Section 54F: Avoid capital gains tax on jewellery sale with house buy

The house purchase must be via registered sale deed and within specified time limit

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The Bengaluru bench of the Income Tax Appellate Tribunal (ITAT) recently granted a deduction on long-term capital gains (LTCG) from the sale of inherited jewellery. This decision came after an assessing officer (AO) had earlier denied the benefit under Section 54F of the Income-Tax Act, 1961, which permits taxpayers to claim an exemption on LTCG from the sale of capital assets other than house property.

"If a taxpayer sells assets such as stocks, bonds, jewellery, or gold for a profit (long-term capital gains), they can avoid paying taxes on that profit by using the proceeds to purchase a new house," says Akarsh Garg, partner, Trilegal Associates.

The verdict

The ITAT affirmed that the exemption under Section 54F applies to capital gains from the sale of inherited gold and jewellery, provided the gains are reinvested in purchasing a residential house through a registered sale deed.

"The Income-Tax (I-T) Department had challenged the veracity of the transaction involving the sale of inherited gold, questioning whether the assessee actually possessed such gold and labelling the entire transaction as a sham," says Garg from Triolegal Associates.

The ITAT rejected the AO's decision. "The tribunal concluded that the sale price of inherited jewellery cannot be taxed as income arising from 'other sources' but rather should be treated as a long-term capital asset inherited from the assessee's mother-in-law," says Mohit Garg, managing partner, Lex Panacea.

Who is eligible?

The exemption under Section 54F is available to individual or Hindu Undivided Family (HUF) taxpayers who earn long-term capital gains (LTCG) from the sale of an asset other than residential property, provided they reinvest the gains in purchasing or constructing a new residential house in India. "The taxpayer should not own more than one residential house, other than the new one, on the date of sale of the asset," says Ankit Jain, partner, Ved Jain & Associates.

How much can be exempted?

If the cost of the new asset equals or exceeds the net consideration from the asset sold, the entire capital gains is exempt. "However, if the cost of the new asset is less than the net consideration from the sold asset, proportionate exemption is granted," says Kishore Kunal, advocate, the Supreme Court of India.

An amendment effective from April 1, 2024, has set the exemption limit at Rs 10 crore.

Taxation of inherited gold

In India, inheriting gold does not give rise to tax incidence. "When you decide to sell the gold, you might be liable for capital gains tax depending on how long you have held it," says Garg from Triolegal Associates.

Taxation of inherited assets functions similarly to that of acquired assets. "The cost and date of acquisition of the inheritor are considered the same as of the original owner," says Pallav Pradyumn Narang, partner, CNK.

The cost of acquisition for calculating capital gains is the cost to the original purchaser, adjusted for inflation, known as the indexed cost of acquisition. The nature of the gains (short-term or long-term) depends on the period for which the gold was held by the original owner and the inheritor combined.

Availing Section 54F benefit

Taxpayers seeking to save tax from the sale of gold (including inherited) should reinvest the capital gains into residential property to avail of Section 54F benefit.

"Plan the purchase or construction of the new property ahead of the sale to comply with the time limits specified by Section 54F," says Jain.

Some sellers may not be able to reinvest in a residential house within the time limit. “For them, depositing the gains in the Capital Gains Account Scheme (CGAS) before filing the income tax return can offer a temporary solution for claiming the exemption,” says Jain.

Sell the jewellery to large, well-known jewellers. “Inform the jeweller that they should respond promptly to the I-T authorities if there are any questions in the future,” says Ashish Mehta, partner, Khaitan & Co.

Maintain proper documentation. “If you inherit a substantial amount of gold, the tax authorities might request proof of inheritance, such as a will or a partition deed,” says Garg from Triloegal Associates.

How Section 54F benefits taxpayers: A case

* Priya inherited gold from her grandmother in January 2018, which the latter had bought in January 2000 for Rs 10 lakh; Priya sold it in January 2024 for Rs 50 lakh

* To calculate capital gains tax, the original purchase price was indexed for inflation (100 in 2000-01; 350 in 2023-24); the indexed cost came to Rs 35 lakh

* The long-term capital gains was Rs 15 lakh

Priya’s tax liability on long-term capital gains @ 20 per cent was Rs 3 lakh

• If Priya invests the entire net sale consideration (Rs 50 lakh) in purchasing a residential house, she can claim an exemption on the entire LTCG of Rs 15 lakh

• Under Section 54F, her Rs 15 lakh capital gains become non-taxable as she reinvested the sale proceeds in a residential property

• Doing so saves Priya the Rs 3 lakh tax liability

Source: Ved Jain & Associates