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Relief cue in capital gains levy

OUR SPECIAL CORRESPONDENT

New Delhi, June 6: Employee stock options, foreign direct investment, investment made by venture capital firms and off-market deals that are recognised by the RBI, Sebi, a high court or the Supreme Court will not face a capital gains tax, even if no securities transaction tax has been paid on them, the income tax department has said.

The clarification on tax rules for capital gains made on certain equity investments where securities transactions tax (STT) has not been paid puts an end to the uncertainty that arose from a budget proposal relating to such transactions.

An amendment to section 10(38) of the income tax act had been brought in after the tax department noticed that shell companies were being created by entering into sham transactions and unaccounted income was being routed into these companies to get the benefits of long-term capital gains.

The amendment provides that capital gains exemptions for income arising from the transfer of shares acquired on or after October 1, 2004 will be available only if the acquisition was chargeable to STT.

STT mandatory

The income tax department has now notified three types of transactions where the provision will apply, while sparing genuine ones.

The first is where an acquisition of a listed equity share, which is not frequently traded on a recognised bourse, takes place through a preferential issue.

Second, those acquisitions where the listed scrip is not purchased on a recognised stock exchange. Third, an acquisition during the delisting period of the company.

For each of the three categories, payment of STT will be mandatory to enjoy benefit of capital gains exemptions.

CLARITY CLUE

No capital gains tax even if STT not paid

- Esops, FDI, investment by VC firms and off-market transactions recognised by the RBI, Sebi, a high court or Supreme Court

STT mandatory to get tax benefit

- When a listed share, which is not frequently traded on a recognised bourse, is bought through preferential issue
- When a scrip is not purchased on a recognised bourse
- Acquisition during de-listing period

Exempted list

In the final regulations released today, the tax authority has provided clear exemptions for employee stock options (ESOPs) and approved merger and acquisitions (M&As). Even the acquisitions made by scheduled banks as a part of a debt restructuring have been exempted.

However, the government has postponed the implementation of the new rules by one year to April 2018.

Abhishek Goenka, partner and leader direct tax, PwC, said: "This notification comes as a breather for foreign investors and venture capital houses as well as shareholders who have acquired shares upon corporate restructuring undertaken vide court-approved schemes on which no STT was paid."

"The notification clearly intends to allow genuine transactions the benefit arising from section 10(38) without making any exceptions," he said.

"The notification is a big relief for investors and shall re-instate their confidence that the Indian tax system is becoming taxpayer friendly and is prompt in bringing tax certainty to avoid unwarranted litigation. This notification is applicable from April 1, 2018 and shall accordingly apply to assessment year 2018-19," Nangia & Co managing partner Rakesh Nangia said.

"One notable differentiation is extending the benefit of exemption to transactions such as gifts, holding subsidiary transactions or transactions involving mergers and demergers and other forms of corporate reorganisations, provided that the original allottee of the said equity shares had acquired the equity shares in a manner compliant with this final notification," said Amit Agarwal, partner, Nangia & Co.