



Global Business Tax Alert Sharp Insights

Applicability of MAT on
FIIs – Recent
controversy & way
forward

Issue no: GBTA/11/2015

In this issue:

- Synopsis
- Background
- In case MAT applies to FIIs
- Current position adopted by FIIs and recent budget amendment
- Recent controversy
- Next steps and how Deloitte can assist
- Comments
- Do you know about Dbriefs?
- Contacts

Synopsis

In the recently concluded audit proceedings of FII's for assessment year 2012-13, the Indian tax authorities have applied the provisions of Minimum Alternate Tax ('MAT') under Section 115JB of the Indian Income-tax Act, 1961 ('Act') to FII's and demanded tax at approximately 20% on total gains (including long term capital gains which are otherwise exempt from tax). This comes in the backdrop of the Finance Minister specifically proposing to exclude certain incomes of FII's from the purview of MAT vide Finance Bill 2015. The position adopted by the Indian tax authorities and the proposed amendment gives rise to various questions with respect to the taxability of an FII.

Background

What is MAT?

- In the past, there were various instances of companies which earned 'book profits' and also paid dividends but did not pay any income-tax owing to various tax incentives and allowances available under the Indian Income-tax Act, 1961 ('Act') – Such companies were referred to as ZERO TAX COMPANIES
- Provisions relating to taxation of 'book profits' [Minimum Alternate Tax ('MAT')] were introduced in the domestic tax law to bring such Zero tax companies within the tax net
- Current applicable rate of MAT is 18.5 percent (plus applicable surcharge and education cess)
- These provisions are separate and independent charging provisions and over-ride other provisions of the domestic tax law

When does MAT apply?

- MAT provisions are applicable to Companies in case where the tax payable on the total income of a company as computed under other provisions of the Act is less than 18.5 percent of the book profits

How is MAT computed?

- MAT is computed on 'book profits'. Book profits are to be computed by considering the net profit as shown in the profit and loss account prepared in accordance with the Indian Companies Act subject to certain specified additions/ reductions - Company is required to maintain books of accounts as per the Indian Companies Act

To whom does MAT apply?

- MAT provisions are applicable to "Companies". Indian Income-tax Act defines a company to inter alia include anybody corporate incorporated by or under the laws of a Country outside India. Thus, technically, a foreign company qualifies as a 'Company' under the Indian Income-tax Act
- Trusts, partnerships and other non-corporate entities will be outside the purview of MAT

Does MAT apply to a Foreign Company? – On-going controversy

- This matter has been a subject matter of debate and litigation (refer illustrative table below). There are contradictory judicial precedents on this issue and matter is pending before various Courts including the Supreme Court (Apex Court)

Name of the case	Authority passing the order/ decision	Conclusion
The Timken Company	Authority for Advance Ruling	MAT not applicable to foreign company who do not have a permanent establishment in India
Castleton Investment Limited	Authority for Advance Ruling	MAT applicable to foreign company
Praxair Pacific	Authority for Advance Ruling	MAT is not applicable to foreign company
Bank of Tokyo Mitsubishi UFJ Ltd	Delhi Tribunal	MAT is not applicable to foreign company

- It is arguable that the intent of introduction of MAT provisions was to tax Companies which had book profits but were not paying tax owing to tax deductions/ incentives. Support can inter alia be drawn from other Budget documents relating to introduction and implementation of MAT provisions – No intent to apply MAT provisions to Foreign Companies

- Foreign Companies, computing income under a tax treaty, may have a better case to argue that provisions of MAT are not applicable to it, depending on the terms of the treaty.

In case MAT applies to FIIs

Tax implications under MAT will arise where the tax on total income as computed under other provisions of the Act is less than 18.5% of book profits

Types of Income	Rate under normal provisions on income computed as per the regular provisions of the Income-tax Act	MAT upto 31 March 2015 on “book profits” computed as per the Companies Act	MAT from 1 April 2015 on “book profits” computed as per the Companies Act
Long term capital gains (STT paid)	Exempt	18.5%	Exempt
Long term capital gains (no STT paid)	10%	18.5%	Exempt
Short term capital gains (STT paid)	15%	18.5%	Exempt
Short term capital gains (no STT paid)	30%	18.5%	18.5%
Interest on Government bonds and certain corporate bonds	5%	18.5%	18.5%
Interest from securities (excluding above)	20%	18.5%	18.5%

Rates exclusive of surcharge and education cess

Current position adopted by FIIs and proposed Budget amendment

- Currently, FIIs are taking a position that MAT provisions are not applicable to FIIs:
 - MAT provisions should not apply to foreign companies
 - FIIs do not have a place of business in India and are not required to maintain books of accounts under the Indian Companies Act
- Indian tax authorities, in the past, have also not applied MAT provisions to Foreign Companies/ FIIs. However in December 2014, during the course of on-going audit proceedings for assessment year ('AY') 2012-13 [Financial Year 2011-12: 1 April 2011 to 31 March 2012], Indian tax authorities issued notices to various FIIs seeking explanation as to why MAT provisions should not apply
- representations were made to the Central Board of Direct Taxes (Tax administration body) to issue clarifications on this issue
- Acceding to the request of various stakeholders, the Finance Minister proposed to amend the MAT provisions vide the Finance Bill 2015 which was tabled in the Parliament on 28 February 2015

Proposed amendment – Budget 2015

- MAT will not apply to the following income of FII
 - long term capital gains which are exempt from Indian income-tax;
 - short term capital gains which are taxed at 15% on equity sales on stock exchanges
- The corresponding expenditure in relation to earning such income will also not be allowed
- This amendment is proposed to be effective from 1 April 2015

Position adopted by Indian tax authorities

- The tax officers have interpreted that the proposed amendment applies only from 1 April 2015 onwards and therefore MAT should be applied for previous years
 - Intention of the legislature was that MAT provisions apply to all companies including foreign companies and FIIs. This is clear from the amendment made in the Budget 2015-16 which exempts specified capital gains earned by FIIs while computing book profits

- Accordingly, tax officers have demanded MAT from FII's formed as corporates in the recently concluded audit proceedings for AY 2012-13 (financial year 2011-12)
- Tax officers have also issued notices to re-open the cases for previous years to apply MAT for those years
 - The statute of limitations for re-opening of cases allows tax officers to go back upto 7 years to open the assessments (audits) – Re-opening now possible for financial year 2008-09 onwards i.e. for income from 1 April 2008
- FII's are in the process of filing appeals to Appellate authorities against the orders passed by the Indian tax authorities applying MAT provisions

Recent Controversy

MOOT CONTROVERSY

Applicability of MAT to foreign companies – Still unanswered

- While the proposed amendment is well intended, it does not provide an answer to the moot question of whether MAT provisions are applicable to foreign companies
- The Finance Minister, in a recent news conference, mentioned that the issue of applicability of MAT provisions in earlier years will be settled by the Courts (effectively stating that no formal clarification will be issued on this controversy)

Proposed amendment poses more questions than answers

- Are FII's now required to maintain books of accounts as per the Indian Companies Act for the purposes of determining book profits?
- Since, MAT provisions are based on 'book profits' i.e. profits as per books of accounts to be drawn up in accordance with the Indian Companies Act;
 - Can FII's make a claim for deduction of expenses incurred e.g. fund manager fees?
 - In case where an FII records unrealized gains in their books of accounts, will such unrealized gains be subject to MAT?
- Under the Act, there is specific mechanism provided for set-off of losses e.g. short term capital gains cannot be set-off against long-term capital loss. However, there is no such provision under MAT. Thus, should all losses be adjusted to arrive at the book profits?

- Can past years losses be set-off against the book profits?
- Can MAT provisions apply in case an FII chooses to be taxed under a tax treaty?

Next steps and how Deloitte can assist

Next steps

- Filing of appeal before appellate authorities challenging the application of MAT provisions in the assessment order for AY 2012-13
- Formally filing returns and seeking reasons for re-opening of completed audits for earlier years
- Preparedness going forward considering the impact of the Budget proposal
- Analysis from the perspective of tax provisioning (similar to US FIN 48)

How Deloitte can help – Tax controversy management and risk mitigation

Orders received and MAT provisions applied	Re-opening in earlier years (notice issued or potential to be issued)	Preparedness going forward
<ul style="list-style-type: none"> • Assistance in preparation and filing of appeals to Appellate authorities • Litigation support • Guidance/ assistance in evaluating expense claims • Preparation of India specific financial statements • Obtaining a report from an Indian CPA 	<ul style="list-style-type: none"> • Assistance in responding notices issue for re-audit proceedings • Evaluating whether the validity of the re-opening can be challenged in the High Court • Litigation support • Analyzing the data for earlier years to evaluate MAT impact, if any • Guidance/ assistance in evaluating expense claims • Preparation of India specific financial statements • Obtaining a report from an 	<ul style="list-style-type: none"> • Guidance/ assistance in evaluating expense claims • Preparation of India specific financial statements • Obtaining a report from an Indian CPA certifying that the book profit on which MAT is computed is correct

certifying that the book profit on which MAT is computed is correct	Indian CPA certifying that the book profit on which MAT is computed is correct	
Deloitte can also assist in analysis from a tax provision standpoint (similar to US FIN 48)		

Comments

The Budget amendment proposed by the Finance Minister in the Finance Bill 2015, although well-intended, has given rise to various questions. FIs will need to ensure preparedness against levy of MAT by evaluating the risks involved and then take steps to mitigate the risks.

Do you know about Dbriefs?

Dbriefs are live webcasts that give valuable insights on important developments affecting your business. To register, visit the [Dbriefs](#) page.

 [Download the report](#)



Contacts

Ahmedabad

Heritage, 3rd Floor,
Near Gujarat Vidyapith,
Off Ashram Road,
Ahmedabad – 380 014.
Tel: + 91 (079) 2758 2542
Fax: + 91 (079) 2758 2551

Bangalore

Deloitte Centre, Anchorage II,
100/2, Richmond Road,
Bangalore 560 025.
Tel: +91 (080) 6627 6000
Fax: +91 (080) 6627 6010

Chennai

No.52, Venkatanarayana Road,
7th Floor, ASV N Ramana Tower,
T-Nagar,
Chennai 600 017.
Tel: +91 (044) 6688 5000
Fax: +91 (044) 6688 5050

Coimbatore

Shanmugha Manram
41, Race Course,
Coimbatore
Tamil Nadu - 641018
Tel: + 91 (0422) 439 2801
Fax: +91 (0422) 222 3615

Delhi/Gurgaon

Building 10,
Tower B, 7th Floor,
DLF Cyber City,
Gurgaon 122 002
Tel : +91 (0124) 679 2000
Fax : + 91 (0124) 679 2012

Hyderabad

1-8-384 and 385, 3rd Floor,
Gowra Grand S.P.Road,
Begumpet,
Secunderabad – 500 003.
Tel: +91 (040) 6603 2600
Fax: +91 (040) 6603 2714

Kolkata

Bengal Intelligent Park Building Alpha,
1st floor, Block EP and GP Sector V,
Salt Lake Electronics Complex,
Kolkata - 700 091.
Tel : + 91 (033) 6612 1000
Fax : + 91 (033) 6612 1001

Mumbai

Indiabulls Finance Centre,
Tower 3, 28th Floor,
Elphinstone Mill Compound,
Senapati Bapat Marg, Elphinstone (W),
Mumbai – 400013
Tel: + 91 (022) 6185 4000
Fax: + 91 (022) 6185 4101

Pune

106, B-Wing, 7th Floor,
ICC Trade Tower,
Senapati Bapat Road,
Pune – 411 016.
Tel: + 91 (020) 6624 4600
Fax: +91 (020) 6624 4605

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms, each of which is Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. Please see www.deloitte.com/about for a more detailed description of DTTL and its member firms.

This material and the information contained herein prepared by Deloitte Touche Tohmatsu India Private Limited (DTTIPL) is intended to provide general information on a particular subject or subjects and is not an exhaustive treatment of such subject(s). This material contains information sourced from third party sites (external sites). DTTIPL is not responsible for any loss whatsoever caused due to reliance placed on information sourced from such external sites. None of DTTIPL, Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the "Deloitte Network") is, by means of this material, rendering professional advice or services. The information is not intended to be relied upon as the sole basis for any decision which may affect you or your business. Before making any decision or taking any action that might affect your personal finances or business, you should consult a qualified professional adviser.

No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this material.

©2015 Deloitte Touche Tohmatsu India Private Limited. Member of Deloitte Touche Tohmatsu Limited

[Home](#) | [Add Deloitte as a safe sender](#)

Follow us on:

