Section 54EC Bonds: A Way to Save Tax on Capital Gains

As we all know that selling property in India at a great profit attracts the huge amount of tax burden. This is the common scenario in India but there is a way to save huge chunk of taxes by just simple investment in "Long Term Specified Bonds" or "54EC Bonds". **Section 54EC Bonds (Section 85 as per The Income Tax Act, 2025)** offers the great opportunity for the investors to reinvest their long term capital gains in such specified bonds to enjoy maximum tax exemptions with minimum risk. But it is crucial to understand that the gains from shares, mutual funds or any other securities are ineligible for reinvestment under 54EC Bonds. The gains from selling land and building are only eligible for taking tax exemption under this section.

One of the most secured and government-backed tax-saving options available to taxpayers in India is the **Section 54EC Bond.** These bonds, issued by specified public sector infrastructure institutions, offer individuals and entities a legitimate way to **reduce long-term capital gains tax liability** while ensuring the investment remains secure.

What Is Section 54EC Bond?

Section 54EC of the Income Tax Act, 1961 allows taxpayers to claim exemption from long-term capital gains (LTCG) arising from the sale of land or building or both, provided they have to reinvest such capital gain amount into "long term specified bonds" redeemable after five years and issued on or after the 1st April 2018, within a prescribed time.

These bonds are commonly known as Capital Gains Tax Exemption Bonds or 54EC Bonds. They are regarded as low-risk options because they are issued by highly rated public sector infrastructure companies backed by the Government of India.

Section 54EC is replaced by Section 85 under the The New Income Tax Act, 2025.

Section 85 of The Income Tax Act, 2025 also states that where the investment in such bonds has been taken into account for the purpose of exemption from long-term capital gains (LTCG) arising from the sale of land or building or both, no deduction under section 123 of The Income Tax Act, 2025, for any tax year shall be allowed for such investment.

Eligible Issuing Institutions

- HUDCO (Housing and Urban Development Corporation)
- REC (Rural Electrification Corporation)
- PFC (Power Finance Corporation)
- IRFC (Indian Railway Finance Corporation)
- IREDA (Indian Renewable Energy Dev Agency)

While all four have authorization, their bond issuances may vary depending on the year and government notifications.

Purpose of 54EC Bonds

The primary objective of introducing Section 54EC was to:

- Promote huge investment in India's infrastructure sector
- Provide taxpayers a safe, reliable, and transparent method of saving tax
- Promote the growth of economy due to the advancement of infrastructure sector
- Direct private investment toward long-term development outcomes and infrastructure programs.

By investing in these bonds, taxpayers not only save on capital gains tax but also contribute to the growth of critical national infrastructure.

Key Features of Section 54EC Bonds

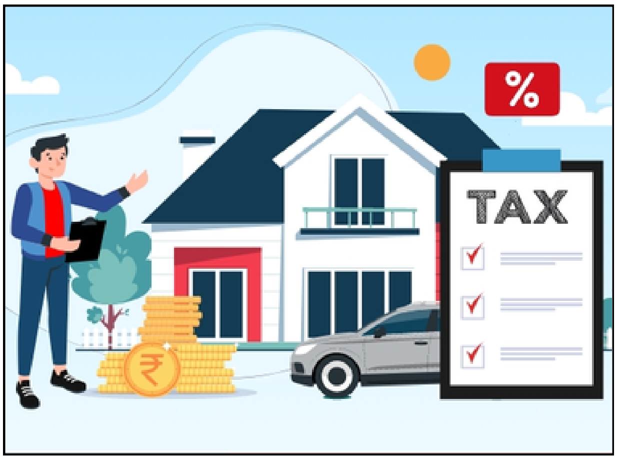
1. Tax Exemption Eligibility

To claim exemption under Section 54EC:

- The capital gain must arise from the **sale of long-term land or building.**
- The investment must be made **within 6 months** from the date of sale of the long term asset.
- The exemption amount equals the investment in the bonds, subject to a limit of **Rs.50 lakhs** per financial year.

2. Lock-in Period

54EC bonds come with a mandatory **5 years lock in period.** During this tenure, the investment cannot be redeemed or transferred.



If the investment made under Section 54EC is withdrawn or transferred before the lock-in period of five years as mentioned above, the capital gain exempted earlier will become taxable in the year of withdrawal, and the assessee will be liable to pay tax accordingly.

3. Interest Rate

These bonds typically offer an annual interest rate ranging from **5% to 5.75%**, depending on the issuer.

The interest is **taxable** and added to the investor's income. (currently it is 5.25%)

4. Minimum and Maximum Investment

- Minimum investment is generally Rs. 10,000.
- Maximum investment allowed for claiming tax exemption is **Rs.50 lakhs** in a financial year.

5. Mode of Holding

These bonds can be held in **dematerialized** or **physical certificate** form, subject to issuer availability.

How Section 54EC Helps Save Taxes

The tax exemption applies only to the **amount of capital gain invested.**

Here's a simple example to understand the whole concept of these bonds:

Mr. X sold a long-term commercial building on 10 January 2025.

After indexation, his long-term capital gain (LTCG) :Rs.80 lakhs.

He also sold shares during FY 2024-25 with a long-term gain of Rs.5 lakhs, but this cannot be claimed under Section 54EC, because 54EC applies only to gains from land or building, not shares or securities.

Mr. X must invest within 6 months from the date of sale of long term asset:

Sale date: 10 January 2025
6-month deadline : 9 July 2025

He must ensure all investments are completed before this date.

How the Rs.50 Lakh Yearly Limit Affects the Investment Plan

Section 54EC permits a **maximum investment of Rs.50 lakhs in a single financial year.**

Let's understand this with the above example of Mr. X:

In Mr. X's case, the 6-month investment window spans **two different financial years,** which creates a potential planning advantage.

- The property was sold in **FY 2024-25** (1 April 2024 to 31 March 2025).
- The 6-month deadline for investing under Section 54EC falls in **FY 2025-26.**

Because the investment window overlaps two financial years, Mr. X is allowed to structure his investment as follows:

- Invest **Rs.50 lakhs in FY 2024-25,** and
- Invest the remaining **Rs.30 lakhs in FY 2025-26,**

provided both investments are completed within the 6-month eligibility period.

This staggered approach is fully permissible under Section 54EC and is often used to maximize exemption benefits.

"Consequence of Delayed 54EC Investment"

If Mr. X fails to invest the first Rs.50 lakhs before 31 March 2025, he loses the advantage of splitting the investment across two financial years. Under Section 54EC, only Rs.50 lakhs can be invested per year, so any amount invested after 1 April 2025 will be counted entirely in FY 2025-26. As a result, although his total capital gain is Rs.80 lakhs, he can claim exemption on only Rs.50 lakhs, and the remaining Rs.30 lakhs will be fully taxable under the Section 112. (Now Section 197)

How to Invest in 54EC Bonds

- **Check Eligibility:** Ensure you are eligible to invest.
- **Choose Issuer:** Select from NHAI, REC, PFC, or IRFC as per your preference.
- **Application Method:** Apply online through the issuer's website/bank platform or you can also submit the application form offline.
- **Submit Required Documents:** Provide KYC documents such as **PAN card, Aadhaar card, address proof, passport-size photo,** and bank details for the verification.
- **Payment:** Make payment via cheque, DD, or online transfer depending on the application mode.
- **Bond Allotment:** Receive the bonds in your **De-mat account** or as a **physical certificate.**

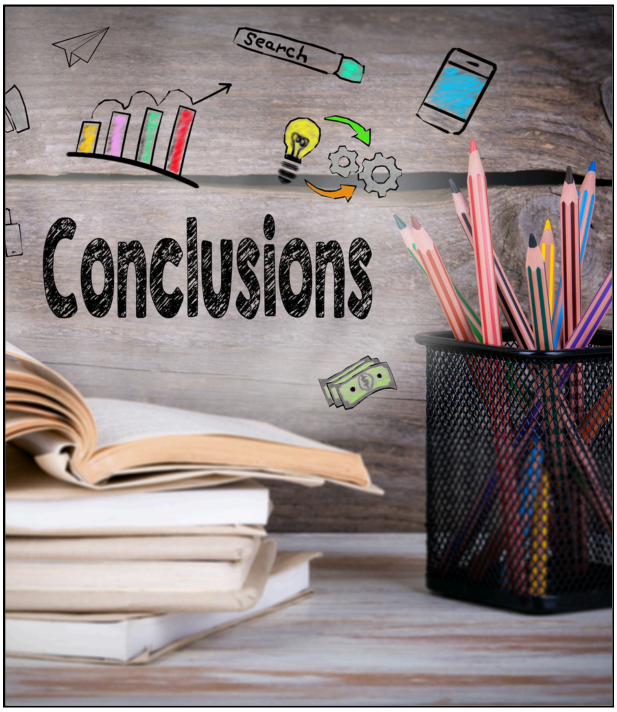
Who Should Invest in 54EC Bonds

- **Individuals with Capital Gains:** Ideal for anyone who has earned long-term capital gains, only from selling property, land, or buildings. (Not from selling shares, mutual funds or other securities.)
- **Investors Seeking Tax Exemption:** Suitable for those wanting to save capital gains tax under Section 54EC by reinvesting within 6 months of the sale of the long term asset.
- **Low-Risk Investors:** Investment in this type of bonds are beneficial for those who wants risk free returns without any headache.
- **People Who Can Hold for 5 Years:** This can be a better option for those who can patiently hold their investment in such bonds for minimum 5 years.
- **Retirees or Senior Citizens:** This is mostly preferred by the retired individual and senior citizen as they seek risk free returns and stable income.

Impact of the New Income Tax Act, 2025 on 54EC (Now Section 85)

As per The Income Tax Act, 1961, Long Term Capital Gains arising from the sale of land or building were taxable under Section 112 at the rate of 20% so the taxpayer could escape from this huge tax liability by investing such gains in 54EC Bonds.

In the Income Tax Act, 2025, Long Term Capital Gains arising from the sale of land or building is now governed under **Section 197** at the reduced rate of **12.5%**. Due to this reduction in LTCG tax rates, the overall tax benefit deriving from investment in 54EC Bonds (Section 85) has reduced. Under the previous Act, taxpayer was avoiding 20% of tax and now the exemption benefit can be claimed with the extent of 12.5% on LTCG as per Income Tax Act, 2025. If we compare both the Act, the benefits from the such investment plan is reduced by 7.5%.



CONCLUSION

Section 54EC Bonds are not just a tax saving bond, they are a smart way to secure your profits from the sales of long term assets i.e. land or building or both. By investing on time and following the annual limits as mentioned above, you can reduce your capital gains tax while showing interest in national infrastructure and joining hands in the advancement of the economy of the India. Escaping deadlines of investing in such bonds can lead to forfeiture of the tax benefits, so strategic planning is very crucial under this section to reinvest the capital gains for the purpose of tax exemption.

CA Sangam Aggarwal

Regional Council Member, NIRC of ICAI
National Vice President
International Navodaya Chamber of Commerce.