19th July 2014

To,
The Honourable Finance Minister
Shri Arun Jaitley

On behalf of Foundation of Independent Financial Advisors (FIFA) we congratulate you on your maiden budget!

Under the dynamic leadership of the Prime Minister, the financial proposals as laid down by the Government will surely provide a much needed impetus to growth and development.

FIFA represents a pan India body of Individual Financial Advisors/Distributor's who channelize household savings of investors into Mutual Funds.
FIFA had been invited to participate in meetings held by finance ministry to discuss and finalize steps to reenergize the Mutual Fund Industry in July2012.

We are especially concerned about the changes proposed regarding taxation of investments in debt mutual funds. While drafting the changes some vital facts pertaining to various categories of investors seem to have been overlooked. Though you have been espousing the ill effects of retrospective amendments to the Finance Act, the proposed amendments seek to effect changes which have a retrospective tax effect on the investors. This anomaly which quite appears to be more out of oversight needs to be addressed. On behalf of all the Individual Savers and Investors we give herein below our thoughts and suggestions. We request you to kindly consider the same, before the finance bill is being passed.

Prior to the proposed amendments the period of holding of various equity and debt instruments for the purpose of Long Term Capital Gains was a period of twelve calendar months. In case of equity instruments if the same are sold after the period of twelve months of holding and Securities Transaction Tax is paid thereon, then the Long Term Capital Gains are exempt from Tax. In respect of debt funds the Long Term Gains were being taxed at 10%.

The Dividend declared by debt funds is charged to Dividend Distribution Tax @ 28.325 % in case of Individuals and 33.99% in case of corporates. Whereas long term capital gains before indexation were charged to tax @ 10%. Investments in Bank and other debt instruments attract a higher rate of tax. In your Budget Speech, you have mentioned that this allows tax arbitrage opportunity. With a view to remove this tax arbitrage, you have proposed to increase the rate of tax on Long Term gains from 10 % to 20% on transfer of units of such debt funds. You have also proposed to increase the period of holding in respect of such units being treated as long term assets from 12 months to 36 months. In the same speech you have mentioned that this arbitrage has hardly benefitted retail investors as their percentage is very small among such mutual fund investors. These changes are effective from 1st April 2014.

The effect of these proposed changes on investors including retail investors is as under:

- Till the date of declaration of the Budget in respect of 2014, Investors who have invested in Debt Mutual Funds in the genuine belief that holding such units for a period of 12 months would entitle them to concessional rate of tax of 10% on the gains would now have to either hold such investments for a period of 36 months or would have to pay tax at the rate of 33.99 % if they are in the maximum tax bracket.

- Those investors who have redeemed their investments which had been held for a period exceeding twelve months but less than thirty six months between 1st April 2014 till now would have to pay higher tax as the benefit of concessional rate of tax on such Long Term Capital Gains would not be available.

Our humble suggestions

1. The differential tax rate on Bank Deposit Interest and Income from Debt Mutual Funds cannot be compared as they are distinct categories of investment. By its very nature Interest on Bank Deposits is assured. As against that Income from debt funds is a function of many factors bearing interest and credit risks. As such the returns from debt funds are not assured, at times the returns have been negative. In fact even in closed ended products such as FMP's the fund houses cannot give an indicative yield. Therefore it is not strictly an arbitrage opportunity. As there is no arbitrage the proposal to increase the rate of tax on these long term gains from 10% to 20% and to increase the holding period to 36 months is not justified.

2. The period of holding in respect of Mutual Fund debt schemes to be classified as Long Term should be restored to 12 months and the rate of tax on Long Term Gains from such funds without indexation should be restored to 10%.

3. If it is not possible to restore it to 12 months, then the provisions should be made applicable to investments made after the budget date ie 11th July 2014 onwards. Else it will tantamount to retrospective taxation.

4. The tax arbitrage, if any, exists generally and mainly in closed ended products such as Fixed Maturity Plans (FMP's). As such the new provisions should be made applicable only to closed ended schemes all other debt schemes should be outside its purview.

5. Since the Hon'ble Finance Minister has mentioned in the speech that the percentage of retail investors is very small, the proposed provisions should be made applicable only to corporate investors and not to retail investors.

6. The Finance ministry is encouraging individual investors to invest their savings through mutual funds. These investors will find investing through mutual funds not attractive as compared to other avenues. Considering the fact it has taken years to build the assets to current level, movement of assets from mutual funds to other assets classes will not be in the interest of the industry and detrimental to channelizing household savings to capital markets for growth and development and **could see shift back to gold as a preferred savings instrument.**

We have taken this opportunity to highlight the concerns of the investors, especially the retail investors. We are confident the overwhelming mandate given to you by the common people of this country will surely enthuse use you to make the necessary changes in the interest of the retail investors.

Thanking you.

Best Regards,

Dhruv Mehta
Chairman

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