

Background and Budget Proposal

The Securities Transaction Tax (STT) on transactions in specified securities was introduced through the Finance (No.2) Act, 2004. Under STT provisions, recognized stock exchanges, mutual funds (with equity-oriented schemes), insurance companies, or lead merchant bankers appointed for initial public offerings are responsible for collecting and remitting the tax on specified securities to the Central Government within seven days from the end of the month in which STT is collected. Since its inception in 2004, the STT rates have been periodically revised.

Currently, the STT rate on the sale of options in securities is 0.0625% of the option premium, while the rate on the sale of futures in securities is 0.0125% of the trading price of such futures. For delivery trades in equity shares, the STT rate is 0.1% on both purchase and sale transactions. In the case of exercised options, the purchaser pays 0.125% of the intrinsic price (the difference between the settlement price and the strike price).

The derivative markets (F&O markets) have experienced significant growth recently, constituting a substantial portion of trading on stock exchanges. In light of this growth, it is proposed to increase the STT rates on the sale of options in securities from 0.0625% to 0.1% of the option premium, and on the sale of futures in securities from 0.0125% to 0.02% of the trading price of such futures. This amendment is intended to take effect from October 1, 2024.

Impact

An increase in STT would increase government tax revenue but could potentially reduce market volumes and liquidity, thereby adversely affecting exchange revenues and SEBI's income. Additionally, it might deter retail investors, which aligns with the government's objective of curbing speculative activities in the F&O segment.

ELP's Insights

Recently, the RBI and SEBI have raised concerns regarding investor safety, highlighting that retail traders often incur losses in the F&O segment.

The proposed increase in STT on F&O trades can be viewed as a response to these concerns raised by the RBI and SEBI ahead of the budget.

This government initiative aims to boost tax revenue and discourage retail investors from participating in F&O trading. However, historical data indicates that the introduction of STT has not had a detrimental impact on trading activity in this segment; in fact, turnover in the F&O segment has shown significant growth. It remains to be seen whether the proposed increase will indeed dissuade retail investors from engaging in trading within this segment.