# Finance Bill 2025

# Fueling India’s Financial Powerhouse - AIFs

A special communique, February 2025


SINGHVI
DEV & UNNI LLP
CHARTERED ACCOUNTANTS

# Finance Bill 2025: Review of Key proposals


The Finance Bill 2025 ('Bill') represents an effort to walk the middle path – balancing the pressing need for tax simplification with the realities of economic and administrative constraints. This communique examines the key proposals against the backdrop of:

- **Raising of capital by Indian AIFs.**
  - Trend
  - Tax Proposals
  - Critical Caution Points

- **Deployment of Funds by Indian AIFs.**
  - Trend
  - Tax Proposals – Sectors Benefiting
  - Tax Proposals – GIFT City

- **Thinking for the future**

# Raising of capital by Indian AIFs - Trend

**Investor confidence in the "India story" remains strong, driven by:**

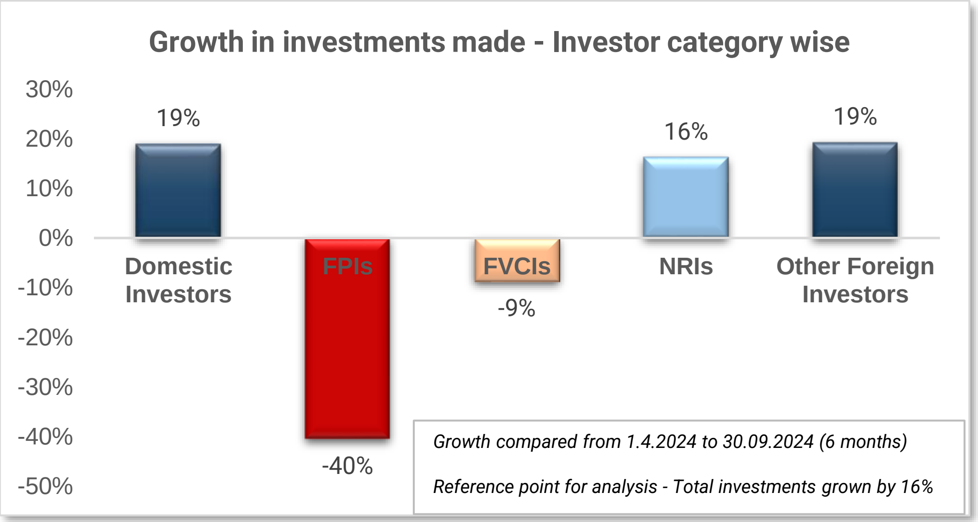
Digital adoption I A thriving startup ecosystem I Structural reforms – sluggish but impactful I Rising investments - foreign, domestic, and IPOs.

**Alternative Investment Funds (AIFs) have expanded significantly:**

- Registered AIFs surged from 42 (March 2013) to 1,485. (January 2025)
- GIFT City commitments reached USD 12.1 billion. (September 2024)

**Maturing investment landscape**

- Investments in AIFs has grown 30% year on year.
- Growth has been primarily driven by domestic investors.




Data is based on the Reports and Statistics published by SEBI on its official website.

# Tax Proposals – Impact Assessment and caution points

## Tax Proposals – Impact Assessment on Raising Capital

- Income from securities such as treasury investments and ***secondary transfers (including units of other funds)*** by Category-I and II AIFs will be ***capital gains***. All securities **held by** Category-I and II AIFs are classified as "capital assets," ensuring gains are taxed as capital gains and not business income.

- The sunset for ***Overseas Sovereign Wealth and Pension Funds*** to invest tax-free in India is extended from March 31, 2025 to March 31, 2030. Further, gains from unlisted debt securities to be treated as LTCG (if held for more than two years) and remain exempt.

***The reduction in personal taxes announced in the Union Budget is likely to increase disposable income & consumer spending, drive economic growth, and enhance investor confidence.***

## Caution Points – Missed the legislature's eye in FB 2025

- Potential double taxation arises in **secondary transfers of AIF units** because the fund's income is taxed at the investor level under the pass-through system, and any subsequent sale of AIF units is again subject to capital gains tax.

- Taxes are accrued on NAV dates assuming full liquidation but are only paid upon realization, ensuring adjustments for fairness among investors. Redemption proceeds are tax-paid at the fund level, but without a clawback mechanism, early exits may **shift the final tax burden** to remaining investors.

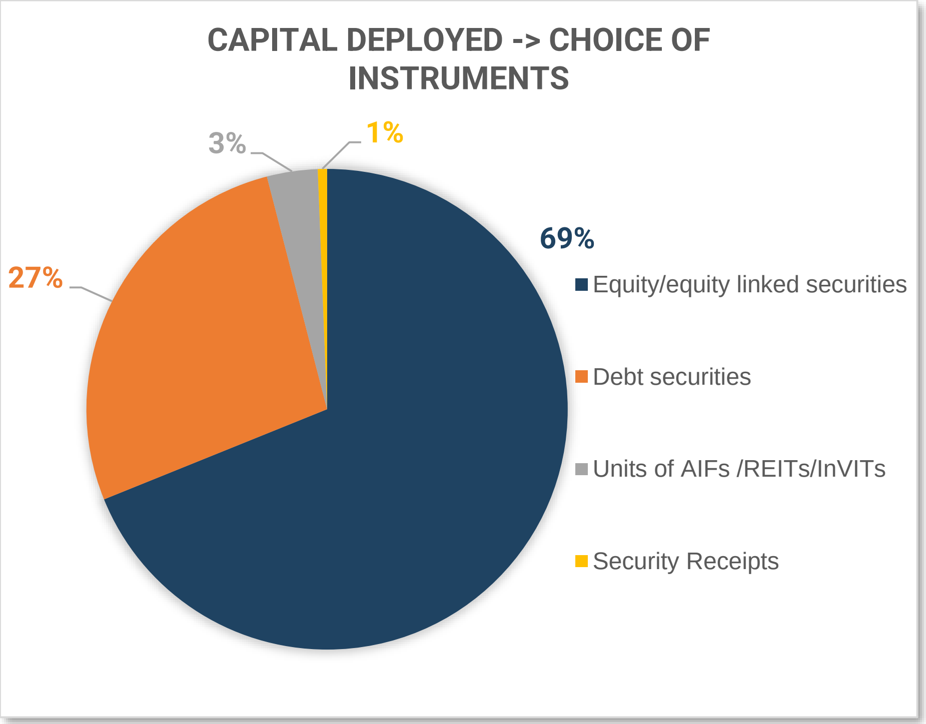
- **Domestic investors** in India generally face a higher tax burden on interest and dividend income compared to **foreign investors**, as they are taxed at their applicable slab rates without treaty benefits. In contrast, foreign investors benefit from lower withholding tax rates under Double Taxation Avoidance Agreements.

# Deployment of Funds by Indian AIFs - Trend

Capital deployment by AIFs has grown by 10% over April to September 2024.

While the unlisted investments by AIF are higher than the listed securities, the AIF as an investment vehicle for Listed securities is gathering traction. (primarily driven by Category III funds)

In the period April 2024 to September 2024, there has been an increase of 25% in investment in listed securities while compared to a 3% increase in unlisted securities.

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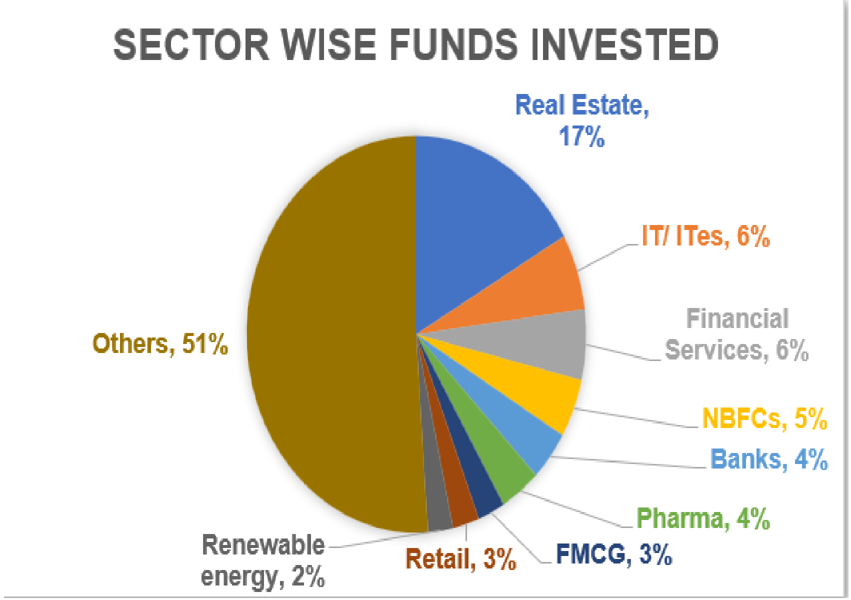
The data for funds deployed is as at 30.09.2024

# Deployment of Funds by Indian AIFs - Trend

**Sector Attraction**

- Last 6 months shows Pharmaceuticals and Financial Services are emerging as preferred sectors for deployment of capital by AIFs.
- Renewable energy, though a theme loud in perception, investments have grown only meagre 2% since 31 March 2024.
- Real estate continues to be the prominent sector, driven by sector focused funds of major fund houses.




**Notable Budget Announcements : Government proposes**

- A new Fund of Funds (FoF) with a contribution of INR 10,000 crores.
- A deeptech FoF to function as a catalyst to the industry is proposed.
- An urban challenge fund with contribution of INR 1 lakh crores – providing focus towards urban infrastructure.

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# Tax Proposals : Deployment of Funds - Sectors Benefitting

- **Start-up incentive extended:** The startup incentive, available for start-ups registered till 31.03.2025 has been extended to 31.03.2030. This shall provide a further boost to the start-up ecosystem.

- **Consolidation / Re-organization of entities:** Businesses can carry forward losses for **eight years**. Previously, mergers and reorganizations reset this period for the successor entity. Effective April 1, 2025, the Union Budget removes this reset.

- **Encouraging businesses by**
  - Rationalisation of withholding tax provisions – particularly removing tax collection at source (TCS) for transactions involving goods.
  - Beneficial tax regime for non-residents providing services and technology in the electronics manufacturing sector.
  - Reduction in levies on capital goods for lithium-ion batteries, textiles, and solar PV cells.
  - Specific tax benefits to ship-leasing units, insurance offices, and treasury centers in the International Financial Services Centre (IFSC).

# Tax Proposals : GIFT City rising in Stature!

- **Tax-Neutral Fund Relocation:** Offshore AIFs, retail schemes & ETFs can relocate to IFSC without tax implications, ensuring seamless transition for global investors.
- **Extended Sunset Clause:** Tax incentives for AIF fund relocation extended to March 31, 2030, providing long-term regulatory clarity and stability.
- **Tax Exemption on Derivative Income:** Non-residents' income from derivative contracts with FPIs in IFSC is now tax-neutral, enhancing flexibility for AIF transactions.
- **Deemed Dividend Exemption:** Inter-group loans involving an IFSC-based Finance Company or Treasury Centre are exempt, benefiting structured AIF investments.

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# Thinking for the future

- **Expanding IFSCs Beyond GIFT City:** As India cements its role in global finance, expanding IFSCs beyond GIFT City could create a more distributed, resilient ecosystem—attracting diverse capital and enhancing competitiveness in cross-border financial services.

- **Taxation Clarity for Carry Interests, Secondaries & Category-III AIFs:** A clear, well-defined tax framework for carry interests, secondary transactions and Category-III AIFs is key to unlocking liquidity, reducing uncertainty, and positioning India as a more attractive investment destination. Hoping the new direct tax code provides the impetus.

- **Carryback Provisions for Losses:** Aligning Taxation with Fund Lifecycles - with AIFs realizing profits early and losses closer to winding up, introducing carryback provisions or tax credits could optimize capital efficiency and better reflect economic realities.

- **Indian AIFs as a Global Investment Powerhouse – Unlocking Capital Flows:** With Indians and their businesses expanding globally, a more flexible ODI framework for AIFs can strengthen India's role in international fund flows, and enhance its standing as a global financial hub.

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**Write to us for a detailed discussion:**

hemant@sdu.works I manojnair@sdu.works I vinay@sdu.works I vishnu@sdu.works

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**Bengaluru**
6th Floor, Trade Centre,
29/4, Race Course Road,
Bengaluru – 560 001

**Mumbai**
WeWork, Raheja Platinum, Sag Baug Road, off Andheri-Kurla Road, Marol, Andheri (East) Mumbai - 400059

91. 80. 22261371

## Thank you