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Minimum Alternate Tax ("MAT") Update

Operational tax news

Historic position

Foreign Institutional Investors ("FIIs")/Foreign Portfolio Investors ("FPIs") mainly invest directly in Indian listed securities and their profits consist of interest, dividend and capital gains considered as Indian sourced income.

As per Section 115AD of the Income Tax Act, short-term capital gains realized on securities subject to the Securities Transaction Tax ("STT") are taxed at a rate of 15% while a 30% rate applies on short-term gains where no STT was paid. Long-term capital gains realized on securities subject to STT are exempt from tax while a 10% rate applies on long-term gains where no STT was paid. Interest income on Government and certain corporate bonds is subject to a tax rate of 5% (all of the above rates are also subject to surcharges).

Previously, it was understood that the Minimum Alternate Tax ("MAT"), an 18.5% (plus surcharges) tax computed on the book profits of a company, did not apply to FIIs/FPIs but only to domestic companies.

Very recently, Indian Tax Authorities have started issuing assessments requesting the payment of the MAT to FIIs/FPIs, which are now potentially subject to an 18.5% rate (plus surcharges) across the various types of securities mentioned above.

Consequently, MAT is a clear concern for Luxembourg investment funds investing directly (and not through an intermediary structure) as these do not benefit from treaty protection in India.

2015 Budget approval

In the Indian Budget for the fiscal year 2015-2016, the Finance Minister clarified that the MAT would not apply to FPIs/FIIs as from 1 April 2015 in respect of specific capital gains i.e. short-term capital gains where STT was paid and long-term gains irrespective of STT. This budget was approved by the lower house of the Parliament on 30 April 2015.

More importantly, it is now clear that the Indian tax authorities intend to apply the MAT to previous years (before 1 April 2015) and in line with the seven year statute of limitation (meaning up until the 1 April 2008).

Please see the **Tax Alert** issued by our team in India for a more detailed view on the application of the MAT to FPIs/FIIs.

For the time being, the recent shift in the position of the Indian tax authorities is giving rise to more questions than answers.

Limited clarification for FPIs/FIIs

On 22 April, the Indian government clarified, during a private conference call with asset managers that, where the provision of a Double Taxation Agreement ("DTA") would be applicable to income earned and/or gains realized by FIIs/FPIs, MAT would not apply.

On 24 April, it was further announced that the Indian Central Board of Direct Taxes had informed its offices that they must rule on treaty protection claims made by FPIs/FIIs within one month of filing. Accordingly, where FPIs/FFIs have submitted requests for the application of treaty benefits in respect of the MAT, decisions from the Indian tax offices should be processed within one month.

Impact for Luxembourg investment funds

Luxembourg investment funds have already started receiving tax assessments for the most recent past years, including not only the taxes due but also late payment interest.

As clarified in the 22 April announcement, FPIs/FIIs can, in theory, seek an exemption from the MAT based on an applicable DTA signed by India. In the case of Luxembourg SICAVs, the DTA with India is known, from a Circular issued by the Luxembourg Tax Authorities, not to apply (also specifically noted in Article 30 of the DTA). Therefore, in principle, unless investments were routed through a jurisdiction providing treaty protection with India (such as Mauritius and Singapore), Luxembourg SICAVs directly investing in Indian securities would therefore be exposed to Indian MAT on their income and capital gains.

As, under the Indian domestic rules, the MAT only applies to corporate entities, we understand that FCPs would be out of scope of the tax as these do not qualify as corporate entities.

We advise our clients to reach out to their tax advisors to assess any potential MAT liability and, where required, take legal action to protect your rights and interests if necessary.

We will keep you updated in case of any new developments.

If you have any queries regarding the above, please do not hesitate to contact us.

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