would be beneficial in the vast majority of cases in the property sector.

Based on these assumptions, the Department said that for a property held for five years, the new regime would be beneficial when the value has appreciated 1.7 times or more, while for a property held for 10 years, the new regime would be beneficial when the value has increased to 2.4 times or more. For a property purchased in 2009-10, the new LTCG tax regime would be beneficial if the value has increased to 4.9 times or more.

The government also clarified that rollover benefits have not been touched, which means that if capital gains are invested in Section 54EC bonds or used for buying or constructing residential real estate up to specified limits, LTCG would be exempt from tax.

Have the government's explanations satisfied stakeholders?
Various industry players and analysts have flagged concerns. There are apprehensions that the new regime without indexation benefit is likely to result in an increase in secondary market real estate sales, as people would not want to hold on to assets for more than 3-5 years.

Another concern that has been flagged by some industry watchers and Opposition lawmakers is that the new regime may incentivise the use of cash in property transactions, as sellers will be tempted to deflate the actual transaction value on paper in order to pay less tax.

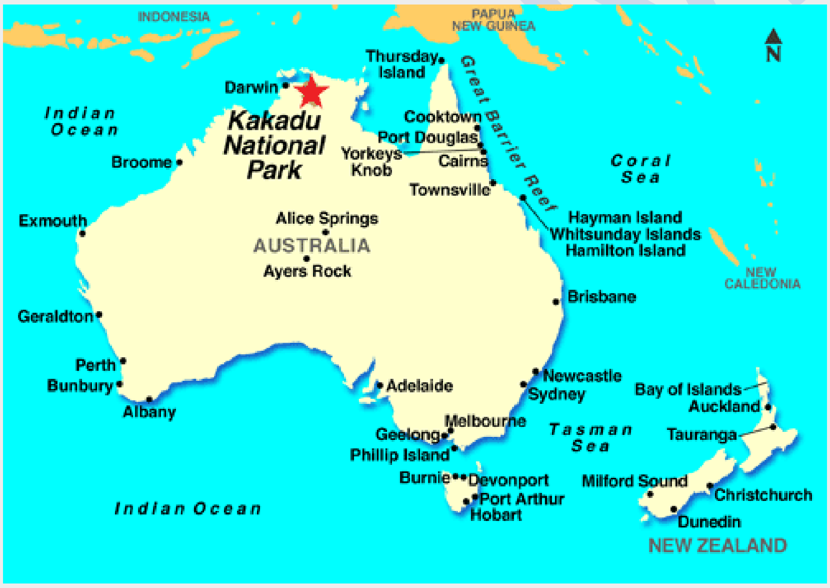
One criticism that the move has attracted from various sections is the absence of grandfathering for purchases made over the past 24 years. Grandfathering is a provision that allows an old rule or law to be applicable to some or all situations up to a certain date, while the new rule or law is applicable to all situations after that date.

In the context of the new LTCG tax regime, grandfathering would refer to extending the indexation benefit till the time the old regime was effective — July 2024. Such a measure could have entailed using the current fair market value of assets as the base, like it is done for properties acquired before 2001. The government, however, claims that the reduction in LTCG tax rate by 7.5 percentage points offsets the benefit that such grandfathering would have provided.

Relevance: GS Prelims & Mains Paper III; Economics
Source: Indian Express

2. Why Australia has banned mining in one of the world's largest uranium deposits

Introduction
Australia took steps recently to ban mining at an Indigenous site surrounded by Kakadu National Park, which is home to one of the world's largest deposits of high-grade uranium.



Rationale by PM
Prime Minister Anthony Albanese said the heritage-listed national park would be extended to include the Jabiluka site, which has long been in the sights of mining companies seeking to exploit it against the wishes of its Indigenous custodians, the Mirarr people.

The prime minister said the planned extension of the park was in line with the wishes of the Mirarr.

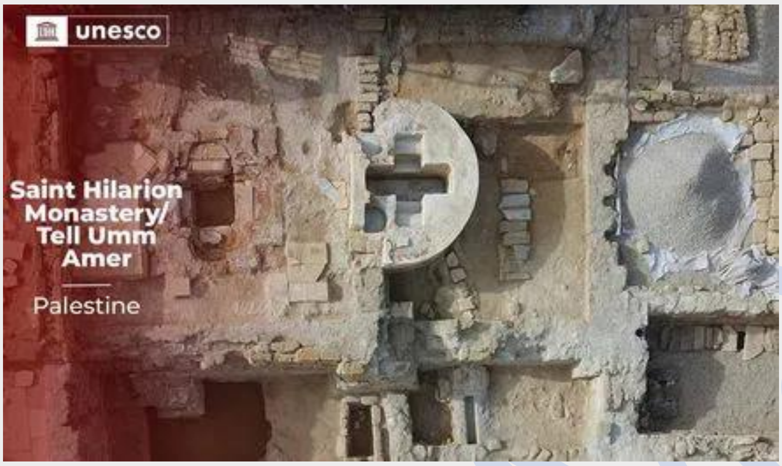
View of Opposition
The move comes after the opposition conservative Coalition recently unveiled plans to build nuclear power plants across the country if it wins the next election, overturning a 26-year nuclear ban.

Relevance: GS Prelims
Source: Indian Express

3. Gaza's Tell Umm Amer in the World Heritage Site List

The World Heritage Committee (WHC) recently decided to include the Palestinian site of Tell Umm Amer in both the UNESCO World Heritage Site List and the Lost of World Heritage in Danger during its 46th session in New Delhi.

Also known as the 'Monastery of Saint Hilarion', the site lies in the Gaza Strip which continues to reel under Israel's relentless assault.



Fourth century monastery

Situated on the coastal dunes of the Nuseirat Municipality, just 10 km south of Gaza city, the ancient Christian monastery was founded in the fourth century by Hilarion the Great (291-371 CE), considered by some to be the father of Palestinian monasticism.

Born in Tabatha, close to where his monastery would eventually come up, Hilarion became a monk at the age of 15. As his fame grew, and people began coming to him for miracles, his small hermitage went on to become a thriving monastery, which attracted followers from all over, many of whom would choose Hilarion's mendicant lifestyle.

The present-day archaeological remains of the site span more than four centuries, from the time of Hilarion to the Umayyad period.

The monastery was likely abandoned after a seventh century earthquake, only to be uncovered by local archaeologists in 1999.

Much-needed protection

With Israel's ongoing onslaught reducing much of the Gaza strip to rubble, monuments and sites of cultural significance have not been spared either.

This is why Tell Umm Amer's inclusion in the aforementioned UNESCO lists matters. The World Heritage Convention of 1972, of which Israel is a party to, sets out duties for identifying, protecting, and preserving World Heritage sites. Crucially, states cannot take any deliberate measures which are likely to cause direct or indirect damage to this site.

In December 2023, UNESCO's Intergovernmental Committee for the Protection of Cultural Property in the Event of Armed Conflict had already decided to grant 'provisional enhanced protection' to the monastery under the 1954 Hague Convention and its Second Protocol.

The inclusion on the list of World Heritage in Danger automatically opens the door to enhanced international technical and financial assistance mechanisms to guarantee the protection of the property and, if necessary, to help facilitate its rehabilitation, the UNESCO statement on Friday said.

Relevance: GS Prelims; International Organisations
Source: Indian Express