Kaplan Herald

Financial & Breaking News

LTCG tax: Larger taxes spark panic amongst international portfolio buyers

February 3, 2018 Kaplan Contributor

The government's decision to reintroduce the long-term capital gains (LTCG) tax has spooked (FPIs), who rushed to the finance ministry on Friday to seek relief. Sources said were concerned about the escalation in the costs for investing in India vis-à-vis other Asian and (EM). Overseas investors were also worried whether the 'grandfathering' relief would be extended to them.

While news about the has been doing the rounds for a while, were hopeful of status quo on the tax benefit on shares held for the longer term. At the most, foreign funds had braced for an increase in the time period from one year to two years or three years for availing of the LTCG exemption.

Most foreign funds are peeved over the reintroduction of the tax without the abolition of the securities transactional tax (STT). In 2004, the STT was introduced as a substitute for the In the Union on Thursday, Finance Minister Arun Jaitley proposed to charge the without any change to the STT regime, making India the only market to levy both.

"The imposition of the is the real negative from the It is wrong to assume that its imposition does not affect investors," said Samir Arora, founder, Helios Capital, adding that India could lose out to other markets as investors would have to temper down their net returns. In the recent past, overseas investors had asked for an increase in the STT instead of imposing the LTCG tax, which creates administrative and compliance difficulties for FPIs, which are pool-investment vehicles like domestic mutual funds.

"The introduction of a tax on LTCG will be a deterrent for foreign investors and could potentially result in a movement of trading activity away from India to other offshore jurisdictions such as Singapore, which offer better tax rates and sophisticated financial products," said Nishith Desai, founder of Nishith Desai Associates.

Experts said another reason for panic among could be whether the 'grandfathering' provision would be applicable to them. Under grandfathering, the mark-to-market gains realised till January 31, 2018, are protected from taxes. Any appreciation in shares after January 31 would be taxed without any indexation benefit. Indexation allows adjustment of cost of acquisition against inflation.

"While the provision relating to does not specifically provide for grandfathering, a reading of the FM's speech indicates that the benefit should be extended to all taxpayers, including all FPIs," said Desai.
Apart from challenges from the taxation perspective, are also concerned about how the end benefit of this tax will be passed on to their investors. are usually pooling vehicles or act as brokerages for their investors. However, current taxation laws treat as a single taxpayer as all their trades are done through a single demat account.

"A tax on LTCG will also throw up a lot of administrative challenges. Apart from the STT and the LTCG tax, also do not receive any indexation benefit while computing the capital gains. Hence, they also have the additional risk of currency fluctuation," said Amit Singhania, partner, Shradul Amarchand Mangaldas. Experts also say the move to impose the could spell an advantage for European countries such as the Netherlands and France as favourable destinations for investing in India compared to Mauritius, Singapore or Cyprus.