India Union Budget 2025-26

Sovereign Wealth Funds ('SWFs') and Pension Funds ('PFs')

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Key Tax Proposals

The Honourable Finance Minister (FM) of India, Ms. Nirmala Sitharaman tabled the Union Budget 2025 before the Parliament on 1 February 2025.

In her Budget Speech last year, the FM had mentioned about a comprehensive review of the Income-tax Act, 1961 (the Act) to be completed in six months. In line with this, on 1 February 2025, the FM has announced that the new income-tax bill will be introduced in the coming week.

At present, it is not clear whether it will be sent for public comments.

Further, there has been no substantial amendment in relation to the tax rates for Foreign Portfolio Investors (FPIs).

With the above background, we have summarised key changes which are set to impact the SWFs/PFs below.

Rate of Tax

Rationalisation of long-term capital gain (LTCG) tax rate in case of few securities

- By virtue of amendments made in the Finance (No.2), Act, 2024, LTCG is taxed at the rate of 12.5 per cent (plus applicable surcharge and cess) in case of following assets subject to levy of Securities Transaction Tax (STT):
  - Equity shares
  - Units of an equity oriented mutual fund
  - Units of a business trust (REITs/InvITs)
- However, LTCG on other assets such as listed bonds/debentures, etc., continued to be taxed at erstwhile tax rate of 10 per cent (plus applicable surcharge and cess).
- To bring parity in rate of tax on all instruments, it is now proposed to increase the tax rate to 12.5 per cent (plus applicable surcharge and cess) on LTCG on sale of such assets (i.e., listed bonds/ debentures, etc.)
- FPIs can continue to avail the tax treaty benefit on such gains (wherever applicable).

This change will take effect from AY 2026-27.

Sovereign Wealth Funds (SWF) and Pension Funds (PF)

Sunset clause on exemption to be extended

Income earned by SWFs and PFs from specified infrastructure investments in India, in the nature of interest, dividend and LTCG is exempt from tax in India subject to certain qualifying conditions.

- One of the condition is that the qualifying investment must be made on or before 31 March 2025.
- It is now proposed to extend the said sunset date to 31 March 2030.

This change will take effect from 1 April 2025.

Exemption to be extended to transfer of unlisted debt securities deemed as short-term capital gains

- By virtue of amendments made in the Finance (No.2), Act, 2024, the capital gains earned from unlisted debt securities are classified as STCG (irrespective of the holding period). SWFs and PFs qualified for exemption only in respect of LTCG from investments in the specified infrastructure sector and hence, they do not qualify to claim tax exemption in respect of capital gains arising from transfer or redemption of unlisted debt securities which are deemed to qualify as short term in nature.
- It is now proposed that LTCG (whether or not such capital gains are deemed as STCG) arising from investment made by SWFs/PFs in unlisted debt securities would also qualify to be exempt from tax in India.

This change will take effect from 1 April 2025.

Impact of amendments on Start-Ups and Alternative Investments (AIFs and REIT/ InvIT)

Amendment to definition of Capital Assets

- The definition of 'capital assets' is amended to specifically clarify that all securities held by SEBI registered Category I and Category II Alternative Investment Funds (AIFs) are capital assets.
- Any income arising from transfer of such securities by SEBI registered Category I and Category II AIFs shall be taxed as capital gains. Hence, any income arising in hands of SWF and PF investing in Category I and II AIFs on sale of securities held by AIFs, shall inter-alia be taxed under the head capital gains due to existing pass through status of income in hands of AIFs.

This change will take effect from 1 April 2025.

Rationalization of taxation of long-term capital gains of Business trusts

- An amendment is proposed to the special taxation regime for Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InVITs), collectively referred to as business trusts.
- Currently, the regime stipulates that the total income of a business trust is taxable at the maximum marginal rate (MMR), except for capital gains covered under sec 111A (on listed equity share , equity oriented MF and units of business trust (STT is paid)) and section 112 (on unlisted securities).
- There was no exclusion in special taxation regime for business trusts for section 112A of the Act, which provides for tax of 12.5 per cent on LTCG arising in cases of listed equity shares, units of an equity-oriented fund and units of a business trust on which STT is paid.
- The proposed amendment seeks to now additionally also exclude income taxable under Section 112A (besides section 111A and 112) in special regime for business trusts. Thereby income from sale of securities referred in section 112A by the business trusts shall be taxed at 12.5 per cent instead of MMR.

This change will take effect from 1st April 2026.

Impact of amendments on Start-Ups and Alternative Investments (AIFs and REIT/ InvIT) (Contd.)

Extension of timeline for tax benefits to start-ups

The Act provides for deduction of an amount equal to 100% of the profits and gains derived from an eligible business by an eligible start-up for any three consecutive years out of ten years from the date of incorporation, subject to certain qualifying conditions.

- One of the condition is that the incorporation is before 31 March 2025
- It is proposed to amend the said section so as to extend the benefit for another period of five years, i.e. the benefit shall be available to the eligible start-ups incorporated before 1st April, 2030

This change will take effect from 1 April 2025.

International Financial Services Centre (IFSC)

Inclusion of Retail Schemes and Exchange Traded Funds (ETFs) in the existing exemption on relocation regime of funds and extension of time period for relocation

- Transfer by a shareholder or unit holder or interest holder, in a relocation, of a capital asset being a share, unit or interest held by the holder in the original fund in consideration for the share or unit or interest in resultant fund is not considered as a 'transfer' and hence a tax neutral transfer.
- Original fund means a fund established outside India, subject to fulfillment of conditions.
- Resultant fund was defined to mean a fund established or incorporated in India in the form of trust, company or limited liability partnership which was granted registration as an Alternative Investment Fund (Category I, II and III) and regulated by prescribed authorities and is located in IFSC.
- It is now proposed to expand the definition of resultant fund to include retail scheme and exchange traded fund (regulated under International Financial Services Centres Authority (Fund Management) Regulations, 2022 and satisfies conditions prescribed.
- Further, the time period for relocation i.e. transfer of capital asset of the original fund, or its wholly owned special purpose vehicle, to resultant fund has been extended to 31 March 2030 (from 31 March 2025), subject to conditions.

The change will take effect from AY 2026-27.

Scope of exempt income of non-residents from non-deliverable forward (NDF) contract / offshore derivative instruments (ODI) etc. expanded

- Income accrued or arisen to, or received by a non-resident from
  - transfer of NDF contracts or ODI or over the-counter derivatives, or
  - distribution of income on ODI

  entered into with an offshore banking unit of an IFSC is exempt from tax in India.
- It is now proposed to extend the aforesaid exemption incase of transactions entered between non-residents with FPI being a unit in IFSC .

The change will take effect from AY 2026-27.

Simplified regime for Indian fund managers managing offshore funds

- Under the special taxation regime for offshore funds, the fund management activity carried out by an eligible investment fund through an eligible fund manager located in India does not create a **business connection** in India. This is subject to several condition.
- Basis the representation, the following amendments have been proposed:

Present condition	Proposed changes
Applicable for all the Fund Managers	
The eligible investment fund shall fulfill the condition that the aggregate participation or investment in the fund, directly or indirectly, by persons resident in India, should not exceed 5 per cent of the corpus of the fund.	The condition is rationalised, by determining aggregate participation or investment in the fund as on the 1 April and 1 October of the previous year. In case the condition is not satisfied on either of the said days, then the said condition to be satisfied within 4 months of the said days
Applicable for Fund Managers in IFSC only	
The Central Government may by notification provide relaxation/ modification in safe-harbor conditions for eligible offshore funds as well as eligible fund manager where the eligible fund manager of such offshore fund is set-up in IFSC and has commenced its operations on or before 31 March 2024	The Central Government may by notification provide relaxation/ modification in safe-harbor conditions (other than the condition mentioned above) for eligible offshore funds as well as eligible fund manager where the eligible fund manager of such offshore fund is set-up in IFSC and has commenced its operations on or before 31 March 2030

This change will take effect from 1 April 2025.

Compliance

Rationalisation of Transfer Pricing Provisions

- The taxpayer will now have option to opt for block transfer pricing assessments for carrying out multi-year arm's length price determination.
- Rules in this regard including the Form and timelines to be prescribed

This change will take effect from AY 2026-27.

Omission of Tax collection at source (TCS) on sale of specified goods

No TCS on sale of goods – therefore the conservative view where TCS was applied on sale of shares also abolished

This change will take effect from the 1st day of April 2025

Time limit to file updated return of income extended

- The Finance Act, 2022 had inserted provision to allow taxpayer to furnish an updated return (along with payment of additional tax) within 24 months from the end of the relevant assessment year (AY).
- It is now proposed to extend the time-limit to file return from 24 months to 48 months. Considering the extended time-limit, the rate of additional tax payable is as follows:

Rate of additional tax*	Filing period for the updated return
25 per cent	After the due date of filing return and before completion of 12 months from the end of the relevant AY
50 per cent	After 12 months and before completion of 24 months from the end of the relevant AY
60 per cent	After 24 months and before completion of 36 months from the end of the relevant AY
70 per cent	After 36 months and before completion of 48 months from the end of the relevant AY

**The additional tax is computed on aggregate of tax and interest payable*

- Further, there is an expansion of scenarios wherein no updated return can be furnished

This change will take effect from 1 April 2025.

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