

By Electronic Delivery

18 July 2019

Smt. Nirmala Sitharaman
Minister of Finance
Government of India
North Block
New Delhi 110 001
India

RE: *Indian Budget Proposal to Increase Tax
on Non-Corporate CIVs*

Honorable Minister Sitharaman:

The collective investment vehicle (CIV) associations joining this letter—on behalf of CIV investors globally—urge a CIV exception¹ from the tax surcharge increase proposed by the Finance (No. 2) Bill, 2019. As publicly available “retail” investment pools, CIVs are widely held by moderate-income investors. CIVs are not designed for “the super-rich.”

CIVs are highly regulated funds. While their form of organization and taxation varies by jurisdiction, they share a common objective: provide moderate-income investors with ready access to a diversified portfolio of securities that is managed at reasonable cost and subject to a sound regulatory regime. CIV units are publicly offered for purchase through continuous distribution or on a regulated stock exchange. In those countries in which a CIV may be organized in either non-corporate (*e.g.*, trust) or corporate form, the securities laws apply equally to both forms of organization.² The domestic tax regimes applicable to the CIVs we represent operate with the same objective—ensuring that a CIV’s income and gains are taxed only once (either at the level of the CIV or its investors)—as do those domestic mutual funds organized in India.

¹ The exception we proposed would be limited to funds that are widely held, hold a diversified portfolio of securities and are subject to investor-protection regulation in the country in which they are established. This is the precise definition adopted by the Organisation for Economic Co-operation and Development (OECD) in their report entitled “[The Granting of Treaty Benefits with Respect to the Income of Collective Investment Vehicles](http://www.oecd.org/tax/treaties/45359261.pdf)” (the “CIV Report”) — <http://www.oecd.org/tax/treaties/45359261.pdf>. This same definition is being advanced by the United Nations’ Committee of Experts on International Cooperation in Tax Matters as it develops CIV-specific Commentary for the UN Model Income Tax Convention. See, <https://www.un.org/esa/ffd/wp-content/uploads/2018/08/CRP10-Taxation-of-Collective-Investment-Vehicles-CIVs.pdf>. Importantly, our proposed exception would not apply to investments through private equity funds, hedge funds or other entities that are designed for the super-rich.

² In Europe, for example, the Undertakings for Collective Investment in Transferable Securities (UCITS) Directive applies equally to CIVs organized as companies or as non-corporate vehicles such as trusts. The same is true in the United States under the Investment Company Act of 1940 and in Canada under provincial and territorial securities legislation (see, for example, the *Securities Act* (Ontario)).

The recently announced proposed increase (of either three or seven percentage points) on the capital gains of Associations of Persons (AoPs) is very significant and will impact the investment decisions of CIVs organized as trusts and other non-corporate vehicles. CIVs strongly prefer stable tax regimes as taxes have a substantial impact on investors' returns. This tax proposal, which has impacted the market negatively, was very unexpected and discriminates against CIVs organized in non-corporate form. Moreover, it will fall directly on CIV investors—who are not the super-rich. Moreover, if this tax comes into effect, it will have an immediate impact on all funds that have unrealized gains and calculate the net asset value of their units by taking into account capital gains taxes due upon disposition.

We understand, from press reports, that some in the Indian Government believe that funds have a choice of forming as trusts (or other non-corporate vehicles) or as companies and can convert easily from one to the other. This view is not accurate. CIV sponsors typically offer a wide range of CIVs to their investors. Legal requirements and business considerations often dictate, as a practical matter, the form in which a CIV is organized. The business considerations are particularly problematic when a firm sponsors tens or hundreds of CIVs all organized as trusts (or another non-corporate structure) and uses this structure for any CIV that invests in India. Adopting a new structure simply for a CIV that will invest in India is both expensive and fails to address the impact of the proposed tax increase on the investors in the CIVs already investing in India. These costs cannot be avoided by converting from a trust (or another non-corporate vehicle) to a corporate structure because, among other reasons, the conversion could be viewed as a purely tax-driven restructuring—which could have negative tax consequences both in the CIV jurisdiction and in India. Consequently, conversion in many countries is not a viable option.

We strongly urge the Indian Government to resolve this issue for CIV investors by amending the Finance (No. 2) Bill, 2019 to provide an exception for CIVs. The same result also could be reached by either carving out CIVs registered with the Securities and Exchange Board of India as Category 1 FPIs or Category 2 FPIs for surcharge rates at par with corporates or by notifying CIVs as companies under section 2(17) of the Indian Income-tax Act, 1961.³

Because CIVs are available to all investors, and not crafted for the super-rich, our proposal will achieve the Government's objective without substantially disrupting the flow of foreign portfolio investment that is important to the Indian economy. Particularly if the legislation is not amended, and a notification is required to prevent the negative impact on CIVs' net asset values, it is essential that this exception be agreed promptly.

Please feel free to contact any of the signatories below for additional information regarding the CIVs represented by their organizations.

³ Section 2(17) of the Indian Income-tax Act, 1961 empowers the Central Board of Direct Taxes to declare by general or special order any institution, association, or body whether incorporated or not, and whether Indian or non-Indian, to be a company.

CIV Industry Coalition Letter on Proposed Tax Surcharge Increase on Trusts

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With kind regards,

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