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GES Alert
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No capital gains tax at the time of roll over of mutual fund under Fixed Maturity Plans

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Background

- As per the provisions of the Income-tax Act ,1961 (“the Act”), prior to amendment made by Finance (No.2) Act, 2014, capital assets in the nature of shares, listed securites, units of a mutual fund and zero coupon bonds, held for a period of more than 12 months qualified as long term capital assets.
- After amendment in sub-section (42A) of Section 2 of the Act by the Finance (No. 2) Act, 2014, for qualification as long term capital assets, the period of holding for shares not listed on a recognised stock exchange in India and units of mutual funds (other than equity oriented fund) was changed from 12 months to 36 months if these were sold/ redeemed after July 10 ,2014.
- Accordingly, units of Fixed Maturity Plans (FMPs) held for 36 months or less qualify as short term capital assets. (FMPs are closed ended funds having a fixed maturity date wherein the duration of investment is predetermined.)
- To enable the FMPs to qualify as long term capital assets, some Asset Management Companies administering mutual funds have offered extension of the duration of FMPs to a date beyond 36 months from the original investment date by providing investors an option of roll-over of FMPs in accordance with provisions of Regulations 33(4) of the SEBI (Mutual Funds) Regulations, 1996.

Issue

Whether roll over / extension of FMPs would be considered as transfer under the Act and if so whether the same would be liable to tax as capital gains in the hands of the unit holders?

Clarification

- SEBI allows the roll over of FMPs in case the following conditions are satisfied:
  - The purpose, period and other terms of the roll over and all the material details of the scheme, including the likely composition of assets immediately before the roll over, the net assets and net asset value of the scheme, are disclosed to the unit holder and a copy of the same is filed with the SEBI.
  - Written consent for roll over is provided by the unit holders and in case they do not opt for roll over or do not provide written consent, such unit holders should be allowed to redeem their holdings in full at net asset value based price.
- SEBI has further clarified that in case of roll over in accordance with the aforesaid regulation, there is no change in the scheme and it essentially remains the same.
- Based on the above, the CBDT has clarified that roll over in FMPs in accordance with the aforesaid regulations will not amount to transfer and no capital gains will arise at the time of exercise of the option by the investor to continue in the same scheme (i.e. as per the SEBI regulations). The capital gains will, however, arise at the time of redemption of the units or opting out of the scheme, as the case may be.

Comments

This clarification provides certainty on tax treatment to the unit holders of FMPs who opt for roll over of their investment. If the total period of holding exceeds 36 months, then such units would qualify as long term capital asset leading to beneficial tax treatment.

Source: CBDT circular No. 6 of 2015 dated April 9, 2015

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