Capital gains: For FPIs, new SEBI norm is a tax-free 'gift'

SEBI has allowed foreign portfolio investors (FPIs) to invest from Gujarat Gift city, in a move that could see FPIs heading to the international financial services centre (IFSC) in Gandhinagar.

Business units operating from GIFT City enjoy a 10-year tax holiday. The measure comes as a cushion for foreign investors, who were troubled by Finance Minister Nirmala Sitharaman's tax proposals in her maiden Budget.

Under SEBI's new rules, FPIs trading in India's stock market will face 'zero' tax and transaction charges if they register with the IFSC.

"Entities established in IFSC will be deemed to have met the jurisdiction criteria for FPIs," SEBI said in a press release issued on Wednesday after its board meeting in Mumbai.

GIFT City has no income-tax, LTCG, STCG, dividend distribution or minimum alternate tax. Those FPIs now trading on the BSE and the NSE will only have to pay securities transaction tax (STT). Another way to avoid paying STT is to trade on the BSE and NSE exchanges established in GIFT City, where the transaction tax is not applicable.

FPIs can trade derivative contracts in GIFT City and buy shares on the NSE and BSE in Mumbai. It will be similar to trading Nifty futures on the Singapore Stock Exchange and cash market in India, experts said. However, the Prevention of Money Laundering Act, which is India's law to check round-tripping of money, will be applicable on FPIs in GIFT City, too.

KYC norms relaxed

SEBI has also relaxed other registration and KYC norms for FPIs, which is the icing on the cake, experts say. Even participatory notes, favoured instruments by large investors, can be issued by top FPIs from Gift city.

Sitharaman had hiked the effective rate of peak LTCG and STCG (long term and short capital gains) tax to 14.25 per cent and 21.37 per cent, respectively. The earlier rates were 11.96 per cent and 17.94 per cent, respectively. For decades, FPIs invested in India via tax havens such as Singapore and Mauritius, which had double taxation avoidance treaties with India and enjoyed capital gains from Indian markets without any tax.

In 2014, after the Modi government took charge, the avoidance treaties were re-worked and even LTCG and STCG was imposed on FPIs. This was in addition to STT and a 30 per cent business profit tax in the derivatives segment.

The FPI mood soured when Sitharaman hiked the tax on these entities in July and they resorted to relentless selling in stock markets, contributing to a more-than-10 per cent fall in benchmark indices and a brutal crash in small and mid-cap stocks.

"SEBI's move to allow FPIs coming from IFSC... could see FPIs flocking to Gujarat," said a senior tax consultant.

(The Hindu Business Line)