Changes to Capital Gains Tax rates for foreign investment in India

The Central Board of Direct Taxes in India has issued a circular announcing an amendment to the India/Mauritius Double Taxation Treaty (DTT). Currently a significant number of both Foreign Direct and Foreign Portfolio investments have been routed through jurisdictions with whom India has signed a double taxation treaty (such as Mauritius and Singapore).

Current situation

- The current India/Mauritius DTT provides for residence-based taxation on investments in India ie. for a Mauritian resident fund investing in India, the Mauritian CGT of 0% applies

Announced details

- The amended DTT provides for source-based taxation on investments in India ie. the Indian CGT rates apply to overseas investments in India
- In India, short term CGT, defined as less than one year, is applied at a rate of 15% and long term CGT, defined as greater than one year, is 0%
- From 1 April 2017 to 31 March 2019, investments in India will be liable to pay short term CGT at 50% of the current 15% rate, (i.e. 7.5%), providing the Mauritian resident investing structure is not deemed to be a “shell/conduit” company. The latter is defined as having total expenditure on operations in Mauritius less than MUR1.5m (US$40,000 approx.)
- From 1 April 2019 – investments in India will be liable to short term CGT at the full rate, currently 15%

Potential impact to the market

The Government has acted responsibly in its efforts to align CGT rates for domestic and foreign investors by providing both an 11 month preparatory period and a two year transitional phase. Most importantly there is full transparency on zero retrospective taxation prior to April 2017 for both portfolio and direct investors.

- The amendments will equally apply to investments routed via Singapore, and we are not aware of any other credible jurisdictions where a similar DTT with India exists that could be used as an alternative
- These changes are not expected to affect long term investment into India, either portfolio or direct

Potential impact to Ocean Dial “Long Only” investors

- The long term nature of Ocean Dial’s investment process and the relatively low level of portfolio turnover ensures that the impact on the investment process will be minimal
- The current portfolio will not be affected, and there is a further period to April 2017 where adjustments if required, can be made
- Ocean Dial Mauritian investment structures will not be defined as shell/conduit companies, however
    - The NAV will incorporate a CGT liability where applicable
    - We understand that short term capital losses can be used to offset short term gains, which will mitigate the potential liability
    - The increase short term CGT may affect fund returns at the margin
    - And an element of tax management will be incorporated into the investment process to minimise any potential CGT liability

The immediate reaction to the announcement has overall been positive. This issue has loomed over current market participants for some time with genuine fears that any tax amendments could be enforced retrospectively. That this has not transpired draws a line under the matter. Not only is there greater clarity on future treatment of investments, but also tax compliance in India has made further step towards being simpler and more transparent.

The information in this document is provided for information purposes only and is based on information from third party sources which has not been independently verified. While all reasonable care has been taken in the preparation of this document, no warranty is given on the accuracy of the information contained herein, nor is any responsibility or liability accepted for any errors of fact or any opinions expressed herein. It does not constitute any offer, recommendation or solicitation to any person to enter into any investment transaction, nor does it constitute any prediction or likely movements in rates or prices. The material in this document should not be relied upon to be sufficient to support an investment decision. Past performance is not a guide to the future and the value of investments and income from them can go down as well as up. Exchange rate changes may cause the value of the underlying overseas investments to go down as well as up. Investment in emerging markets may involve a higher degree of risk. Investment in smaller companies may also involve a higher degree of risk as small cap markets tend to be more volatile than their larger capitalisation counterparts. This document is issued by Ocean Dial Asset Management Limited and views expressed in this document reflect the views of Ocean Dial Asset Management Limited and its Mumbai based affiliated company and advisor, Ocean Dial Advisers Private Limited as at the date of publication. Comments on individual sectors and companies also reflect those views as at that date. Subsequent events may cause such views to change. It may contain forward-looking statements, which can be identified by words like “anticipate,” “intend,” “believe,” “plan,” “hope,” “goal,” “initiative,” “expect,” “future,” “intend,” “will,” “could” and “should” and by similar expressions, in reliance upon certain “safe harbour” provisions of applicable securities laws. Other information herein, including any estimated, targeted or assumed information, may also be deemed to be, or to contain, forward-looking statements. Prospective investors should not place undue reliance on forward-looking statements as this information is subject to various risks and uncertainties. Forward-looking statements are necessarily speculative in nature, and it can be expected that some or all of the assumptions underlying any forward-looking statements will not materialize or will vary significantly from actual results for many reasons. Variations of assumptions and results may be material. This information is for the use of intended professional and institutional investor recipients only and may not be reproduced, redistributed or copied in whole or in part without the express consent of Ocean Dial Asset Management Limited. Ocean Dial Asset Management Limited is authorised and regulated by the Financial Conduct Authority in the United Kingdom. Registered office 13-14 Buckingham Street, London WC2N 6DF.