FPIs bat for equal taxation on dividends and buybacks

Experts say current situation can lead to double taxation

ASHLEY COUTINHO
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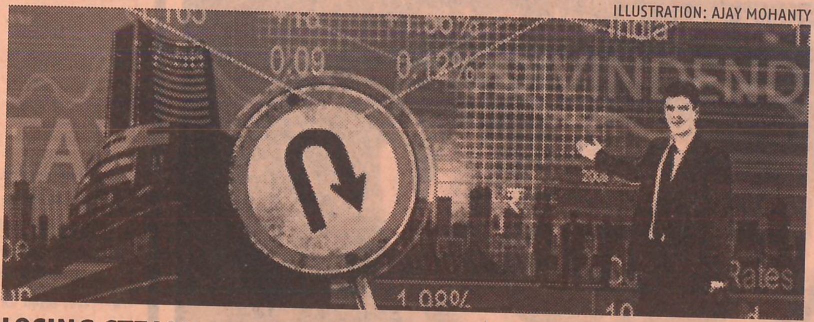
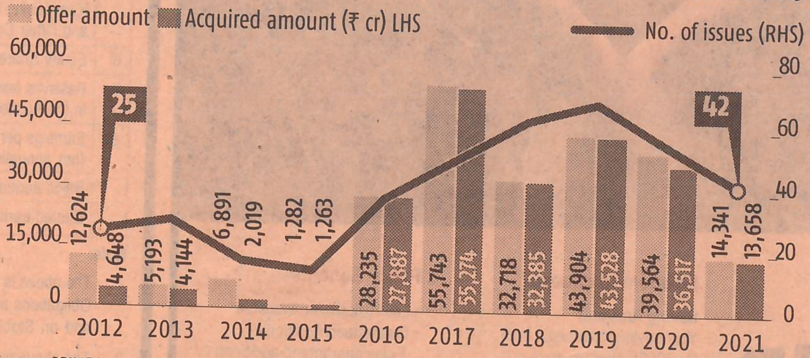
ILLUSTRATION: AJAY MOHANTY



LOSING STEAM

Buyback offers last year were the lowest since 2015



Source : PRIME Database

This year's Union Budget must consider bringing a parity in tax treatment of dividends and buybacks, said market players.

The Budget in 2020 did away with the dividend distribution tax (DDT) in the hands of the company and instead decreed that tax be deducted at source (TDS) at 10 per cent on dividend income paid by a company to shareholders if the amount exceeded ₹5,000 a year. This made dividends taxable in the hands of investors.

Indian companies, however, are still subject to 20 per cent tax (plus surcharge and cess) on share buybacks. In 2013, tax on buybacks was introduced for unlisted companies and exempted for shareholders. In 2019, this was extended to listed companies as well. The reason specified for this was instances of tax arbitrage, whereby listed companies resorted to share buybacks instead of dividend payment, since the tax rate for capital gains was lower than the rate of DDT.

RUN-UP TO THE BUDGET 2022-23

Most of these buybacks were done through the tender route, which allowed promoters to tender their shares. Analysts said promoters had gained the most through share repurchases, while companies had not benefited much.

The taxation, as it stands, could especially impact large shareholders such as foreign portfolio investors (FPIs). For such investors, dividends are now taxable at 20 per cent (plus surcharge and cess) and can be lower if the FPI is from a treaty jurisdiction. Further, due to the re-negotiation of major tax treaties, capital gains on equity shares are no longer exempt.

"For an FPI from a treaty jurisdiction, the tax rate on both dividend and capital gain can be either 10 per cent or 15 per cent. Therefore, the rationale for buyback tax in the hands of listed companies is no longer applicable," said Suresh Swamy, a chartered accountant. "Also, exemption to buyback income in the hands of shareholders leads to a situation where they are unable to claim capital losses on the buyback as the income is exempt."

Tax experts believe that the current situation can lead to double taxation. "Tax on buybacks needs to be abolished and replaced with a tax on shareholders similar to the removal of DDT. Buyback tax results in potential double taxation on the same income because of the way it is calculated," said Rajesh Gandhi, a partner, Deloitte India. "Foreign investors find it challenging to claim credit for the buyback tax since it is not in the nature of a withholding tax on the shareholder. Finally, tax should not decide which method is adopted by the company to reward shareholders."

Buybacks in 2021 dipped 64 per cent year-on-year to ₹14,341 crore. The value of actual buybacks stood at ₹13,658 crore.

Industry seeks tax parity between NBFCs and banks

Over the years, the RBI has tightened the regulatory framework for non-banking finance corporations, especially for large and deposit-taking ones, and brought it close to what is applicable for banks. "For example, their interest on NPAs is taxed on accrual basis and not on receipt basis. Their interest income suffers TDS deducted by borrowers, said Sunil Gidwani, partner, Nangia Andersen. **BS REPORTER**

Economy needs more hand-holding: Goldman

Warning that any sudden and sharp fiscal consolidation steps can throttle the nascent and uneven recovery of the Indian economy, Goldman Sachs said the Budget should instead focus on boosting overall demand, from rural consumption in particular, and invest in infrastructure. The successive Covid waves has made it more difficult to reduce debt as a share of GDP in the medium-term, they said. **PTI**