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Long-term capital gains on transfer of listed securities in an off-market transaction by a non-resident to be taxed at lower rate of 10%

In brief

The Authority for Advance Rulings (AAR), in case of Pan-Asia iGATE Solutions Mauritius[1] (applicant), held that long-term capital gains (LTCG) on sale of listed shares in an off-market transaction by a non-resident would be taxable at lower rate of 10%. Delhi High Court (HC) ruling in case of Cairn UK Holdings Limited[2] followed.

Facts

- Patni Computer Systems Limited (Patni) was a listed Indian company.
- iSolutions Inc., USA purchased equity shares of Patni in foreign currency.
- Applicant proposed to purchase equity shares of Patni from iSolutions Inc., USA, in an off-market transaction.

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1 Pan-Asia iGATE Solutions, Mauritius, *In re* [TS-296-AAR-2014]
2 Cairn UK Holdings Limited, *In re* [TS-510-HC-2013(DEL)]

Issue

Whether applicant was required to withhold tax under section 195 of the Income-tax Act, 1961 (the Act) at 10% (excluding surcharge and cess) under the Act on the LTCG arising to iSolutions, Inc.

AAR ruling

The AAR took note of the observations of Delhi HC ruling in the case of Cairn UK Holdings Limited (Cairn UK)[2] (supra) and held as under:

- First proviso (to neutralize exchange rate fluctuation) and second proviso (to neutralize the effect of inflation by way of indexation) to section 48 of the Act operated independently and had different purposes and objectives.

- Proviso to section 112 of the Act was applicable to listed securities (on which Securities Transaction Tax was not paid), or units or zero coupon bonds. Proviso to section 112 of the Act was not applicable to debentures. Thus, proviso to section 112 of the Act was more restrictive and would not necessarily apply in all cases covered by first proviso to section 48 of the Act.

- The legislative intention of section 112 of the Act was to tax LTCG on listed shares, bonds and units at 10% without the benefit of indexation, under the second proviso to section 48 of the Act.

- It was impermissible to read more into the above provisions based on assumption and guess work.

PwC Observations

Relying on the Delhi HC ruling in case of Cairn UK[2] (supra), the AAR held that the applicant shall withhold tax on LTCG arising to a non-resident seller at a lower rate of 10.56% (including surcharge and education cess) under the proviso to section 112(1) of the Act.

The Ruling reaffirms that a non-resident taxpayer is liable to a lower rate of 10% in determining its capital gains tax liability on the sale of listed securities in an off-market transaction.

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