

## Tax Hotline

October 11, 2004

### GAINS ON SALE OF SHARES TREATED AS 'BUSINESS INCOME' IN THE HANDS OF FIIS

In a recent tax ruling pronounced by the Authority for Advance Rulings ("AAR") it was held that, gains arising to Foreign Institutional Investors ("FIIs") on sale of their portfolio investments in India were in the nature of business income, and would not be taxable in India in the absence of a permanent establishment ("PE") in India.

The applicant in this case was an investment fund organised in the US and invested in India under the FII route. The ruling was sought from the AAR for the specific determination as to whether gains arising in India from the trading of shares would be regarded as business income or capital gains.

Currently, while long term capital gains on listed securities are tax exempt in India under the domestic law, a 10% tax is levied on short term capital gains on listed securities. In the case of unlisted securities, long term capital gains are subject to tax at the rate of 10%, while short term capital gains are taxed at the rate of 30%.

While pronouncing that the gains were in the nature of business income, the AAR laid down the following principles:

- Mere power in the byelaws to trade in shares is not decisive of the nature of transaction. It must be established that a company dealing in shares is holding the same as stock in trade;
- Substantial nature of transactions, manner of maintaining records and magnitude of transactions are relevant factors in determination of the nature of transactions; and
- Trading in shares with the motive of earning profit would result in the transaction being regarded as adventure in the nature of trade.

The AAR also examined as to whether the applicant had a PE in India due to the presence of a custodian in India. The AAR after perusing the custodian agreement and various other documents held that the custodian was an agent of independent status and hence would not be treated as a PE in India. Thus, relying on the provisions of Article 7 of the India-US tax treaty, they held that in the absence of a PE in India, the trading income of the applicant will be taxable only in the US and cannot be taxable in India.

It should be noted that advance rulings are binding only on the applicant and in respect of the specific transaction in relation to which such advance ruling was sought.

### DISCLAIMER

The contents of this hotline should not be construed as legal opinion. View detailed disclaimer.

This Hotline provides general information existing at the time of preparation. The Hotline is intended as a news update and Nishith Desai Associates neither assumes nor accepts any responsibility for any loss arising to any person acting or refraining from acting as a result of any material contained in this Hotline. It is recommended that professional advice be taken based on the specific facts and circumstances. This Hotline does not substitute the need to refer to the original pronouncements.

This is not a Spam mail. You have received this mail because you have either requested for it or someone must have suggested your name. Since India has no anti-spamming law, we refer to the US directive, which states that a mail cannot be considered Spam if it contains the sender's contact information, which this mail does. In case this mail doesn't concern you, please unsubscribe from mailing list.

## Research Papers

### FAQs on Setting Up of Offices in India

December 13, 2024

### FAQs on Downstream Investment

December 13, 2024

### Gaming Law 2024

December 12, 2024

## Research Articles

### The Revolution Realized: Bitcoin's Triumph

December 05, 2024

### The Bitcoin Effect

November 14, 2024

### Acquirers Beware: Indian Merger Control Regime Revamped!

September 15, 2024

## Audio

### Securities Market Regulator's Continued Quest Against "Unfiltered" Financial Advice

December 18, 2024

### Digital Lending - Part 1 - What's New with NBFC P2Ps

November 19, 2024

### Renewable Roadmap: Budget 2024 and Beyond - Part I

August 26, 2024

## NDA Connect

Connect with us at events, conferences and seminars.

## NDA Hotline

[Click here to view Hotline archives.](#)

## Video

### "Investment return is not enough" Nishith Desai with Nikunj Dalmia (ET Now) at FI18 event in Riyadh

October 31, 2024

### Analysing SEBI's Consultation Paper on Simplification of registration for FPIs

**Scope of judicial interference and inquiry in an application for appointment of arbitrator under the (Indian) Arbitration and Conciliation Act, 1996**

September 22, 2024