MEMO# 30538

January 25, 2017

Industry Coalition Letter on India Indirect Transfer Tax

[30538] January 25, 2017 TO: ICI Members
ICI Global Members
ICI Global Tax Committee
International Committee
Tax Committee SUBJECTS: International/Global
Tax RE: Industry Coalition Letter on India Indirect Transfer Tax

ICI Global coordinated the ten national, regional, and global industry associations[1] that sent senior Indian Government officials the attached letter expressing our serious concerns with their guidance addressing certain indirect transfer provisions of Indian law. This guidance, as explained below, could result in tax being imposed multiple times on a fund investor's allocable share of gains arising from a fund's investments in Indian securities. Likewise, investors could incur Indian tax even when no gain was attributable to Indian investments.

The letter was crafted after India's Central Board of Direct Taxes (CBDT), on December 21, issued CBDT Circular No 41 of 2016 (attached) and then, on January 17, issued a press release (also attached) stating that the Circular will be "temporarily kept in abeyance." The CBDT's December Circular purportedly "clarifies" the application to nonresident investors, including funds, of India's indirect transfer provisions that were enacted in 2012; these rules were enacted with retroactive effect (subject to the applicable statute of limitations) all the way back to 1962.

The indirect transfer rules, as described in the Circular, may apply to investors in any foreign portfolio investor (FPI) that invests more than 50 percent of its assets in Indian securities that have a value in excess of approximately US$1.5 million. Under these rules, the fund investor is treated as having "indirectly" transferred his or her interests in the underlying Indian securities when fund shares are sold, redeemed, or exchanged (including in a tax-free merger).

Although the indirect transfer rules at least nominally are intended to apply only when an investor owning more than 5 percent of the fund's shares transfers some or all of those shares, the Circular has broader effect. Among other scenarios, the indirect transfer tax could apply when a fund redeems shares of an Indian-only-investment subsidiary (that represents less than 50 percent of the upper fund's total assets); when two funds merge; and when a fund's gains are exempt from Indian tax.

The letter raises several concerns with the Circular including:

- The indirect transfer provisions were never intended to apply to foreign investment funds – as evidenced by the Shome Committee report;[2]
- Economic double or even multiple levels of taxation of income will occur;
- Practical calculation considerations will arise in calculating any individual investor’s indirect transfer tax;
- Clarification is needed that nominees are not 5 percent investors;
- Non-Indian funds will face substantial Indian tax compliance issues; and
- Investors may not receive tax credits in their home jurisdictions for any Indian tax on indirect transfers.

To resolve these concerns, the letter urges that permanent relief – with both prospective and retroactive effect – be provided through either amendments to the 2012 Indian law or a new CBDT Circular.

Keith Lawson
Deputy General Counsel - Tax Law

Attachment No. 1

Attachment No. 2

Attachment No. 3

endnotes

[1] The other nine associations are: Association Française de la Gestion financière (AFG); Association of the Luxembourg Fund Industry (ALFI); Assogestioni; *BVI Bundesverband Investment und Asset Management e.V. (BVI)*; European Fund and Asset Management Association (EFAMA); Financial Services Council (FSC); Investment Funds Institute of Canada (IFIC); The Investment Association; and Irish Funds.

[2] ICI Global met with Dr. Shome and supported strongly the recommendations of the Shome Committee. *See, e.g.*, https://www.iciglobal.org/pdf/28221.pdf; https://www.ici.org/pdf/27651.pdf (Serial No. 10).
