Taxation of Capital Gains and benefits for Non residents / Foreign Co.s

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* *Offshore Indirect Transfer – To be covered on 25 June 2021*

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Taxability under the Act

Taxability of Capital Gains

Deemed to accrue / arise in India - Sec. 9(1)(1):

- All income accruing / arising, whether directly or indirectly, through **transfer** of a **capital asset** situate in India

Charging provisions for CGs

- Sec. 45(1), and other charging provisions under the head 'Capital Gains'. Eg. sec. 46(2)

Computation of CG

- Computation mechanism

Particulars	Amount
Full Value of Consideration	xxx
Less:	
Cost of **acquisition** and **improvement** of the asset	xxx
Expenditure incurred in connection with transfer	xxx
= Capital Gain / Loss	xxx

- 1st proviso to sec. 48: Forex rate adjustment
- 2nd proviso to sec. 48: Indexation

First proviso to sec. 48

- CG from **shares** or **debenture** of I.Co. (Listed / unlisted):
  - Step 1: Conversion of consideration, COA and expenditure into original foreign currency
  - Step 2: CG to be re-converted to INR
- Also applies to **re-investment**
- Not applicable to all securities. Eg. MF units

CGT rate under ITA

Nature of Income	Rate	Remarks
LTCG from **unlisted** securities	10%	1st, 2nd proviso, not available
LTCG from all other assets	20%	With indexation
LTCG from **Listed securities** (except units / ZCBs)	20%	But such tax should **not exceed** 10% of CG, without indexation
STCG from equity sh. or units of EOF / business trust, chargeable to STT	15%	

TDS from Capital Gains

- Sec. 195: **Rate of TDS**
  - **10%:** LTCG on unlisted securities, and eq. share / EOF units that have been subjected to STT
  - **20%**: Other LTCG
  - **15%**: STCG on equity share / EOF unit that have been subjected to STT
- **Monetary threshold:** None
- Exemption for indiv. (non 44AB) deductor: None

TDS from Capital Gains

- Should TDS rate be applied **only to the element of gain**, or to **gross consideration**
  - **CBDT circular, Hon'ble SC:** TDS only from income
  - Practical experience, say, when applying for a certificate under sec. 197

Not to be overlooked

- Even when opting for DTAA provisions, any **deeming** provisions in CGT's computation mechanism under the Act will continue to apply. Eg.
  - Sec. 50CA: **FMV** > sale price of **unquoted shares**, deemed to be their Full Value of Consideraion
  - Sec. 50C: **Stamp duty** value of land / building
  - Cost of acquisition deemed to be NIL for certain specific assets, under sec. 55

Capital Gains - Taxability under DTAAs

Immovable property

- Art 13(1) of UN Model:

  *Gains derived by a resident of a Contracting State from the alienation of **immovable property** referred to in Article 6 and **situated in the other Contracting State** may be taxed in **that other State**.*

Immovable property

- Art 13(4) of UN Model

  Gains from ***alienation of shares*** *of capital stock* ***of a company****, or of an interest in a partnership / trust / estate,* <u>*property of which consists directly / indirectly*</u> ***principally*** <u>*of*</u> ***immovable property situated in a CS*** *may be taxed in that State. In particular:*

  (a) Nothing in this para shall apply to a company, etc. ***engaged in the business of management of immovable properties,*** *the property of which consists directly / indirectly principally of* ***immovable property used by such company****, etc.* ***in its business activities****.*

Immovable property

- Art 13(4) of UN Model

  *(b) "**Principally**" in relation to ownership of immovable means value of such immovable **exceeding 50%** of aggregate value of all assets owned by the company, etc.*

Property of PE

- Art. 13(2): Property of PE

  *Gains from **alienation of movable property** forming part of **business property of a PE *** which an enterprise of a CS has in the other CS, may be taxed in that other State.*

  ** Including gains from alienation of the PE itself (alone / with whole enterprise)*

Ships and aircrafts

› Art 13(3): Ships and aircrafts

*Gains that an **enterprise of a CS** that operates ships / aircraft in **international traffic** derives from the alienation of:*

- Such ships / aircraft, or
- Movable property pertaining to operation of such ships / aircraft)

*shall be **taxable <u>only</u> in that CS.***

Transfer by a substantial shareholder

- Art 13(5): Shares

  Gains, other than those to which para 4 applies, derived by a resident of a CS ***from alienation of shares*** *of a company which is a* ***resident of the other CS, may be taxed in that other State <u>if the alienator</u>****, at any time during the 12-month period preceding such alienation,* ***<u>held</u>*** *directly or indirectly* ***at least XX% * of the capital of that company****.*

  ** to be established through bilateral negotiations*

Transfer by a substantial shareholder

- Art 13(5):
  - Transferor (Resident of State R) held at least 10% (say) shares in Investee Company (Resident in State S) at any time during the last 12-mth before sale of its shares
  - CG on sale of any part of such shares: Taxable in State S
  - **Effective outcome:** CGT on sale of shares, allowed to be taxed by Source State (with minority protection)
- No such clause in OECD MC

Residual Clause

- Art 13(6) of UN Model: **Residual Clause**

  *"Gains from alienation of **any property other than** that referred to in para 1, 2, 3, 4 and 5 shall be taxable **ONLY** in the State of which **alienator is a resident**"*

- Art 13(5) of OECD MC is identical to above

Residual Clause

- Securities, say **bonds, debentures** and **units**
  - Ardex Investments Mauritius Ltd (AAR)
- Index futures, Index **options**, **stock options**
  - Credit Suisse First Boston Cyprus Ltd. (Bom)
  - Morgan Stanley & Co. International (AAR)
- Other financials instruments
- **Intangibles**: Trademarks and technology

Article 13 - Summary

	Property	State where taxable
13(1)	Immovable Property **situated in other CS**	Where property is situated
13(2)	Movable Property attributable to PE situated in State S	Where PE is situated
13(3)	Ships and aircrafts	Where POEM of the enterprise is located
13(4)	Shares in a company, of which **> 50%** assets consist of immovable situated in State S	Where property is situated
13(5)	Share in a company - except Art. 13(4)	Resident state of company
13(6)	Other asset	Resident state

Illustrative clauses of certain DTAAs

- India - UK / US Treaty
  - CS may tax capital gains **in accordance with the provisions of its domestic law**

CGs on transfer of shares in Indian Co by a US Co. to another US Co. ***are taxable in India*** *– Trinity Corp. (AAR)*

Illustrative clauses of certain DTAAs

- India-Netherlands DTAA

  …gains from alienation of shares issued by a Co. resident in other State which shares form part of at least a 10% interest in capital stock of that Co., may be taxed in <u>that other State</u> ***IF alienation takes place <u>to a resident of that other State.</u>***

  However, such gains shall remain taxable only in the CS of which alienator is a resident if they're realised in the course of a ***corporate reorganisation****, amalgamation, or similar transaction,* ***<u>and</u> buyer / seller owns at least 10% of capital of the other.***

Illustrative clauses of certain DTAAs

- India-Sweden DTAA
  - 13(5): CG on sale of shares taxable only in State R, **“provided that such resident is subject to tax thereon in that State”**
  - 13(6): CG on sale of property derived by individual, being resident of CS **and who becomes resident of other CS**, is taxed in first CS if alienation is made within **4 years from ceasing as resident of first CS**

Certain unique cases

- Taxability of CGT when:
  - DTAA doesn’t contain any CGT clause
    - Residuary clause (Other income)
  - DTAA has **no clause on CGT and Other Income**
    - India-Libya DTAA
    - Taxable in both countries as per DTL

India-Mauritius DTAA

- Pre-amendment
  - Art 13(4): CG on sale of shares taxable only in Resident State
  - **Condition:** Mauritius resident to present TRC issued by Mauritian Govt.

India-Mauritius DTAA

- Protocol to India-Mauritius DTAA
  - **Grandfathering** of investments prior to 1 April 17
  - **Source-based taxation** of capital gains, on alienation of shares **acquired on / after 1 April 2017**
  - For gain during Apr’17 - Mar’19, tax rate to be limited to **50% of rate in ITA** (subject to new LOB)
  - NRs not entitled to 50% reduction above, in case **LOB conditions** are not met

India-Mauritius DTAA

- Protocol to India-Mauritius DTAA
  - **LOB:** No Treaty benefits to resident with **negligible or nil business operations** / no real and continuous business activities carried out in that State
  - Resident not to be deemed as a **shell / conduit** if:
    - Listed on a recognized stock exchange
    - Exp. on operations in that State is >= INR 2.7 Mn

India-Singapore DTAA

- Protocol to India-Singapore DTAA
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  - **LOB:** No Treaty benefits to resident with **negligible or nil business operations** / no real and continuous business activities carried out in that State
  - Resident not to be deemed as a **shell / conduit** if:
    - Listed on a recognized stock exchange
    - Exp. on operations in that State is >= SGD 2 lakhs / INR 50 lakhs

CGT - Special provisions under the Act

Sec. 115AB: Income of Offshore Funds

- Applicable to **Offshore Funds.**
  Eg. SBI Resurgent India Opportunities Fund
- LTCG on sale of **MF units purchased in foreign currency** (or income from such units)
- **Tax rate**: 10% without indexation
- **No deduction** for expenses, or under Ch. VI-A

Sec. 115AB: Income of Offshore Funds

- Benefits:
  - **Applicability of first proviso to sec. 48** which is otherwise not available to NR paying tax at 10%
  - Listed units are also **taxed at 10%** as against 20% tax rate under sec. 112

Sec. 115AD: Income of FIIs

Tax rate for **FII's income**:

- 20%: Income of FIIs from securities (other than MF units)
- 15%: STCG on equity shares / units subjected to STT
- 30%: STCG (other than above)

** Applies to income from transaction in derivative – Platinum Investment Management Ltd. v. DDIT*

Sec. 115AD: Income of FIIs

- 10%: LTCG

  (This rate shall apply only to income > INR 1 Lac, w.r.t. gains on sale of equity shares/ units chargeable to STT)

Special provisions for NRIs

Sec. 115E: Special rate on income from **foreign exchange assets** of an NRI

- Investment income: 20%
- LTCG (other than specified asset): 20%
- LTCG (specified asset): 10%
- **Benefit**: Availability of **1st proviso** to sec. 48 (otherwise not available to NR taxed @10%)

Special provisions for NRIs

- **Foreign exchange assets**: Following assets purchased in forex
  - **Shares** in Indian Company
  - **Debentures** issued by an Indian Co. (except Private Co.)
  - **Deposits** with an Indian Co. (except Private Co.) - **also includes banks**
  - Security of CG
- STCG shall not be considered as investment income - CIT v. Sham L. Chellaram (Bom.)

Sec. 115F: Exemption from LTCG

- Exemption of LTCG from transfer of foreign exchange asset, upon re-investment **of net proceed** within 6 months, in:
  - Specified assets, or
  - Saving certificates
- **Amount of exemption**: $\text{LTCG} \times \dfrac{\text{Amount invested}}{\text{Net consideration}}$
- Lock-in period: 3 year from re-investment

Exemptions under sec. 47

Sec. 47(via), 47(viab) – Foreign Amalgamation

- Transfer of asset (share of I.Co. / F.Co. deriving its value from an I.Co.) **by a F.Co. to another F.Co.** in an amalgamation
- Condition :
  - 25% shareholders of Amalgamating F.Co. remains shareholder of Amalgamated F.Co.; and
  - No CG tax in the country of Amalgamating F.Co.

Exemptions under sec. 47

Sec. 47(vic) and 47(vicc) – Foreign Demerger

- Transfer of asset (share of I.Co. / F.Co. deriving its value from an I.Co.) **by a F.Co. to another F.Co.** in a demerger
- Conditions:
  - Shareholder holding ¾ value of share of Demerged F.Co. remains shareholder of Resulting F.Co.; and
  - No CG tax in the country of Demerged F.Co.

Exemptions under sec. 47

Following transactions of transfer by a NR to another NR outside India:

- 47(viia): Transfer of **GDR**
- 47(viiaa): Transfer of **RDBs** of an Indian Co.

Exemptions under sec. 47

- Sec. 47(viiab): Transfer of **GDR, RDB, derivative by a NR**
  - On a recognized stock exchange located at **IFSC**
  - Where the consideration is payable in **foreign currency**

Exemption on reinvestment

Sec.	Exemption to	Sale of	Purchase of	Time period for purchase	Exemption Amount	Additional conditions
54	Individual or HUF	Residential house (Long term capital asset)	One new residential house in India If CG amount is less than INR 2 Crore: 2 residential house (option can be exercised only once)	If purchased: 1 year before or 2 year after If constructed: within 3 years	Lower of amount invested or LTCG	New asset should not be sold within next 3 years
54F	Individual or HUF	Any LTCA except residential house	One new residential house in India	If purchased: 1 year before or 2 year after If constructed: within 3 years	Cost of new asset x CG / Net consideratio n (maximum up to capital gain	New asset should not be sold within next 3 years Individual cannot hold more than 2 house properties

Exemption on reinvestment

Sec.	Exemption to	Sale of	Purchase of	Time period for purchase	Exemption Amount	Additional conditions
54EC	Any person	Land or Building (LTCA)	Bonds issued by NHAI and REC, redeemable after 5 years	Within 6 months	Cost of new asset x CG / Net consideration (maximum up to capital gain	New asset should not be sold within next 5 years Investment should not exceed INR 50 Lakhs

› An NR can also avail benefit under Sec. 54B, 54D, 54G and 54GA

Benefits under sec. 10 to NRs / F.Co.

Sec. 10(4E)

- Income of NR from **transfer of non-deliverable forward contracts**, entered into with an **offshore banking IFSC** unit which commenced its operations by 31 March 2024

Interest incomes of NR

- Sec. 10(4)(ii): In case of a PROI under FEMA, interest on **NRE Account** in any bank in India

- Sec. 10(4C): Interest on **RDBs** (Masala bonds) issued outside India by I.Co., between 17 Sept. 2018 and 31 Mar. 2019

Interest income of NRs

- Sec. 10(15)(iv)(fa): Interest paid by schedule bank to NR or RNOR on **foreign currency deposits,** acceptance of which is approved
- Sec. 10(15)(viii): Interest paid to NR or RNOR on deposit made in an **Offshore Banking Unit** on or after 1 April 2005
- Sec. 10(15)(ix): Interest paid by a unit located in **IFSC** for **money borrowed** by it on or after 1 Sept. 2019

Sec. 10(6)(vi) - Short stay exemption

- Remuneration received by a person (not a citizen of India) for **service rendered in India** shall be exempt upon satisfaction of following **conditions**:
  - **Presence** in India < 90 days in relevant year;
  - Foreign enterprise is **not engaged in any trade or business in India**; and
  - Such **remuneration is not deductible** from income of foreign enterprise in India.

Sec. 10(50)

- *Any income arising from any **specified service** provided on / after the date on which provisions of Ch. VIII of FA2016 comes into force or arising from any **e-commerce supply or services** made / provided / facilitated on or after 1 April 2020 **and chargeable to EQL** under that Chapter.*

  ***Expl. 1:** For the removal of doubts it is hereby clarified that income referred to in this clause shall not include and shall be deemed never to have been included any income which is chargeable to tax as **royalty** or **fees for technical services** in India under this Act read with a DTAA.*

Questions?

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- Gaurav has an experience of 19+ yrs, specializing in Corporate and International Taxation. He has worked for more than 10 years, with organizations such as BMR Associates, KPMG and Ernst & Young.
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Annexure: Residential status (FEMA)

Residential status under FEMA

- The FEMA also uses certain expressions which are similar to that of NR, such as:
  - Person Resident Outside India (PROI)
  - Non-resident Indian (NRI)

Residential status under FEMA

- PRI: Person residing **in** India for more than 182 days in the preceding FY, but excludes person:
  - Leaving / staying outside India for business / employment; and
  - Person coming to / staying in India for purpose other than business / employment.
- **PROI**: Person who is not a PRI

Residential status under FEMA

- **NRI:** PROI who is a citizen of India OR a PIO
- **PIO:** Citizen of any country other than Bangladesh and Pakistan –
  - Who held an Indian Passport, at any time;
  - Who / his parents / grand-parents, was / were a citizen of India (under the Constitution of India or under the Indian Citizenship Act, 1955); or
  - Who is spouse of an Indian citizen / spouse of person referred above