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ASIA SECURITIES INDUSTRY & FINANCIAL MARKETS ASSOCIATION

28 March 2012

The Hon. Pranab Mukherjee
Finance Minister
Ministry of Finance
North Block
New Delhi 110001

Dear Finance Minister,

Re: Certain amendments proposed by the Finance Bill, 2012, (the 'Bill') to the Income-tax Act, 1961

On behalf of the membership of the Asia Securities Industry & Financial Markets Association (ASIFMA)[1] and the Securities Industry and Financial Markets Association (SIFMA)[2], we are writing to express our deep concern that certain portions of the Finance Bill 2012 ('Bill') could adversely impact investment in the Indian capital markets by the global investment community.

Specifically, the Bill's provisions relating to taxation of indirect transfers of assets as well as the General Anti-Avoidance Rule ('GAAR') are very broadly worded and could be interpreted to tax Foreign Institutional Investors ('FIIs') on their investments in the Indian listed equity markets.

FIIs are significant sources of foreign direct investment in India, with assets under custody of more than Rs. 10 lakh crores (over US$200 billion) or 17% of the capitalization of India's equity markets. They have also infused substantial sums in buying Indian Government and corporate debt and are keen to increase such investments, regulations permitting. Global investors who do not qualify as FIIs or Qualified Foreign Investors ('QFIs') rely on these institutions to invest in the Indian capital markets.
FIIs fear that the new tax rules could subject this foreign investment to double or triple taxation. Such onerous taxation – or even the risk of such taxation – could threaten this important source of capital for India's businesses.

Since the budget announcement on March 16, an enormous amount of attention has been paid to these taxation issues within the investor community. FIIs are carefully evaluating these new tax risks. Some institutions have told their clients that they will not take on any new India positions. Others are hopeful that once the Indian government understands the gravity of the situation the tax rules will be clarified. However, if these tax uncertainties are not resolved quickly we fear that FIIs will decide that the tax risks are unacceptable. These investors may then proceed to liquidate their India investments and such a

[1] The Asia Securities Industry & Financial Markets Association (ASIFMA) is an independent association that promotes the development of liquid, efficient and transparent capital markets in Asia and facilitates their orderly integration into the global financial system. ASIFMA priorities are driven by over 40 member companies involved in Asian capital markets, including global and regional banks, securities dealers, brokers, asset managers, credit rating agencies, law firms, trading and analytic platforms, and clearance and settlement providers. ASIFMA is located in Hong Kong and works closely with global alliance partners: the Global Financial Markets Association (GFMA), the Securities Industry and Financial Markets Association (SIFMA) and the Association for Financial Markets in Europe (AFME). More information about ASIFMA can be found at: www.asifma.org.

[2] The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org

disorderly dissolution of large positions held by these overseas investors could seriously disrupt the Indian capital markets.

We believe these tax results are *unintended* consequences of the Bill and that the solutions are straightforward. The Standing Committee on Finance (‘Standing Committee’) has given detailed recommendations with respect to the indirect transfer and the GAAR provisions. Their recommendations would avoid market disruptions.

- ***Explanation 4 to Section 9((1)(i) and Explanation to Section 2(14):*** The Bill should incorporate the Standing Committee’s recommendations that the indirect transfer rules should not apply to indirect ownership of “small shareholdings” of Indian companies. We understand that this recommendation was intended to ensure that the indirect transfer rule would not affect portfolio investments in listed securities.
- ***GAAR:*** The Bill should reflect the Standing Committee’s recommendations that “there should be certainty on the GAAR provisions so that foreign investors do not become wary of investing in India.” For this purpose, we believe that the GAAR should not apply to “small” investments in listed securities or derivatives that reference these securities or debts held by FIIs.

For both purposes, a “small” investment could be defined as an interest of 10% or less of an Indian listed company (in keeping with the 10% investment limit for each FII). For debts held by FIIs, such as government bonds and listed corporate bonds, these would be within the prescribed limits set by the Securities Exchange Board of India (SEBI). If the Bill were to incorporate these two simple suggestions, then we believe that the Indian capital markets would not be disrupted and the tax authorities would retain the right to tax transactions as intended in the Bill.

As an industry, we are committed to the Indian economy and recognize the potential of India as an investment jurisdiction. We are not averse to paying the appropriate level of Indian taxes, as long as the rules are clear so that investors can plan their affairs with a degree of certainty. Clarifying the above issues will go a long way in further making India an attractive investment jurisdiction.

We are happy to nominate people from among our memberships to work with your team to deliberate on the above issues. Please contact Will Sage, ASIFMA Managing Director at: office - +852 2537 3895; mobile - +852 9813 1519 or email – wsage@asifma.org.

Yours sincerely,

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