



Foreign Portfolio Investors

September 2024

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Regulatory updates – SEBI, RBI

University funds and university related endowments exempted from additional disclosures¹

Pursuant to Board Meeting of Securities and Exchange Board of India (SEBI) dated 27 June 2024, SEBI issued circular providing exemption from additional disclosure to University Funds and University related Endowments, which are registered or eligible to be registered as Category I FPI, subject to conditions.

The eligible jurisdictions with respect to exemption granted to university funds and university related endowments to be as specified by SEBI.

Source: SEBI circular SEBI/HO/AFD/AFD-POD-2/P/CIR/2024/104 dated 1 August 2024

Reduction in timelines of bonus issue

In order to have uniformity in timelines for credit and trading of bonus shares, SEBI has issued draft circular for public comments on streamlining the process and reduction in timelines of bonus shares.

Presently, the bonus shares are made available for trading in 2-7 working days post record date.

Bonus shares to be credited in depository system latest on T+1 day and bonus shares allotted be made available for trading T+2 day.

Source: SEBI Draft Circular for Public Comments dated 6 August 2024

¹ Criteria for additional disclosure

- FPIs holding more than 50 per cent of their Indian equity Assets Under Management (AUM) in a single Indian corporate group (concentration criteria); or
- FPIs that individually, or along with their investor group holds more than INR25,000 crore of equity AUM in the Indian markets (size criteria).

Foreign portfolio investments in Indian company

Ministry of Finance has amended Foreign Exchange Management (Non-debt Instruments) Rules, 2019 which *inter alia*, provides that aggregate foreign portfolio investments up to sectoral caps will not require government approval or compliance² with sectoral conditions, provided such investment does not result in transfer of ownership or control of resident Indian company from resident Indian citizen to non-residents.

Source: Ministry of Finance, Foreign Exchange Management (Non-debt Instruments) (Fourth Amendment) Rules, 2024 dated 16 August 2024

Scope of additional disclosure¹ expanded

SEBI released consultation paper on investment by Foreign Portfolio Investors (FPI) through segregated portfolios/P-notes/Offshore Derivate Instruments (ODI) seeking comments from public by 27 August 2024.

Background

The requirement for granular disclosure was not directly applicable to ODI subscribers i.e., the concentration criteria and size criteria in equity investments are not considered at the ODI subscriber level. This enables a FPI to potentially get around the granular disclosure obligations by taking exposure through ODI route. A potential for regulatory arbitrage was also seen in case of FPIs with segregated portfolios.

² Earlier, the regulations provided that aggregate foreign portfolio investment up to forty-nine percent of the paid-up capital on a fully diluted basis or the sectoral or statutory cap, whichever is lower.

FPIs with ODIs

Additional disclosure framework to be made applicable to ODI subscribers. The criteria to be monitored by ODI issuers and their designated depository participants/depositories.

Use of derivatives by ODI issuers

FPIs are prohibited from issuance of ODI with derivative as underlying, with exception of those derivative positions taken by the ODI issuer for hedging the equity shares held by it, on a one-to-one basis.

It is proposed to discontinue the existing exceptions related to use of derivatives by ODI issuers. ODI issuers to be prohibited from issuing ODIs with derivatives as reference/underlying and hedging their ODIs with derivative positions on stock exchanges.

Existing ODIs to be redeemed within one year from date of issuance of the framework.

Issuance of ODIs through separate registration

Where ODIs are issued by an FPI that holds assets on behalf of other investors, there is a possibility of commingling of such investments with the assets held for hedging the ODIs.

It is proposed that issuance of ODIs only through separate dedicated FPI registration where no proprietary investments are permitted.

FPIs with segregated portfolio

The additional disclosure requirements to be made applicable to segregated portfolio of FPIs with sub-funds or separate classes of shares or equivalent structures.

Further, for computing breach of concentration criteria by an FPI with segregated portfolios, the Indian equity AUM of each of segregated portfolios to be considered independently.

General:

The FPI issuing the ODI or having segregated portfolio be required to ensure compliance.

In case of non-compliance with the disclosure requirements within specified timelines, it would result in mandatory redemption of ODIs by subscribers within 180 days or in case of FPI with segregated portfolio, liquidation within 180 days from the date registration becomes invalid.

Source: SEBI Consultation Paper dated 6 August 2024



International Financial Services Centres (IFSC)

Persons resident outside India permitted to invest in Sovereign Green Bonds (SGB) in IFSC

Reserve Bank of India (RBI) has permitted persons resident outside India³ that maintain a securities account with a depository in IFSC in India to purchase or sell SGB in IFSC issued by the Government of India. The amount of consideration for purchase to be paid out of

inward remittance from abroad through banking channels or out of funds held in a foreign currency account maintained in accordance with the regulations issued by the RBI/IFSC Authority. The sale/maturity proceeds (net of taxes, as applicable) may be remitted outside India.

Source: RBI notification No. FEMA.396(3)/2024-RB dated 2 August 2024



Income tax- case laws, notification

The Finance (No.2) Act, 2024

The Finance (No.2) Bill, 2024 received the assent of the President on 16 August 2024 and is enacted.

Source: Ministry of Law and Justice dated 16 August 2024.

Dispute Resolution Scheme (e-DRS)

The Central Board of Direct Taxes (CBDT) has notified e-DRS with the aim to reduce litigation and provide relief to eligible taxpayers.

³ Funds/schemes, including the ones setup by entities incorporated in India, regulated by IFSCA under the IFSCA (Fund Management) Regulations, 2022 to also be considered as eligible investors.

A taxpayer can opt for e-Dispute Resolution against the 'specified order' as defined in section 245MA of the Income-tax Act, 1961 (the Act) which includes an order in which the aggregate sum of variations proposed or made does not exceed INR10 lakh (approx. USD0.120 million) and returned income for relevant assessment year does not exceed INR50 lakh (approx.USD0.602 million). The dispute resolution committee may make modification to the variations in the specified order and decide to grant reduction/waiver of penalty and prosecution.

Further, such order should not be based on search/surveys or information received under a double tax avoidance/exchange of information agreement etc. referred to under section 90 or 90A of the Act.

The application is to be filed within one month from the date of receipt of specified order. In cases where appeal has already been filed and is pending before the Commissioner of Income-tax (Appeals), the application is to be filed on or before 30 September 2024.

Source: Press Release, Ministry of Finance dated 30 August 2024

Review petition against Supreme Court (SC) order which held that treaties and protocols are per se unenforceable and are required to be notified - dismissed

The SC had passed on order dated 19 October 2023 ruling in favour of the Revenue and had held that the Most Favoured Nation (MFN) clause under tax treaties between India and other countries is not triggered automatically and a separate notification is required to extend the benefit.

Further, SC had stated that a notification under section 90(1) of the Act is necessary and a mandatory condition to give effect to a tax treaty, or any protocol. Also, that the beneficial treatment given under a subsequent treaty with a country, which is not an OECD member on the date of entering into the treaty, but subsequently becomes an OECD member, cannot be claimed under MFN clause. Against the above order, review petition was filed which has been dismissed by the SC.

Source: Supreme Court Review Petition Nos. 77, 82 & 83 OF 2024 dated 6 August 2024

Claim of tax deducted at source cannot be restricted to the amount claimed in the return of income (ITR) where the appellate authorities have allowed credit while passing order

In the present case, the Income-tax Appellate Tribunal (ITAT), during appeal proceedings had allowed grant of short credit of taxes deducted at source to the taxpayer, which was reflected in Form 26AS but was not claimed in the ITR and directed Assessing Officer (AO) to verify and pass order.

However, while passing order giving effect, AO had restricted the refund to the amount claimed in the ITR. Against this order, the taxpayer filed writ petition before the High Court (HC).

The HC ruled in favour of taxpayer and held that where refund becomes due and payable consequent to order passed in appeal or other proceedings, AO is obliged to refund the amount to taxpayer without having made claim in ITR.

Source: Delhi HC Writ Petition 6589 of 2024 dated 22 August 2024

Subscription of shares cannot be treated as income

The taxpayer made subscription of shares in an Indian company and thereafter made outward remittance of excess funds. The taxpayer had not earned any income and did not file ITR.

The AO initiated re-assessment proceedings alleging that in absence of ITR, the source of income of the investment remained unexplained. Against the order initiating re-assessment, the taxpayer filed writ petition.

The HC held that subscription of share capital in India would be a 'capital account transaction'. Since funds were remitted in India were used for subscription in securities, no income was earned and therefore the taxpayer was under no requirement to file ITR in India.

Further, HC held the fundamental premise of the Revenue that the investment made by the petitioner in shares amounted to "income" which has escaped assessment, was flawed and notices cannot be sustained.

Source: Delhi HC Writ Petition 10507 of 2023 dated 09 August 2024

Tax treaty benefit under India- Mauritius tax treaty (tax treaty) allowed on capital gains on transfer of shares

The taxpayer is a Mauritius based company holding Global Business License (GBL) and has Tax Residency Certificate (TRC). The taxpayer had acquired shares prior to 1 April 2017 of a Singapore based company which derived its value from India. On the sale of shares, the taxpayer claimed tax treaty benefit under Article 13(4) of the tax treaty.

The taxpayer had filed an application before Authority for Advance Ruling which denied tax treaty benefit on the ground that arrangement was designed to avoid tax. Against the order, the taxpayer filed writ petition before the HC.

The HC ruled in favor of the taxpayer based on the TRC provided, the economic substance, satisfaction of limitation of benefit clause and stated that tax treaty benefit would be available, and the transaction is

grandfathered in regard to the General Anti Avoidance Rules. Further the HC inter alia, held that:

- A parent/holding company would have a legitimate right to exercise oversight and broad supervision over the affairs of its subsidiaries which could take the form of seats on the Board of Directors, appointment of key managerial personnel etc.
- An entity situated in Mauritius should not result in a default adverse inference or raise a presumption of such an entity being a colourable device nor are Mauritian entities required to satisfy any separate standard of legitimacy or stricter standard of proof
- Domestic tax legislation not to be interpreted in a manner which brings it in direct conflict with a treaty provision or with an overriding effect over the provisions contained in a tax treaty
- The concept of **beneficial ownership** would get attracted if it be established that the holder of income had no control over the income and merely holds the same till such time it be instructed to deploy that income to another entity or if the income is controlled or regulated by a third party with holder having no

real or substantive control over that income.

Source: W.P.(C) 6764/2020 & CM APPL. 23479/2020 Delhi High Court dated 28 August 2024

Interest under section 234B or 234C of the Act cannot be imposed where the payer failed to withhold tax

The FPI had investments in debt securities such as commercial papers, non-convertible debentures, and government securities. On interest income received from such securities, the payers did not deduct tax at source. Hence, FPI paid advance tax to discharge tax liability.

At the time of processing ITR, interest under section 234B (interest for defaults in payment of advance tax) and 234C (interest for deferment of advance tax) was levied.

On appeal, ITAT held noted that the provisions provide that in order to compute interest, the tax chargeable on the total income is to be reduced by amount of tax deductible or collectible. The taxpayer cannot be held responsible for the default of the payers and deleted the interest.

Source: ITA No. 2505/Mum/2024 Mumbai ITAT dated 14 August 2024



Market watch-press articles- select extracts

India votes for UN's Terms Of Reference on global tax

India was among top 110 countries that voted, in favour of adopting the 'Terms of Reference' for United Nations (UN) Framework on international tax co-operation.

A key term of reference which India and several countries wanted was addressing tax-related illicit financial flows, tax avoidance, tax evasion and harmful tax practices.

Under the UN framework, developing countries – African and Asian countries including India – are likely to have a greater say in the formulation of global tax rules.

Source: The Times of India, Lubna Kably, 18 August 2024

FinMin may make life easy for FPIs keen on larger equity slice in listed companies

The Finance Ministry is working on a mechanism that would allow certain foreign portfolio investors (FPIs) the flexibility to seamlessly move into FDI category, if they so wish.

This facility is likely to be extended to those FPIs who are keen to own more than 10 per cent in a listed entity but are unable to do so given the current 10 per cent ownership cap in this category. Currently, FPIs can only own below 10 per cent in a listed company.

Source: The Hindu Businessline, KR Srivats, 23 August 2024



FPI statistics – FPI portal, NSDL

Parameters	Current month	Earlier month	Changes
Net Equity inflows during August 2024 (in USD million)	882	3,899	
Net Debt inflows during August 2024 (in USD million)	2,057	1,949	
Total FPIs registered as on 31 August 2024	11,525	11,479	46
AUC of FPIs at end of July 2024 (in USD million)	968,552	928,777	39,775

Source: FPI portal, NSDL, 31 August 2024

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