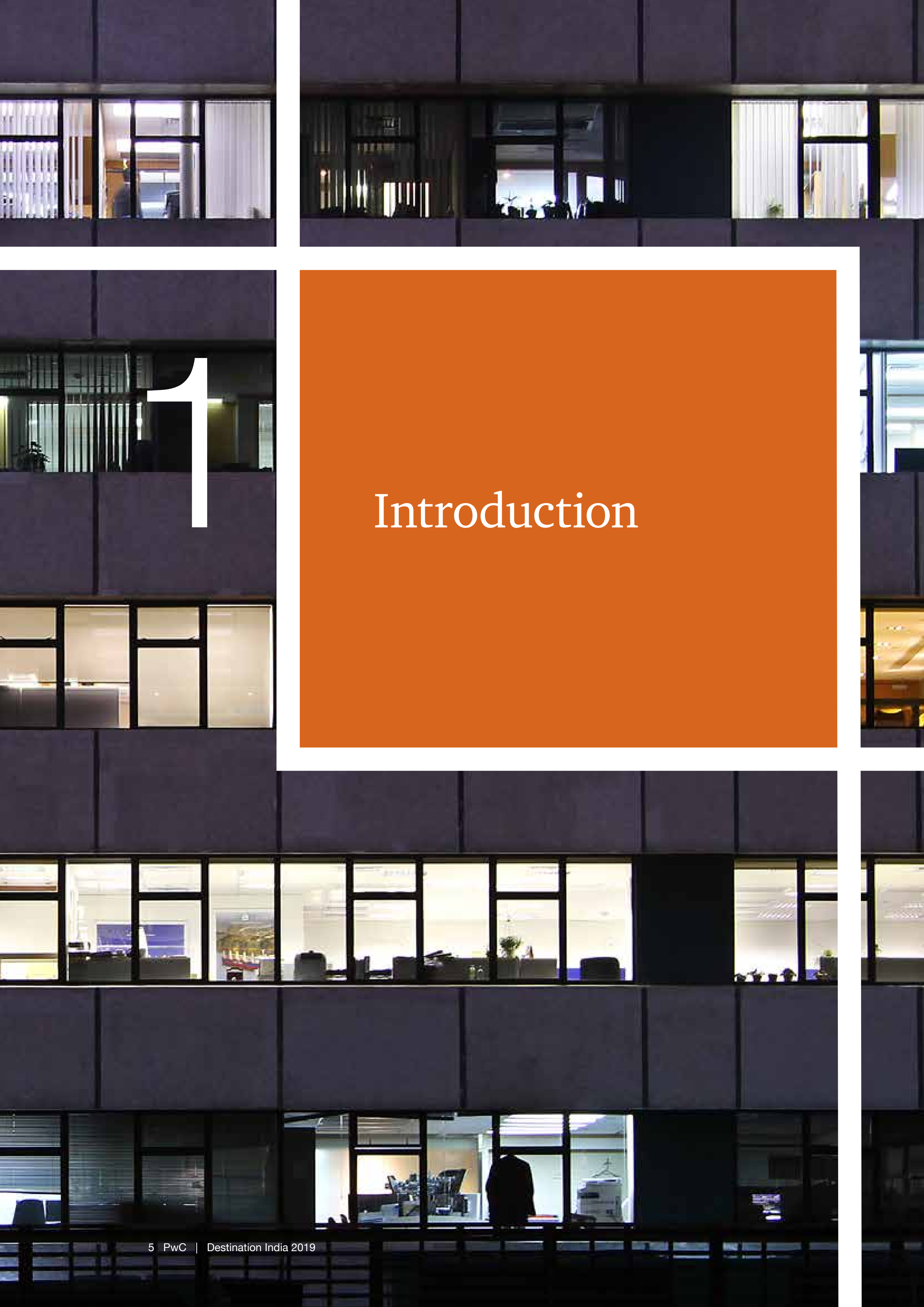
Destination India

2019

Contents



1 Introduction

Standing tall

After the emphatic victory of the Prime Minister Narendra Modi-led NDA Government in the Indian general elections, it is natural to expect that the Government will embark on bold measures and reforms for fostering growth. India is the seventh-largest economy in terms of GDP and aims to grow into a USD 5-trillion economy by 2024-25, which will make it the third-largest economy in the world.[1]

The latest indicators from various authorities continue to place India on a relatively high growth trajectory:

***IMF*[2]**

Country/region	Expected GDP growth rate (per cent)					
	2019	2020	2021	2022	2023	2024
India	7.257	7.489	7.74	7.731	7.742	7.737
China	6.267	6.119	6	5.75	5.6	5.5
United States	2.331	1.871	1.766	1.64	1.615	1.565
European Union	1.825	1.279	1.548	1.480	1.440	1.390

***World Bank*[3]**

Country/region	Expected GDP growth rate (per cent)		
	2019	2020	2021
India	7.5	7.5	7.5
China	6.2	6.2	6.0
United States	2.5	1.7	1.6
European Union	1.6	1.5	1.3

The Indian economy is classified into three sectors: Agriculture and allied segments, Industry and Services.

The Agriculture sector includes Agriculture (agriculture proper and livestock), Forestry and Logging, and Fishing and Related Activities.

Industry includes Mining and Quarrying; Manufacturing (registered and unregistered); Electricity, Gas, Water Supply and Other Utility Services; and Construction.

The Services sector includes Trade, Hotels, Transport, Communication and Services Related to Broadcasting; Financial, Real Estate and Professional Services; Public Administration and Defence and Other Services.

The Services sector is the largest segment in India. The Gross Value Added (GVA) at current prices for the sector was estimated at INR 93.39 lakh crore in 2018-19. It accounts for 54.30% of India's total GVA of INR 172 lakh crore.

With a GVA of INR 50.85 lakh crore, the Industry sector contributes 29.56% to the economy, while the Agriculture and allied segments contribute 16.14% with a GVA of around INR 27.76 lakh crore.

At basic prices, the sectors which registered a growth rate of over 7.0% are Public Administration, Defence and Other Services at 8.6%; Construction at 8.7%; Financial, Real Estate and Professional Services at 7.4%; and Electricity, Gas, Water Supply and Other Utility Services at 7.0%. The growth in Agriculture, Forestry and Fishing; Mining and Quarrying; Manufacturing; and Trade, Hotels, Transport, Communication and Services Related to Broadcasting is estimated to be 2.9%, 1.3%, 6.9% and 6.9% respectively.

At current prices, all sectors except Agriculture - that is, Mining and Quarrying; Manufacturing; Electricity, Gas, Water Supply and Other Utility Services; Construction; Trade, Hotels, Transport, Communication and Services Related to Broadcasting; Financial, Real Estate and Professional Services; and Public Administration, Defence and Other Services have registered a growth rate of over 9.0%.[4]

1. https://www.indiabudget.gov.in/economicsurvey/
2. https://www.imf.org/external/pubs/ft/weo/2019/01/weodata/weoselgr.aspx
3. http://www.worldbank.org/en/publication/global-economic-prospects
4. http://www.pib.nic.in/Pressreleaseshare.aspx?PRID=1572945

The following are some of the key developments over the past 12 months which account for India's growth:

FDI reforms

Foreign Direct Investment (FDI) is a major driver of economic growth and a source of non-debt finance for economic development in India. The Government has put in place an investor-friendly policy, under which FDI up to 100% is permitted through the automatic route in most sectors and activities.

In the recent past, the Government has implemented reforms in its FDI policy in a number of segments. The measures it has undertaken have resulted in increased FDI inflows into the country. During FY 2014-15, total FDI inflows into India amounted to USD 45.15 billion as against USD 36.05 billion in FY 2013-14. In FY 2015-16 and FY 2016-17, India received total FDI of USD 55.56 billion and USD 60.22 billion respectively. During FY 2017-18 and FY 2018-19, India's FDI inflows remained strong at USD 60.97 billion and USD 64.37 billion respectively.[5] India represents the most attractive markets.[6]

The following are some of the key initiatives taken by the Government[7] in the recent past:

- The Government released the Draft National e-Commerce Policy in relation to FDI in the marketplace model of e-commerce.
- The Government has proposed 100% FDI for insurance intermediaries.
- The Government released the National Digital Communications Policy, 2018, which aims to attract FDI inflows of USD 100 billion by 2022 in the Telecommunications sector.
- The Government clarified that Real Estate Broking Services would be eligible for 100% FDI under the automatic route.
- The Government allowed 100% FDI under the automatic route for single brand retail trading and is planning to ease local sourcing norms.
- The Government has proposed to further open up FDI in the Aviation, Media and Insurance sectors.
- The Government has proposed to increase the statutory limit for Foreign Portfolio Investor (FPI) investment in a company from 24% to the sectoral foreign investment limit with an option for concerned corporates to limit it to a lower threshold.
- The Government has proposed to permit FPIs to subscribe to listed debt securities issued by Real Estate Investment Trusts (ReITs) and Infrastructure Investment Trusts (InvITs).

Ease of doing business[8]

India has recorded a jump of 23 positions on its rank of 100 in 2017 and now ranks 77th among 190 countries assessed by the World Bank. India's leap of 23 ranks on the Ease of Doing Business ranking is significant considering that it had improved its rank by 30 places last year, a rare feat for any large and diverse country of India's size. As a result of continued efforts by the Government, India has improved its rank by 53 positions in the last two years and 65 positions in the last four years.

The highlights of India's performance in 2018 are:

- The World Bank has recognised India as one of the top improvers for the year.
- This is the second consecutive year in which India has been recognised as one of the top improvers.
- India is the first BRICS and South Asian country to be recognised as a top improver for two consecutive years.
- Since 2011, India has recorded the highest improvement in two years by any large country in the doing business assessment, having climbed 53 positions.
- As a result of its continued positive performance, India now holds the top spot among South Asian countries as against the 6th position in 2014.

5. https://dipp.gov.in/sites/default/files/FDI_Factsheet_27May2019.pdf
6. As per 2019 Emerging Markets Private Equity Association's Global Limited Partners Survey
7. https://www.ibef.org/economy/foreign-direct-investment.aspx and https://www.indiabudget.gov.in/budgetspeech.php
8. http://pib.nic.in/newsite/PrintRelease.aspx?relid=184513

Start-up India, Stand-up India[9]

Start-ups drive economic growth, create employment and foster a culture of innovation. As on 1 March 2019, 16,578 new start-ups were recognised across 490 districts. The Government has taken steps to ease regulations for start-ups such as exemption from income tax on investments raised by start-ups, implementation of 22 regulatory reforms to improve Ease of Doing Business for start-ups, introduction of a self-certification regime for six labour laws and three environmental laws and launch of the Start-up India Hub as a 'one stop shop' for the start-up ecosystem.

Healthcare[10]

The Government aims to develop India as a global healthcare hub. Some of the initiatives it has undertaken are:

- The world's largest government-funded healthcare scheme, Ayushman Bharat, targeted at more than 500 million beneficiaries, was launched on 23 September 2018.
- As of January 2019, around 9,00,000 patients received benefits worth INR 1,210 crore (USD 167.71 million) under the Pradhan Mantri Jan Arogya Yojana.
- The Government has allocated INR 85,217 crore (USD 13.16 billion) for the National Nutrition Mission which aims to monitor, supervise, fix targets and guide nutrition-related interventions across ministries. In May 2018, the Government signed a USD 200-million deal with the World Bank for 315 districts across India under the National Nutrition Mission.
- A solidarity human chain was formed by the Government in partnership with the World Health Organization on 4 April 2019.
- The Government has approved the continuation of the National Health Mission with a budget of INR 31,745 crore (USD 4.40 billion) under Interim Budget 2019-20.

9. https://www.indiabudget.gov.in/economicsurvey/
10. https://www.ibef.org/download/healthcare-may-2019.pdf

Infrastructure[11]

The Infrastructure sector has become one of the largest focus areas of the Government. The Government plans to invest INR 100 lakh crores in infrastructure over the next 5 years and aims to ensure power connectivity through 'One Nation, One Grid'. Some key developments in the sector are listed below:

- During January-December 2018, the Infrastructure sector witnessed 12 private equity and venture capital deals worth USD 500 million and eight USD 1 billion plus deals.
- India improved its ranking on the Energy Transition Index published by the World Economic Forum.
- Electricity generation in the country increased by 3.77% during April-February 2018-19.
- 2018-19 was declared as the 'Year of Construction' as road construction in km grew @ 30 km per day in 2018-19 as compared to 12 km per day in 2014-15.
- In June 2018, the Asian Infrastructure Investment Bank (AIIB) has announced an investment of USD 200 million in the National Investment & Infrastructure Fund (NIIF).
- The Government has given a massive push to all forms of physical connectivity through Pradhan Mantri Gram Sadak Yojana, industrial corridors, dedicated freight corridors, Bhartamala and Sagarmala projects, and the Jal Marg Vikas and Ude Desh Ka Aam Nagrik (UDAN) schemes.

With the aim of enhancing the sources of capital for infrastructure financing, the following measures have been proposed by the Government in Budget 2019:

- A Credit Guarantee Enhancement Corporation to be set up in 2019-20.
- An action plan to be put in place to deepen the market for long-term bonds, including for deepening markets for corporate bond repos and credit default swaps, with a specific focus on the Infrastructure sector.
- It is proposed to permit investments made by Foreign Institutional Investors/FPIs in debt securities issued by Infrastructure Debt Fund-Non-Bank Finance Companies (IDF-NBFCs) to be transferred/sold to any domestic investor within the specified lock-in period.

11. https://www.ibef.org/industry/infrastructure-presentation and https://www.indiabudget.gov.in/economicsurvey/ and https://www.indiabudget.gov.in/budgetspeech.php

Resolution of insolvency

The Insolvency and Bankruptcy Code is considered one of the most important economic reforms in recent times. The code provides flexibility to financial and operational creditors and enables them to initiate insolvency-resolution procedures against companies that have defaulted on payments of INR 1 lakh or more to repay the legitimate dues of financial or operational creditors. The entire process is altogether different from that prescribed by the erstwhile legislation, the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA).

The new law makes a commitment to deal swiftly with failing companies, removing the owners and blocking them from trying to buy back businesses out of bankruptcy. Its architects have set a nine-month limit for the completion of the entire process. This makes it one of the world's fastest bankruptcy regimes on paper, and strikes a marked contrast with the sluggish pace of other Indian legal processes. This process enables firms to remain in business as long as they are competitive and makes place for new entrants when they lose their competiveness.

Until 31 March 2019, 1,858 cases were admitted for resolution of issues by the National Company Law Tribunal. Of these, 152 have been closed on appeal or review or settled, 91 have been withdrawn, 378 have ended in liquidation, 1,143 are undergoing the resolution process and 94 have ended in approval of resolution plans.[12] For this set of 94 cases, out of the total claims worth INR 1,73,359 crore of financial creditors admitted, claims worth INR 74,497 crore have been resolved. This accounts for nearly 43% recovery.[13]

The Hon'ble Supreme Court, vide its order dated 2 April 2019, has held the RBI circular dated 12 February 2018 on resolution of stressed assets as ultra vires. The Reserve Bank has issued a new framework for resolution of stressed assets by banks in the wake of the Supreme Court's judgement.[14] While the old framework required lenders to initiate steps to cure a default as soon as one occurred and mandated initiation of recovery proceedings on account of failure to implement a resolution plan, the new framework provides for a review period of 30 days within which the lenders may decide on the resolution strategy, including the nature of the resolution plan, the approach for implementation of the resolution plan, etc. The lenders may also choose to initiate legal proceedings for insolvency or recovery.

Due to the concerted effort made with the enactment and implementation of the Insolvency and Bankruptcy Code (IBC), India improved its 'Resolving Insolvency' ranking from 134 in 2014 to 108 in 2019. This is a significant jump given that the country had a low ranking for many years. Moreover, India won the Global Restructuring Review award for the most improved jurisdiction in 2018.[15]

The Government stands committed to maintaining and enhancing the momentum of resolution of stressed assets and adherence to credit discipline.[16]

Recapitalisation of banks

In October 2017, the Government announced a major recapitalisation drive to the tune of INR 2.11 lakh crore by utilising three channels – the Budget, market borrowings and issue of recapitalisation bonds. After the recapitalisation announcement, INR 0.88 lakh crore was infused by the Government in banks during FY 2017-18,[17] and the Government infused INR 1.06 lakh crore during FY 2018-19, up from budget estimates of INR 0.65 lakh crore.[18]

The Government is ceaselessly working towards a comprehensive clean-up of the banking system under its 4R approach of Recognition, Resolution, Recapitalisation and Reforms, thereby rejuvenating the Banking sector and helping banks extend fresh credit as well as sort out the stressed asset problem to some extent. At the same time, recapitalisation is not indiscriminate and banks have to commit themselves to implementing performance improvement measures by signing a memorandum of understanding with the Government.

12. https://www.ibbi.gov.in/uploads/publication/NewsLeter%20Jan-%20March.,%202019.pdf
13. https://www.indiabudget.gov.in/economicsurvey/
14. https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx-?prid=47248
15. https://www.indiabudget.gov.in/economicsurvey/
16. https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx-?prid=47248
17. http://pib.nic.in/newsite/PrintRelease.aspx?relid=186589
18. https://www.livemint.com/news/

Digital governance

In Budget 2018, the then Finance Minister announced a host of technology-driven projects in areas such as budgeting, depositing of fees and penalties. The Government has started implementation of these e-Governance projects to make its functions more transparent and efficient, and ease citizens' interactions with it. The following are some of the highlights of the initiative:[19]

- Draft discussion paper on the National Strategy for Artificial Intelligence issued in June 2018. The Government is now working on implementing this strategy.
- In December 2018, the Government approved the National Mission on Interdisciplinary Cyber-Physical Systems (NMICPS) at a total outlay of INR 3,660 crore for a period of five years. The mission will enable the Central Ministries/ Departments, State Governments as well as industry to effectively use cyber-physical technologies in their projects and schemes for the benefit of society.
- The Department of Telecommunications approved a financial grant for a multi-institute collaborative project to set up end-to-end 'Indigenous 5G Test Bed' in India at a total cost of INR 224 crore over a period of 36 months. The eight collaborating institutes in the project are the Centre of Excellence in Wireless Technology, IIT Bombay, IIT Delhi, IIT Hyderabad, IIT Madras, IIT Kanpur, IISc Bangalore and the Society for Applied Microwave Electronics Engineering & Research.
- In order to promote blockchain technology in India, a distributed inter-institutional Centre for Excellence in blockchain technology is being set up by the Government with premier academic institutes, Government organisations and R&D institutes.
- Income tax e-assessments has been initiated by the Government.

The UN E-Government Survey 2018 (July 018) has ranked India at the 96th position for its development and execution of information technology**,** up from 107 in 2016 and 118 in 2014 – a significant leap!

Science and technology[20]

India ranks third among the most attractive investment destinations for technology transactions in the world. Technology is a strong priority area for the Government. India is among the leading countries in the world in the field of scientific research and one of the top five nations in the field of space exploration. India has repeatedly undertaken space missions, including missions to the moon and the famed Polar Satellite Launch Vehicle.

In FY18, India ranked 6th in the world in terms of scientific publications and 10th in terms of patents (only resident applications). The number of patent applications filed by Indian scientists and inventors increased to 47,857 in FY18 from 46,904 in FY16. India ranked 13th on the Nature Index in 2018, based on the volume of high-quality research output in the natural sciences. The country also improved its rank on the Global Innovation Index 2019, moving from the 81st position in 2015 to the

19. https://www.indiabudget.gov.in/ub2019-20/impbud/impbud.pdf
20. https://www.ibef.org/industry/science-and-technology.aspx, https://www.natureindex.com/annual-tables/2019/country/all and https://www.globalinnovationindex.org/gii-2019-report#

52nd position. The Government is extensively promoting research parks (RPs) and technology business incubators (TBIs) which would promote innovative ideas till they become commercial ventures. India is the world's third largest technology start-up hub with 1,000 new companies having been incorporated in 2017.

Following are some of the initiatives taken by the Government in the recent past:

- In February 2018, the Union Cabinet approved the implementation of the Prime Minister Research Fellows (PMRF) scheme, a mission for development through innovation at a total cost of INR 1,650 crore (USD 245.94 million) for a period of seven years beginning 2018-19.
- In February 2018, the Government announced a grant of INR 1,000 crore (USD 155.55 million) for the second phase of Impacting Research Innovation and Technology (IMPRINT).
- The Government granted USD 24.84 million to the Atal Innovation Mission, which will help boost innovation among academicians, entrepreneurs and researchers. In July 2018, the 'Innovate India Platform' was launched with the aim of providing a common point for all innovation happening across India.

Macroeconomic review[21]

India's GDP at current prices in Q4 of 2018-19 is estimated at INR 50.16 lakh crore as against INR 45.85 lakh crore in Q4 of 2017-18, showing a growth of 9.4%. The GVA at current basic prices in Q4 of 2018-19 is estimated at INR 44.02 lakh crore as against INR 40.20 lakh crore in Q4 of 2017-18, showing a growth of 9.5%.

The growth rates in various sectors are as follows: Agriculture, Forestry and Fishing at 3.8%; Mining and Quarrying at 9.7%; Manufacturing at 5.7%; Electricity, Gas, Water Supply and Other Utility Services at 8.8%; Construction at 10.3%; Trade, Hotels, Transport and Communication at 9.3%; Financial, Real Estate and Professional Services at 13.3%; and Public Administration, Defence and Other Services at 16.3%.

Key takeaways

The strength of the Indian economy lies in its ability to continue on its path of robust and broad-based growth. Despite global headwinds and economic challenges related to policy development and continuity, the Government's pro-market efforts such as steps for creating an investor-friendly business environment, rationalisation of FDI limits and measures for resolution of stressed assets will culminate in India becoming a destination of choice for investors.

21. http://www.mospi.gov.in/sites/default/files/press_release/Press%20Note%20PE%202018-19-31.5.2019-Final.pdf

2 Corporate Tax

'Transparency', 'lower rates' and 'base erosion' are buzzwords that are resonating in the international tax environment. India has kept up with global trends by introducing sunset clauses in its complex exemption-related rules and deductions in its domestic tax laws. In line with these changes, it has reduced its Corporate Tax rate to 25% for certain eligible companies. In the past few years, India has also introduced certain measures unilaterally, in line with BEPS recommendations, in its domestic tax law to counter base erosion. India has also recently ratified the Multilateral Instrument. The last few years have seen the country's tax administration transitioning to the electronic platform and initiatives being taken to simplify the compliance process for taxpayers, to help them resolve issues with minimum human interaction.

The Government of India enacted the Income Tax Act, 1961 (the IT Act) for levy of Income Tax in India. The Income Tax Rules, 1962 (IT Rules) lay down the procedures to be followed in compliance with the provisions of the IT Act. These rules are administered by the Central Board of Direct Taxes (CBDT), which operates under the Central Finance Ministry.

Tax year and tax return filing

The tax year in India starts from 1 April of one year and ends on 31 March of the subsequent year. Companies are required to file their return of income in India for a particular year as per the due dates set out below:

Nature of company	Deadline to file return of income
Companies that are required to submit a Transfer Pricing accountant's report in Form 3CEB	30 November of the subsequent tax year
Other companies/Limited Liability Partnerships (LLPs)	30 September of the subsequent tax year

Non-resident taxpayers need to file their tax returns in India, even if applicable taxes are withheld from their receipts or income. However, they are not required to file returns of income if their total income includes certain specified categories of income, and taxes have been withheld therefrom at the appropriate rates.

Companies are required to estimate and discharge their tax liability on a quarterly basis by way of Advance Tax. Late filing of return of income, delay in payment and/or shortfall in payment in taxes may attract interest, fines and penalty as well as prosecution proceedings.

Indian companies are mandatorily required to obtain a tax registration number, known as the Permanent Account Number (PAN). A non-resident taxpayer needs to obtain a PAN if its income is taxable in India.

Scope of taxable income of a company

A company that is resident in India (resident company) is taxed on its global income in the country. A company that is resident outside India (non-resident company) is taxed in India in respect of:

- Income that accrues or arises in India
- Income that accrues to the non-resident company from a 'business connection' in India, an asset or source of income in the country (interest, royalties or fees for technical services), or by transfer of a capital asset in the country
- Income received or deemed to have been received in India

The IT Act uses the term 'business connection' to tax business profits instead of Permanent Establishment (PE), used in tax treaties. The term business connection is considered wider in scope than PE. The term business connection includes business activities conducted by agents on behalf of non-residents who habitually conclude contracts in India or play a principal role in

their conclusion in the country. The IT Act prescribes that only income that is reasonably attributable to such activity carried out in India will be taxed in the country.

The term business connection also includes the concept of a significant economic presence (SEP). SEP is defined as (a) a transaction carried out by a non-resident in India in respect of goods, services or property and includes provision for downloading of data or software in India, and (b) systematic and continuous soliciting of business activities or interaction with the prescribed number of users in India through digital means. SEP-related thresholds or monetary limits for transactions (involving goods, services or property) and the number of users are yet to be prescribed by the Central Board of Direct Taxes (CBDT).

Residential status of a company

A company is considered a resident of India if it is incorporated in or its Place of Effective Management (PoEM) is in India. PoEM means a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are made in substance. Thus, the global income of a company will be taxed in India if its PoEM is in the country.

Residential status of other forms of corporate entities

Various forms of corporate entities are permitted in India and operate in the country. These include partnership firms and LLPs. An entity, other than a company, is considered a resident in India if control and management of its affairs or any portion or part thereof is located in India during the year.

Corporate Tax rates

Corporate Tax rates for entities range from 25% to 40%. The tax rate is increased by a surcharge, which varies depending on the quantum of the income and nature of the entity. There is an additional levy of health and education cess at the rate of 4% on the tax amount and surcharge, if applicable.

Tax rates for a company and partnership firm or LLP

Status of entity	Rates in force	Conditions
Domestic company	25%*	Total turnover/Gross receipts in financial year (2017-18) not exceeding INR 4 billion
	30%	All other companies
Foreign company	40%	All foreign companies
Partnership firm/LLP	30%	All firms and LLPs

*A reduced tax rate of 25% is also available to domestic companies (subject to fulfilment of certain specified conditions) set up after 1 March 2016, which are engaged in manufacturing products and are not claiming certain specified deductions in computation of their taxable profits.

Surcharge

(*Amount in INR*)

Taxable income	Income from INR 10 million to INR 100 million	Income above INR 100 million
Domestic company	7%	12%
Foreign company	2%	5%
Partnership firm/LLP	12%	12%

Minimum Alternate Tax (MAT)

MAT is levied at the rate of 18.5% (plus applicable surcharge and cess) on the adjusted book profits of companies if their MAT liability exceeds the corporate tax payable under normal provisions of the IT Act. Credit for MAT is allowed to be carried forward for 15 years and can be set off to the extent of the difference between the tax computed as per the normal provisions and the adjusted book profits. MAT provisions are not applicable for (a) foreign taxpayers that do not have PEs in India (where a tax treaty exists between India and the country of residence of the foreign company) or (b) foreign taxpayers that are not required to seek registration under any law in force relating to companies (where a tax treaty does not exist).

Alternate Minimum Tax (AMT)

AMT is levied on entities other than companies at the rate of 18.5% on their adjusted total income (computed in accordance with the provisions of the IT Act) if the AMT liability exceeds the tax payable under the normal provisions of the IT Act. Credit for AMT is allowed to be carried forward for 15 years and can be set off to the extent of the difference between the tax computed as per the normal provisions and the adjusted total income.

Dividend Distribution Tax (DDT)

Indian companies are required to pay DDT at the rate of 15% (effective rate of 20.56 %[22]) when they distribute, declare or pay dividends. DDT is payable on declaration, distribution or payment, whichever is earlier, and is levied in addition to the Corporate Tax payable on business profits. DDT provisions are not applicable for an LLP.

Dividends received by an Indian company from a foreign one are taxed at the rate of 15%, where the recipient Indian company holds 26% or more of the nominal value of the equity share capital in the foreign one.

Dividends received from Indian companies that are subject to DDT are not taxable in the hands of the recipients. However, in the case of individuals, Hindu Undivided Families (HUFs) or companies that are residents in India, tax is levied at the rate of 10% on dividends received in excess of INR 1 million during a tax year, even if DDT has been paid.

Buyback of shares

When a domestic company buys back shares from its shareholders, it is required to pay an additional tax of 20% (at the effective rate of 23.30%[23]) on the difference between the consideration paid by it for the buy-back and the issue price of the shares. The shareholder is exempted from tax in India on the buyback amount received.

Key considerations

Computation of income

A company's taxable income is divided into the following categories or heads of income:

- Profits and gains from business or profession
- Income from house property
- Capital gains
- Income from other sources

Income from profits and gains of business or profession

Books of accounts and tax audit

A taxpayer conducting business or a profession is required to maintain books of accounts if the total sales, turnover or gross receipts from the business exceeds INR 1 million. Furthermore, a taxpayer needs to have such books of accounts audited if the total sales, turnover or gross receipts from its business exceeds INR 10 million.

Income Computation and Disclosure Standards (ICDS)

Taxpayers that follow the mercantile system of accounting are required to compute their chargeable income under the heads 'profits and gains of business or profession' and 'income from other sources' in accordance with ICDS.

Depreciation

Taxpayers are allowed depreciation on the written down value (WDV) of assets. Depreciation rates generally range from 10% to 40%. In the case of a taxpayer engaged in manufacturing or production, an incentive by way of additional depreciation at the rate of 20% is provided on the value of new plants and machinery in the year of their installation. The additional rate may increase to 35% if certain additional conditions are satisfied.

22. Inclusive of highest applicable surcharge rate and health and education cess
23. Inclusive of highest applicable surcharge rate and health and education cess

Some tax deductions and incentives available for taxpayers

Activity	Benefits*
Deduction for employment of new employees: All taxpayers, whose total sales, turnover or gross receipts exceed INR 10 million	Additional deduction of 30% of employee cost incurred on new employees
Scientific R&D	Weighted deduction of 150% of the expenditure
Units set up in SEZs	100% tax holiday for five years; 50% for the next five years and 50% (subject to certain additional conditions) for the next five years out of profits from export of goods and services
Deduction for specified business categories such as cold chain facilities, warehousing facilities for storage of agricultural produce, cross-country natural gas oil or distribution and infrastructure-related facilities.	100% deduction for capital expenditure
Undertaking engaged in the business of processing, preservation and packaging of fruits or vegetables, meat and meat products, poultry or marine and dairy products; handling, storage and transportation of food grains	100% tax holiday for the first five years and a deduction of 30% (25% if the assessee is not a company) of its profits for the subsequent five years
Expenditure on skill development project	Weighted deduction of 150% on expenditure incurred on a notified skill development project by a company
Start-up businesses (company or LLP) engaged in innovation, development or improvement of products, processes, services or a scalable business model with a high potential for employment generation or wealth creation	100% deduction for profits and gains for three consecutive years out of seven years beginning from the year the start-up was incorporated

** Subject to specified conditions*

Presumptive taxation regime for non-residents

Non-resident taxpayers conducting certain businesses can offer their income to tax in India on a presumptive basis. In such cases, their taxable income is determined on the basis of a certain percentage of their total gross receipts. This is expected to reduce areas of uncertainty and compliance-related requirements, since such taxpayers are not required to maintain books of account and get these audited.

Particulars	Shipping	Aircraft	Oil and gas services	Turnkey power projects
Applicability	Shipping operations	Aircraft operations	Specified business activity relating to prospecting for, extraction of or production of mineral oils	Specified business activity in relation to approved turnkey power projects
Presumptive rate	7.5% of gross receipts from carriage of passengers, livestock, mail or goods	5% of gross receipts from carriage of passengers, livestock, mail or goods	10% of gross receipts from such business	10% of gross receipts from such business
Option of showing income that is lower than the presumptive rate	Not available	Not available	Available, provided taxpayer maintains books of account and gets these audited	Available, provided taxpayer maintains books of account and gets these audited

MAT provisions (discussed above) are not applicable for non-resident taxpayers that offer and compute their taxable income on a presumptive basis.

Losses incurred from business

Losses from business under the head of Profits and Gains of Business or Profession (PGBP) are classified into business losses and unabsorbed depreciation. Business losses for a particular tax year can be set off against income taxable under other heads of income (except 'Salary') earned during the same tax year. Business losses that cannot be set off due to insufficient income under other heads of income can be carried forward for eight subsequent tax years, but can only be set off against business income (under the head PGBP) earned in eight subsequent years. Unabsorbed depreciation can be carried forward indefinitely and be set off against taxable income under any head in subsequent years.

In the case of closely held entities, 51% of their beneficial shareholding needs to be maintained in order to carry forward business losses. Closely held eligible start-up companies have the option of satisfying either of the following two conditions in order to carry forward their business losses (incurred during the period of seven years beginning from the year in which the start-up is incorporated) by (a) maintaining 51% of beneficial shareholding or (b) the continuity of all the shareholders holding shares carrying voting power, irrespective of their percentage of shareholding.

In India, there are no provisions under the IT Act for carrying losses back to earlier years.

Income from capital gains

Income earned from transfer of capital assets is taxed under the head 'capital gains'. Capital assets are broadly defined in the IT Act to cover any property, whether it is connected to a business or a profession, as well as securities held by Foreign Institutional Investors (FIIs), which has been invested in accordance with security-related regulations in India. However, a capital asset does not include the personal effects of taxpayers for their personal use.

The IT Act exempts Capital Gains Tax in certain cases where the consideration amount or capital gains is reinvested in specified assets. Furthermore, the IT Act does not consider certain transactions as 'transfers', and accordingly, exempts these from Capital Gains Tax (subject to satisfaction of prescribed conditions).

Tax rates applicable on capital gains vary, depending on the duration the capital assets, i.e. short-term capital gains and long-term capital gains, are held. Long-term capital gains are generally taxed at reduced rates.

S. no.	Type of asset	Holding period	Classification of gains
1	Listed securities, units of Unit Trust of India, units of equity-oriented mutual funds and zero-coupon bonds	More than 12 months	Long-term capital gains
		Less than 12 months	Short-term capital gains
2	Unlisted securities	More than 24 months	Long-term capital gains
		Less than 24 months	Short-term capital gains
3	Immovable properties	More than 24 months	Long-term capital gains
		Less than 24 months	Short-term capital gains
4	Capital assets other than those specified in s. nos. 1, 2 and 3	More than 36 months	Long-term capital gains
		Less than 36 months	Short-term capital gains

Indirect transfer of shares

As per the IT Act, the shares of a non-resident entity are deemed to be situated in India if they substantially derive their value (whether directly or indirectly) from assets located in the country. 'Substantially' means, if, on a specified date, the Fair Market Value (FMV) of assets located in India exceeds INR 100 million and represents at least 50% of the value of all assets owned by the non-resident entity. Accordingly, transfer of such shares (i.e. of a non-resident entity) is considered transfer of a capital asset situated in India. The provisions of indirect transfers are subject to certain other prescribed conditions.

There are some jurisdictions that provide exemption from taxability of indirect transfer of shares by virtue of tax treaty provisions. A recent trend noticed in the Indian judiciary is that it gauges substance- and ownership-related requirements for meeting the eligible criteria provided in the tax treaties mentioned above.

Income from other sources

Income not covered under any of the specific heads of income is liable to tax under the head of 'income from other sources'. While computing taxable income from other sources, expenditure incurred wholly and exclusively for earning this income is allowed as a deduction.

Gift Tax

There is currently no distinct enactment for levying Gift Tax in India. However, certain specified transactions can be taxed in the hands of recipients as gifts under the IT Act. The relevant section provides that money or property, including shares, received without consideration or for inadequate consideration in excess of INR 50,000, is taxable in the hands of the recipients under the head 'Income from other sources'.

Premium on allotment of shares

Amounts received by closely held companies from Indian residents for issue of shares are taxable under the head 'Income from other sources', if such amounts are in excess of the FMV of the shares. Recently, the CBDT has issued a notification[24] exempting eligible start-ups from such provisions of the IT Act, subject to their complying with prescribed conditions and thresholds.

24. Notification No. 13/2019/F. No. 370142/5/2018-TPL (Pt.)

Other Corporate Tax-related considerations

Patent Box regime

In order to encourage indigenous Research & Development (R&D) and make India a global R&D hub, resident patentees' income from royalty from patents they have developed and registered in India are taxable at the rate of 10%. Under this regime, no expenditure or allowance is allowed as a deduction for computation of taxable income.

Withholding Tax (WT) provisions

Both resident and non-resident taxpayers making specified payments are obliged to withhold taxes according to the relevant provisions of the IT Act. Withholding Tax rates range from 0% to 40%, and in the case of payments made to non-residents, are increased by an additional surcharge, cess, etc., subject to benefits available under various tax treaties.

General Anti-Avoidance Rule (GAAR)

As per the GAAR provisions of the IT Act, the Indian tax authorities have been granted the power to declare an 'arrangement' entered by a taxpayer as an 'Impermissible Avoidance Arrangement' (IAA). Any step in or part of an arrangement entered may also be declared an IAA. GAAR provisions are applicable if the main purpose of the arrangement or step is to obtain a tax benefit. There are wide-ranging consequences, including denial of the tax benefit either under the provisions of the IT Act or the applicable tax treaty, if a transaction is declared an IAA. GAAR-related provisions do not apply if the tax benefit from an arrangement in a relevant tax year does not exceed INR 30 million. Furthermore, the CBDT has clarified that GAAR does not apply to investments made up to 31 March 2017.

Incentives for International Financial Services Centre (IFSC)

The following are some of the key tax concessions that are available in relation to IFSCs:

a) Exemption from capital gains tax on 'transfer' by a non-resident of the following securities listed on a recognised stock exchange located in an IFSC and where the consideration for such transaction is paid or payable in foreign currency:

- Bonds or global depository receipts
- Rupee-denominated bonds of an Indian company
- Derivatives
- Other securities, as may be notified by the Central Government

b) Tax exemption on income earned by Category III Alternative Investment Funds (AIFs) on transfer of specified securities on a recognised stock exchange in an IFSC, where the consideration is in convertible foreign exchange to the extent the income relates to units held by non-residents

c) Tax exemption on interest income earned by non-residents from units located in IFSCs in relation to monies borrowed by such units on or after 1 September 2019

d) 100% profit-linked tax deduction provided to units set up in IFSCs for any 10 consecutive years out of 15 years, beginning with the year in which the required permission for setting up a unit in an IFSC is obtained

e) Dividend distributed by a company, a unit located in an IFSC, which only derives its income in convertible foreign exchange that is exempt from DDT if the dividend is distributed or paid out of its current year's income (From 1 September 2019 onwards, exemption from DDT will also cover dividends distributed from income in convertible foreign exchange accumulated after 1 April 2017 by units located in IFSCs.)

f) Tax exemption for mutual funds (MFs) from Distribution Tax on the funds distributed to investors from income derived from transactions conducted on a recognised stock exchange located in an IFSC, where transactions are in convertible foreign exchange, if:

- The mutual fund is located in an IFSC.
- All the units of the mutual fund are held by non-residents.

Other considerations for taxation of non-residents

Multilateral Instrument (MLI)

The MLI seeks to help governments efficiently implement Base Erosion and Profit Sharing (BEPS)-related measures to eliminate double taxation, counter abuse of treaties and improve dispute-resolution mechanisms without the need to bilaterally renegotiate every tax treaty. India is among the 89 jurisdictions that have signed the MLI.

On 25 June 2019, India deposited its instrument of ratification with the nominated authority under the MLI with its final MLI positions. This means the date on which India's entry into the MLI will come into force is 1 October 2019.

In view of this, the MLI will take effect for any treaty signed by India from 1 April 2020 (FY2020-21) if:

1. India has listed the treaty in its final MLI position as a Covered Tax Agreement (CTA).
2. The treaty partner is a signatory to the MLI.
3. The treaty partner has deposited its instrument of ratification on or before 30 June 2019.
4. The treaty partner has listed India in its Final MLI Position as a CTA.

Accordingly, the MLI will come into effect on 1 April 2020 (FY 2020-21) for 21[25] treaties, based on India's position on 30 June 2019.

25. Australia, Austria, Belgium, Finland, France, Georgia, Ireland, Israel, Japan, Lithuania, Luxembourg, Malta, Netherlands, New Zealand, Poland, Serbia, Singapore, Slovak Republic, Slovenia, United Arab Emirates and the United Kingdom

Equalisation Levy – digital economy (e-Commerce transactions)

In line with BEPS Action Plan 1 (Digital Economy), India has introduced an Equalisation Levy at the rate of 6%, which is to be levied on payments made by a resident or the Indian PE of a non-resident to a non-resident service provider for provision of 'specified services'. A 'specified service' includes (a) an online advertisement or (b) provision for digital advertising space, or any other facility or service for the purpose of an online advertisement or (c) any other service notified by the Central Government.

Thin Capitalisation

Deduction for interest-related expenditure or similar payments made by Indian companies or the Indian PEs of foreign companies to foreign Associated Enterprises (AEs) in relation to borrowings or corporate guarantees is restricted to 30% of their earnings before Interest, Taxes, Depreciation and Amortisation (EBITDA) in certain cases. Excess interest that is disallowed in a year can be carried forward up to eight subsequent consecutive years.

Foreign Tax Credit (FTC)

The Indian Government has entered tax treaties with several countries to provide taxpayers earning an income that is taxable in multiple countries relief from the hardship of being subject to double taxation. In the absence of a tax treaty with a particular country, resident companies can claim FTC for tax paid in a foreign country, subject to certain fulfilment-related requirements. The CBDT has specified the rules and procedures by which an Indian resident can obtain benefit for the taxes paid by it in a foreign country, whether or not this is covered by a tax treaty.

Tax Residency Certificate (TRC)

To avail the benefits of an applicable tax treaty, non-resident taxpayers are required to provide a copy of the TRC issued to them by the revenue authorities of their home countries, along with certain other prescribed documents. The concessional tax rates applicable under certain tax treaties, which India has signed with various countries, are provided in PwC's Worldwide Tax Summary (please follow the link - http://taxsummaries.pwc.com/ID/India-Corporate-Withholding-taxes).

Recent developments in relation to Double Taxation Avoidance Agreements (DTAAs)

India has recently entered a tax treaty with Hong Kong, which has been effective from 1 April 2019.

It has amended its tax treaty with China (which came into force from 5 June 2019), wherein it has incorporated certain MLI-related proposals.

Tax litigation in India

Contentious tax-related issues

Determination of PE

In the recent past, the Supreme Court of India, India's highest judicial forum, has pronounced some rulings that enunciated various key principles for determination of PE in the country. In one ruling, the Court held that a fixed place PE can be constituted in India even if the duration of its presence will be less than six months. It needs to be seen whether this judgement will also be applicable in other cases. This will depend on the nature of the business a non-resident taxpayer conducts in India.

Draft report on profit attribution to PEs

In the recent past, the CBDT formed a committee to examine the existing scheme of profit attribution under Article 7 of the DTAAs, and based on this, to recommend changes in the existing Rule 10 of the IT Rules. The committee has released its draft report for public consultation.

The Committee has suggested a three-factor apportionment approach by assigning equal weightage (one third each) to sales, manpower (employees and wages) and assets. Furthermore, a fourth factor, 'users', has been suggested by the CBDT in respect to the concept of a Significant Economic Presence, whereby a weightage of 10% has been assigned for low or medium user intensity and 20% in other cases. In the SEP-related scenario, the weightage given to 'sales' will remain fixed at 30%. It should be noted that the CBDT has not followed the OECD's guidance on Functions, Assets and Risk (FAR) analysis, based on the rationale that this guidance only focuses on supply-side factors and ignores market- and demand-related factors.

The apportionment mentioned above will be applied to "profit derived from India operations", for which a methodology and formula have been provided. Even in a scenario where a foreign enterprise has international losses or its global profit margin is below 2%, a minimum of 2% of the turnover derived from India will be deemed to be its "profit derived from India operations". The draft report also provides for certain situations, where no attribution to the PE is required in India.

Royalty from software

There is considerable litigation in India regarding characterisation of amounts received for supply of software (including off-the-shelf software). Indian High Courts have divergent views on the issue of whether such consideration should be construed as royalty, and consequently, be taxable in India. The matter is now pending before the Supreme Court for final adjudication.

Offshore supply

Taxability of offshore supply is a vexing tax issue in India and assumes greater proportions when some onshore activities are also carried out in the country consequent to offshore supplies. Indian revenue authorities generally endeavour to attribute a portion of offshore supplies to India, and therefore, seek to bring consequent profits within the country's tax net.

Virtual presence/Digital economy

Today, multinational organisations are not confined by geographical boundaries to conduct their business operations. Sale of goods and services as well as payments are made digitally through servers based in foreign countries. Indian revenue authorities have taken an aggressive stand in capturing online transactions within the ambit of tax.

Appeal mechanism

The tax appellate mechanism in India can be split into the following four levels:

Appellate authority	Nature of appeal
Commissioner of Income-tax (Appeals) [CIT (A)]	First level of appeal: Taxpayers can approach the CIT(A) against audit orders passed by lower authorities (tax officers).
Dispute Resolution Panel (DRP)	Alternative to filing an appeal with the CIT(A): This option can be availed by non-resident companies and specified domestic taxpayers, who can file objections with the DRP against 'draft audit orders' passed by tax officers. The DRP, unlike the CIT(A), is required to issue directions within a prescribed time. Subsequently, the tax officer passes the final audit order on the basis of the directions of the DRP.
Income Tax Appellate Tribunal (ITAT)	Second level of appeal: Taxpayers or the Indian tax authorities can approach the ITAT against an order of the CIT (A) or a final order passed pursuant to the DRP's directions. The ITAT is the final fact-finding authority in India.
Jurisdictional High Court (HC)	Third level of appeal: Taxpayers or the Indian tax authorities can approach the jurisdictional HC against an order of the ITAT, provided the matter pertains to a substantial question of law.
Supreme Court (SC)	Last level of appeal: Taxpayers or the Indian tax authorities can approach the SC against an order of a jurisdictional HC. The SC's order is binding on both the taxpayer and the Revenue.

Alternative Dispute Resolution Mechanisms

Authority of Advance Rulings (AAR)

The AAR is an alternative dispute resolution forum that provides an opportunity to non-residents and certain residents to obtain certainty with respect to tax liabilities arising from transactions undertaken or to be undertaken by them. An order of the AAR is binding on the applicant as well as the Revenue, and can only be challenged under a writ jurisdiction before the jurisdictional High Court.

Income-tax Settlement Commission (ITSC)

The ITSC is another alternative dispute-resolution forum and constitutes a once-in-a-lifetime opportunity available to both residents and non-residents to seek resolution of their tax-related disputes. A taxpayer can file an application for a single year or multiple years. In order to file an application before the ITSC, taxpayers are required to provide 'full and true' disclosure of income they have not disclosed earlier, and pay additional Income-tax amounting to INR 1 million in advance. The ITSC has to dispose of proceedings within 18 months of an application and has the power to grant immunity from penalty and prosecution. An order of the ITSC is binding on both the applicant and the Revenue and can only be challenged under a writ a jurisdiction before a jurisdictional High Court.

3 Indirect Taxes

The Goods and Services Tax (GST), considered the biggest ever tax reform in Independent India, was implemented on 1 July 2017 and received overwhelming support from industry. The GST has brought in many changes in tax- and compliance-related requirements for various businesses because of which the acclimatisation phase during the rollover to the new regime was relatively long. The GST has afforded India Inc. an opportunity to simplify and create value for key business processes, including procurement, manufacturing, distribution and logistics.

India has a federal structure under which the authority to impose taxes has been distributed between the Central and state governments. This has made the Indian taxation system one of the most complex in the world.

The erstwhile Indirect Tax regime, which was applicable till 30 June 2017, had several shortcomings including the following, which resulted in an inefficient production and consumption structure, and thereby hindered economic growth:

- Multiplicity of taxes
- Tax cascading
- Divergent state-specific compliance-related requirements
- The need for interaction with multiple tax authorities at the Central and state levels
- No cross-utilisation of credits, inter se, goods and services imposed at the state level and the Central level, respectively
- Input Tax Credit (ITC) of certain taxes or duties such as CST, Octroi or Local Body Tax not being creditable.
- Onerous compliance-related procedures

The GST seeks to address and eliminate the shortcomings mentioned above. It has opted for a dual GST model that is in line with the Canadian GST. By adopting this model, the Central and state governments have been empowered to levy the GST on supply of goods and services. The GST is a consumption-based tax. Consequently, revenue for a transaction accrues, based on rules of the consumption or destination state, unlike under the past Indirect Tax regime, wherein revenue only accrued to the supplying state.

The following are some of the key concepts of the GST, which companies looking at investing in India should take into consideration:

A. Taxes applicable under the GST include the following:

Tax type	Levied on	Levied by
Central Goods and Services Tax (CGST)	Intra-state (within the state) supply of goods and services	Central Government
State Goods and Services Tax (SGST)*	Intra-state (within the state) supply of goods and services	State governments
Union Territory Goods and Services Tax (UTGST)*	Supply of goods and services in a Union Territory	Central Government
Integrated Goods and Services Tax (IGST)	- Inter-state supply of goods and services - Import of goods and services - Supplies to units and developers of Special Economic Zones (SEZs)	Central Government

** Levy of SCGST and UTGST is mutually exclusive.*

B. Registration under the GST: A supplier of goods and/or services is required to obtain GST registration in every state from which it supplies goods and/or services. GST registration is not required if the turnover of a supplier dealing in goods on a pan-India basis is less than the mandated threshold limit of INR 40 lakh in a financial year (and in the case of some North Eastern and other states, the lower threshold of INR 20 lakhs). For suppliers of services, a lower registration threshold of INR 20 lakh in a financial year (in the case of the North Eastern States, a lower threshold of INR 10 lakh) has been prescribed. Furthermore, a supplier that only supplies GST-exempt goods and/or services is not required to obtain GST registration.

C. Rates under the GST schedule:

The following are the GST rate slabs for goods and services:

- 0%
- 5%
- 12%
- 18%
- 28%

Essential items have been included in the 0% tax slab, most goods and services in the 18% bracket, and specified luxury goods or services and 'sin' goods in the 28% slab.

In addition, identified luxury goods and services are also liable to Compensation Cess. The rate of Compensation Cess varies from 1% to 15%. It is even higher for tobacco and tobacco products. However, while this Cess has been called a 'Cess' (which should apply to the tax element), in reality it is levied on the base value of goods and services.

Since the introduction of the GST, in particular in the last one year, the Government has rationalised GST rates on goods and services multiple times to address concern areas for India Inc. The following are some noticeable developments in this area:

- The list of goods in the 28% bracket has been significantly pruned. This tax bracket now only covers 28 items including cement, auto and auto components.
- The Hospitality industry, which was struggling with a high GST rate of 18%, with limited input credits (due to a large number of suppliers in this sector being from the unorganised sector), heaved a sigh of relief with a reduction in the GST rate on restaurant services from 18% to 5% (without credits).
- The Real Estate sector, which was already going through a downturn due to socio-economic reasons such as demonetisation, had a set-back with an increase in the overall tax incidence due to the introduction of the GST. The Government has played a pivotal role in addressing the industry's key concerns. It has notified a revised reduced slab rate structure for different categories of properties, which has been effective from 1 April 2019.

D. Liability to pay GST: Generally, a supplier of goods or services bears the liability to pay GST. However, the recipient is liable to pay tax for certain types of transactions (such as sponsorship services or import of services). This method of collecting GST is commonly referred to as a 'reverse charge mechanism'.

E. Compliance-related requirements: The GST law stipulates stringent compliance-related requirements. A supplier of goods and services needs to file multiple returns for each registration within a month on a state-wise basis. This has kept the Government machinery on its toes. Now, with two years of experience and the need for further automation in the country, it has decided to revamp the entire compliance mechanism. It has rolled out a transition plan for the new GST returns to be implemented in phased manner from October 2019 onwards. A pilot run of the new process has already been initiated to provide adequate preparation time to industry with minimum disruption of business.

F. Electronic invoicing: The Government is set to implement an electronic invoicing system under the GST regime, which will radically transform administration of indirect tax and the way businesses are conducted in India. The new e-invoicing system will require suppliers to generate a unique Invoice Reference Number (IRN) from the Government portal or through a pre-defined algorithm. The IRN will need to be mentioned on invoices. The requirement for generation of IRN may be initially limited to B2B invoices for beyond a specified amount. The Government intends to implement the proposed system in a phased manner from 1 January 2020. It also plans to provide multiple channels for generation of IRN, e.g. a central portal, an ERP or Application Service Provider (ASP) system, an offline utility and an SMS mobile application.

G. Composition Scheme for small taxpayers: To ease the compliance burden on small taxpayers dealing in goods with an aggregate turnover of up to INR 150 lakhs, the Government has given them the option to opt for the Composition Scheme. Due to the overwhelmingly positive response to it, the Government has extended the scheme for suppliers of services and mixed suppliers with an aggregate turnover of up to INR 50 lakhs from 1 April 2019. Under this scheme, suppliers can pay tax at a specified percentage of their turnover during the year without claiming benefit of ITC on their procurement. However, such suppliers cannot recover taxes separately from buyers on their invoices. Consequently, buyers are not eligible to claim ITC on the tax paid by suppliers under the Composition Scheme.

A supplier with interstate supplies of goods is not eligible for the Composition Scheme and cannot opt for it. And while a regular taxpayer has to pay taxes on a monthly basis, a composition supplier is required to file returns and pay taxes on a quarterly basis. Moreover, it does not need to maintain detailed transaction-wise accounts and records, unlike a regular taxpayer.

Tax rate prescribed under the Composition Scheme:

Composition Scheme — applicable GST rates			
Type of business	**CGST**	**SGST**	**Total**
Manufacturer (other than those specifically notified by the Government, e.g. ice-cream, pan masala and tobacco products)	0.5%	0.5%	1%
Trader of goods	0.5%	0.5%	1%
Restaurant not serving alcohol	2.5%	2.5%	5%
Service providers/Mixed suppliers	3%	3%	6%

H. Input Tax Credit (ITC): The GST seeks to provide a seamless flow of credit across goods and services, compared to the erstwhile Indirect Tax, under which cross-utilisation of VAT paid on goods was not allowed against the Output Service Tax or Excise Duty liability, or vice versa. Taxpayers are permitted to avail ITC of the GST if procurement of goods and services has taken place during the course of or in furtherance of their business to provide taxable supplies. However, there are some exceptions to this general rule where the eligibility of ITC is restricted. Some of these restrictions include construction activities and employee-related expenditure. In a noteworthy departure from the erstwhile regime, ITC will only be available now when the tax collected has been deposited by suppliers and they have complied with the associated compliance-related requirements.

Furthermore, the ITC set-off mechanism has been altered to make credit of central GST more fungible. This new mechanism has been applicable from 1 February 2019, but the online functionality at the government portal has been made operational for returns to be filed for the month of June 2019 onwards. The table below depicts a comparison of the old versus the new set-off mechanism:

Earlier mechanism		
Payment for	First set off from	Then set off from
SGST	SGST	IGST
CGST	CGST	IGST
IGST	IGST	CGST and SGST (in this sequence only)
New mechanism		
SGST	IGST	SGST
CGST	IGST	CGST
IGST	IGST	CGST/ SGST

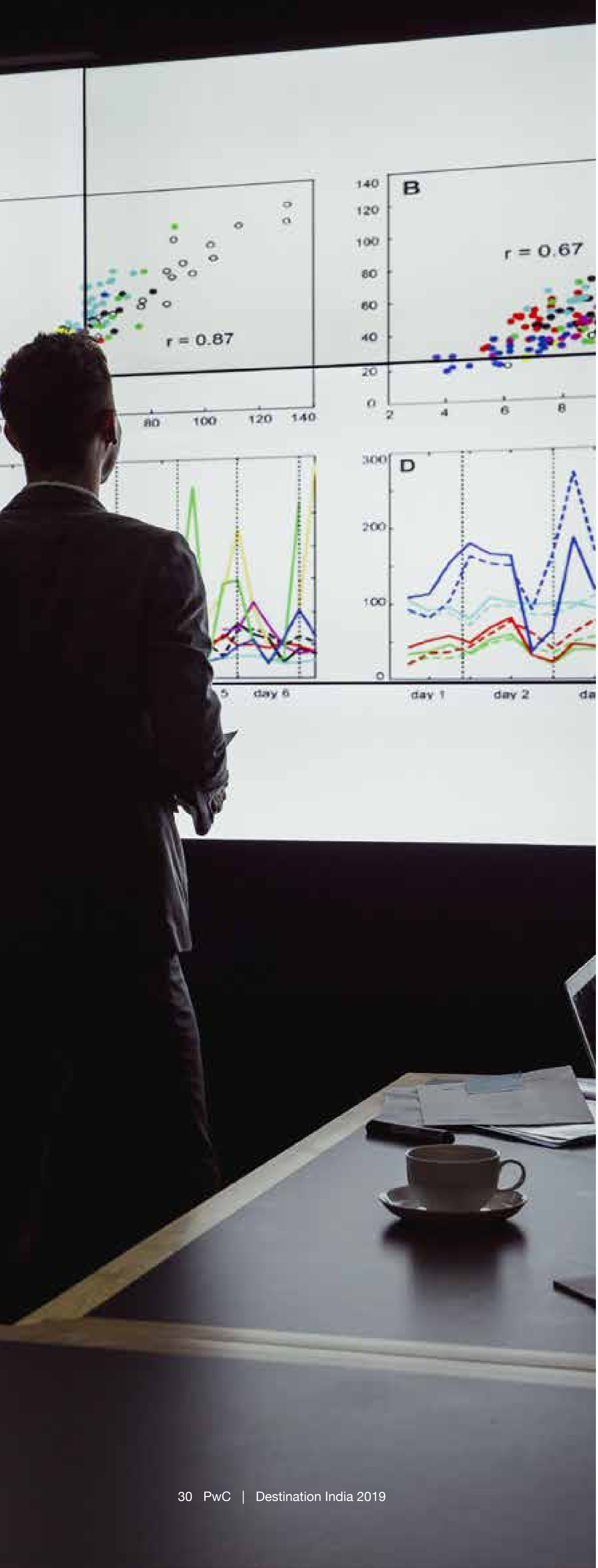
Furthermore, in the Union Budget 2019, the Government has allowed inter-head transfer (IGST, CGST and SGST) of cash ledger balances for tax, interest, penalty and fees for offsetting liability. This will help the industry manage funds in electronic cash ledgers.

I. Anti-Profiteering: The Central Government had constituted the National Anti-Profiteering Authority (NAPA) to verify companies' compliance with the anti-profiteering provision under the GST. GST regulations require suppliers to pass on to their recipients the benefits of incremental Input Tax credits or reduction in the tax rate in the form of a commensurate reduction in the prices of goods or services (or both) supplied by them. Aimed at protecting consumers' interest under GST, the NAPA was initially meant to be operational for a period of two years till November 2019. However, considering the large number of complaints received and the Government's intention of rationalising rates further, this timeline has been extended for a further two years by the GST Council.

J. Import of goods into India: Import of goods into India continues to be governed by Customs law. Imports attract Basic Customs Duty (BCD), Customs Cess, IGST and Compensation Cess (if applicable). BCD and Customs Cess paid at the time of import of goods is non-creditable and is therefore a cost. However, the ITC of IGST is available for adjustment against output GST liability. The ITC of Compensation Cess is only available for utilisation against an output Compensation Cess liability.

K. Exports and supplies to Special Economic Zones (SEZs): Export of goods or services and supplies to SEZs have been categorised as zero-rated supplies. A supplier providing supplies is eligible for either:

- Supply of goods or services under a bond or Letter of Undertaking without payment of tax and avail a refund for unutilised input tax credits attributable to exports
- Supply of goods or services by paying tax and thereafter claiming a rebate for this



L. Transactions between related persons or intra-entity supplies: Generally, only supplies made for a consideration are liable to the GST. However, in the case of transactions between related parties and provision of goods and services to establishments of this entity, even supplies made without consideration attract this tax.

M. Refund to retail outlets in departure area of international airport: Refund of applicable Input Tax has been allowed for retail outlets established in the departure area of international airports beyond immigration counters. Moreover, supplies have been made tax-free for outgoing international tourists.

The GST, as described by our Hon'ble Prime Minister, is a "good and simple tax". It celebrated its second anniversary on 30 June 2019. The GST has expanded the market for goods and services (replacing many small and fractured markets with a single common one) and has totally overhauled the Indirect Tax regime in the country.

The Government and industry had great hopes that the GST would be instrumental in reducing economic distortion and give the necessary boost to India's economic growth. The new tax regime has passed the test with India's GDP recording growth in comparison with numbers in the old taxation system.

Moreover, the favourable policy framework put in place by the Government, including liberalisation of FDI in various sectors and the launch of major national development programmes such as 'Make in India' and 'Digital India', has ensured significant inflow of foreign capital into India.

Improved governance, positive conditions for conducting business, transparency in government procedures and responsive policy-making, with an immediate focus on effective implementation of the Government's reforms, are expected to make India a preferred destination for foreign investment and set it on a growth trajectory that promises all-round development, economic welfare and strong macroeconomic indicators such as GDP, CPI and revenue collections. The GST, as a radical reform, is an enabler that is revitalising the business environment in India and is greatly enhancing its stature around the world.

4 Regulatory

The new Government coming back to power with a clear majority will provide an impetus for continued policy reforms in the country in the near future. The Government is expected to continue to focus on enhancing ease of doing business and promoting Make in India. In its first full budget, the re-elected Government has announced several policy measures with a short and long-term focus, including liberalisation of foreign investment norms, a continued push on building India as a global manufacturing hub, infrastructure development, digitisation of the economy and addressing the systemic risks in the financial system. With these announcements and the recent introduction and passage of numerous bills in the recent parliamentary session, the policy outlook looks positive and focused on driving the country into a new era of investments and formalisation of the economy.

Some of the key developments over the past 12 months are discussed below:

- Liberalisation/rationalisation of foreign investment norms in sectors like Insurance intermediaries, Single Brand Retail trade, coal mining activities, contract manufacturing and digital media
- Rationalisation of concentration norms for investment in Corporate Debt by FPIs
- The reporting mechanism for FDI has been further streamlined by the RBI through introduction of a dedicated portal for all foreign investment related compliances
- Rationalisation of reporting requirements for FPIs
- Amendments to the Insolvency and Bankruptcy Code to ensure smooth implementation of the law
- Overhaul of the cross-border borrowing and lending guidelines through RBI's revised framework on External Commercial Borrowing and rupee (INR) denominated bonds
- Introduction of an enabling framework for undertaking cross-border inbound/outbound merger transactions by the RBI.
- Enhanced focus on compliance and increased enforcement measures by the RBI on non-compliances with stricter penalty proceedings
- Corporates have enhanced accountability in terms of better corporate governance. Shell, inactive and defaulting companies are being constantly scrutinised through enhanced reporting requirements, disclosure of significant beneficial ownership and KYC-related filings.
- The mechanism of penalty and adjudication has been more clearly laid out in the Companies Act, 2013 vide recent amendments.
- Reporting requirements have been introduced for companies with respect to current outstanding dues to Micro, Small and Medium Enterprises (MSMEs).
- Consolidation of multiple labour laws under a single labour law code has been approved by the Government

Foreign investment

Entry options

A foreign entity setting up operations in India can either operate as an Indian company (by creating a separate legal entity in the country) or as a foreign entity with an office in India.

Operating as an Indian entity

Wholly owned subsidiary

A foreign company can set up a wholly owned subsidiary in India to engage in business activities permitted under the country's FDI policy. Such a subsidiary is treated as a separate legal entity and requires at least two shareholders (in the case of a private limited company) and seven shareholders (in the case of a public limited organisation). In addition, two directors are required, with one of them being an Indian resident.

Limited Liability Partnership (LLP)

In India, an LLP is structured as a hybrid entity, with the advantages of a company (since it is a separate legal entity with 'perpetual succession'), and at the same time enjoys the benefits of organisational flexibility associated with a partnership structure. At least two designated partners are required, of which one needs to be an Indian resident.

No tax is levied on distribution of profits as dividends to partners, unlike in the case of a company for which Dividend Distribution Tax (DDT) is applicable on repatriation of dividends.

Foreign investment in LLPs is permitted in sectors where 100% FDI is permitted under the automatic route without any performance-linked conditions.

Joint Venture (JV) with Indian partners (equity participation)

Although a wholly owned subsidiary is generally the preferred option in view of the associated brands and technologies involved, foreign companies also have the option of conducting their operations in India by forming strategic alliances with their Indian partners. Typically, such foreign entities identify partners engaged in the same area of activity or those that can add synergies to their strategic plans in India. Sometimes, formation of JVs is necessitated due to restrictions on foreign ownership in selected sectors under the FDI policy, e.g. the Insurance and Multi-brand Retail Trade segments.

Operating as a foreign entity

A foreign entity can set up an office in India in the form of a liaison office (LO), a branch office (BO) or a project office (PO), based on the nature of activities it proposes to engage in and its commercial objective. This can be done by submitting an application to an Authorised Dealer (AD) bank. However, the approval of the RBI is required under the following circumstances:

- The applicant is a citizen of or is registered or incorporated in Pakistan.
- The applicant is a citizen of or is registered or incorporated in Bangladesh, Sri Lanka, Afghanistan, Iran, China, Hong Kong or Macau and the application is for opening a BO, LO or PO in Jammu and Kashmir, the North East region or the Andaman and Nicobar Islands.
- The principal business of the applicant is concentrated in four sectors—Defence, Telecom, Private Security, and Information and Broadcasting. However, prior approval of the RBI shall not be required in cases where Government approval or licence/permission by the concerned Ministry/Regulator has already been granted. Further, in the case of proposal for opening a PO relating to defence sector, no separate reference or approval of Government of India is required if the said non-resident applicant has been awarded a contract by/ entered into an agreement with the Ministry of Defence or Service Headquarters or Defence Public Sector Undertakings. The applicant is a Non-Government Organisation (NGO), Non-Profit Organisation, or an entity, agency or department of a foreign government.

Once an office has been set up, it needs to be registered with the Registrar of Companies.

Each type of office can be established for the specific objectives mentioned below.

LOs

Setting up an LO or representative office is a common practice among foreign companies or entities seeking to enter the Indian market. The role of LOs is limited to collecting information about the market and providing data pertaining to the company and its products to prospective Indian customers. An LO is only allowed to undertake liaison activities in India, and therefore, cannot earn any income in the country.

BOs

Compared to an LO, a BO can be set up and engage in a wide range of activities, including revenue generation, in India. Foreign entities can set up branch offices in the country to conduct the following activities:

- Export and import goods
- Provide professional or consultancy services
- Participate in research in which their parent companies are engaged
- Promote technical or financial collaboration between Indian companies and their parent organisations
- Represent their parent companies in India and act as their buying or selling agents in the country
- Offer IT and software development services in India
- Provide technical support for products supplied by their parent or group companies
- Represent foreign airlines or shipping companies

Project offices

Foreign companies planning to execute specific projects in India have the option of setting up project and site offices. Such project offices (POs) can be operational during the tenure of a project. Where the criteria prescribed are not met, approval is required from the RBI to set up a PO.

Foreign investment in India

Currently, FDI is permitted in all sectors except in the following:

- Lottery business, including government or private lotteries or online lotteries
- Gambling and betting, including in casinos
- Chit funds and 'Nidhi' companies
- Trading in Transferable Development Rights (TDRs)
- Real Estate business or construction of farmhouses
- Manufacture of cigars, cheroots, cigarillos and cigarettes, and tobacco or tobacco substitutes
- Activities and sectors not open to private sector investment, e.g. atomic energy and railway operations (other than those specifically permitted)
- Collaboration on foreign technology in any form, including licensing of franchises, trademark, brand names, management contracts for lotteries, and gambling and betting activities

India's FDI policy covers 27 sectors and activities with sectoral caps or conditions for receiving foreign investment. Insurance, Construction and Development, Retail, Telecom and Media are some of these sectors.

Foreign investment is allowed in India via the following routes:

- Automatic route: Prior approval is not required from the Government to receive foreign investment.
- Approval route: This requires the Government's approval for receiving foreign investment.

Foreign investment-related proposals under the government approval route (involving a total inflow of foreign equity of more than INR 50 billion) need to be placed before the Cabinet Committee on Economic Affairs (CCEA) of the Government for further consideration.

Computation of foreign investment

From the perspective of the FDI policy, investments made directly by a non-resident entity in an Indian company are considered for foreign investment limits or sectoral caps, along with any investment made by a resident Indian entity (the majority of such entities being owned or controlled by non-residents).

Any downstream investments made by an Indian company (owned or controlled by non-residents either under the FDI route or the portfolio investment route) also need to comply with sectoral caps and conditions. Details of downstream investments made by foreign-owned and controlled companies have to be intimated to the Department for Promotion of Industry and Internal Trade (DPIIT) and RBI.

Any portfolio investment made by a Securities and Exchange Board of India (SEBI)-registered FPI, known as a Registered Foreign Portfolio Investor (RFPI), is also regarded as a 'foreign' investment. Such investments are subject to individual and aggregate investment limits of 10% and 24%, respectively (and the aggregate limit can be increased up to the sectoral cap with a board and special resolution). The individual and aggregate limit for NRIs investing under the Portfolio Investment Scheme is capped at 5% and 10%, respectively (and the aggregate limit for them can be increased to 24% with a board and special resolution).

In addition, RFPIs are eligible to invest in government securities and corporate debt from time to time, subject to limits specified by the RBI and SEBI.

Valuation-related norms

Issue of shares to non-residents or transfer of shares by residents to non-residents, and vice versa, is subject to valuation-related guidelines, based on which there needs to be a fair valuation of shares. This valuation is done in accordance with internationally accepted pricing methodologies on an arm's length basis—duly certified by a chartered accountant (CA) or SEBI-registered merchant banker in the case of unlisted companies. However, if shares are listed, the consideration price cannot be less than that arrived at in accordance with SEBI's guidelines.

When non-residents (including NRIs) make investments in Indian companies by subscribing to the Memorandum of Association, such investments may be made without the need for a valuation.

Funding options in India

A foreign company setting up an Indian entity (subsidiary or JV) can fund it through the following options:

Equity capital

Equity shares constitute the common stock of a company. Equity capital comprises securities representing equity ownership in an enterprise. It provides voting rights to and entitles the holder to a share in its success via dividends or capital appreciation, or both.

Issue of equity shares by an Indian company to a foreign resident needs to comply with the sectoral caps detailed in the Government's FDI policy.

External Commercial Borrowings (ECBs)

ECBs are commercial loans and include bank loans, buyers' credit, suppliers' credit, securitised instruments (e.g. floating rate notes and fixed rate bonds), Foreign Currency Convertible Bonds (FCCBs), Foreign Currency Exchangeable Bonds (FCEBs), INR denominated bonds or a financial lease from non-resident lenders in any freely convertible foreign currency or Indian rupees. However, the ECB framework is not applicable for investments in Non-convertible Debentures (NCDs) made by RFPIs in India.

An ECB can be raised by an Indian 'Eligible Borrower' from an 'Eligible Lender' as follows:

- Foreign Currency ('FCY') denominated ECB
- Indian Rupee ('INR') denominated ECB

ECBs can either be availed of under the automatic route or the approval route. Under the approval route, prior permission of the RBI is required to raise ECBs. Under either route, it is mandatory to periodically provide post-facto intimation to the RBI, as prescribed under the Foreign Exchange Management Act (FEMA), 1999.

Borrowers eligible for ECBs include all entities eligible to receive FDI (except LLPs). Eligible lenders should be residents of FATF or IOSCO compliant countries and include foreign equity holders of Indian borrowing entities holding the prescribed percentage of capital.

The RBI has prescribed the limits up to which ECBs can be availed and its approval is required to raise funds beyond these limits. ECB guidelines also prescribe an 'all-in-cost' ceiling for raising funds through ECBs. This includes the rate of interest, other fees, expenses, charges and guarantee fees (whether paid in foreign currency or INR), but not commitment fees, pre-payment fees or charges and Withholding Tax payable in Indian rupees. In the case of fixed rate loans, the swap cost and the spread should be equal to the floating rate in addition to the applicable spread. The all-in-cost ceiling depends on the track under which ECBs have been raised, and is prescribed through a spread over the benchmark, i.e. 450 basis points per annum over the Benchmark rate for the particular currency.

Fully and compulsorily convertible preference shares and debentures

Indian companies can also receive foreign investments through issue of fully and compulsorily convertible preference shares and debentures. The conversion formula or price for issue of equity shares, based on their conversion needs, needs to be determined in advance at the time they are issued.

Optionality clauses are allowed in fully and compulsorily convertible preference shares, debentures and equity shares under the FDI scheme in the following circumstances:

- There is a minimum lock-in period of one year.
- This period is effective from the date the capital instruments are allotted.
- After the lock-in period, and subject to the provisions of the FDI policy, non-resident investors exercising their option or right are allowed to exit without any assured returns, in accordance with pricing- and valuation-related guidelines issued by the RBI from time to time.

The negative list for end use of ECB is as follows:

a) Real estate activities

b) Investment in the capital market

c) Equity investment

d) Repayment of rupee loans (except for specific cases)

e) On-lending to entities for the above activities.

Non-convertible, optionally convertible or partially convertible preference shares and debentures issued on or after 1 May 2007 are considered as debt, and all the norms applicable to ECBs in relation to eligible borrowers, recognised lenders, amounts, maturity, end-use stipulations, etc., are applicable in such cases.

Investment by FPIs in corporate debt securities

FPIs can make investment under the corporate bond route, including in unlisted corporate debt securities in the form of NCDs or bonds issued by public or private companies.

The RBI relaxed the existing concentration norms for investment by an FPI in Corporate Debt by limiting the exposure to a single corporate (including exposure related entities) to 20% of the FPI's corporate bond portfolio.

Significant exchange control-related regulations

Foreign exchange transactions are regulated by FEMA, under which foreign exchange transactions are divided into two broad categories—current account transactions and capital account transactions.

Transactions that alter the foreign assets or liabilities, including contingent liabilities, of a person resident in India or the assets or liabilities of a person in India who is resident outside the country, including transactions referred to under Section 6(2) and 6(3) of FEMA, are classified as capital account transactions. Transactions other than these are classified as current account transactions.

The Indian rupee is fully convertible for current account transactions, subject to a negative list of transactions, which are either prohibited or which require the prior approval of the Central Government or the RBI.

Current account transactions

The RBI has delegated its powers to AD banks (entities authorised by the RBI) in relation to monitoring of or granting permission for remittances under the current account window. All current account transactions are usually permitted unless they are specifically prohibited or restricted.[26]

According to the Current Account Transaction (CAT) Rules, withdrawal of foreign exchange is prohibited for the following purposes:

- Remittance from lottery winnings
- Remittance of income from racing, riding, etc., or any other hobby
- Remittance for purchase of lottery tickets, banned or prescribed magazines, football pools, sweepstakes, etc.
- Payment of commission on exports for equity investments in the JVs or wholly owned overseas subsidiaries of Indian companies
- Remittance of dividend by a company for which the requirement of 'dividend balancing' is applicable
- Payment of commissions on exports under the 'rupee state credit' route, except for commissions of up to 10% of the invoice value of export of tea and tobacco
- Payment for the 'call back services' of telephones
- Remittance of the interest income of funds held in a non-¬resident special rupee (account) scheme

CAT Rules also specify transactions[27] for which withdrawal of foreign exchange is only permitted with the prior approval of the Central Government. However, the Government's approval is not required if payment is made from funds held in the Resident Foreign Currency Account of the remitter.

Resident individuals can avail of the foreign exchange facility for the purposes mentioned in Para 1 of Schedule III of the FEM (CAT) Amendment Rules, 2015, dated 26 May 2015 (within a limit of USD 250,000), as prescribed under the Liberalised Remittance Scheme (LRS).[28]

26. Foreign Exchange Management (Current Account Transactions) Rules, 2000 (CAT Rules)
27. Schedule II of CAT Rules
28. The LRS is available for resident individuals for remittances towards permissible current and capital account transactions or a combination of both. The scheme has an overall limit of remittance up to USD 2,50,000. However, this scheme does not allow remittances for any prohibited or illegal activities such as margin trading or lotteries.

Current account transactions entered by residents other than individuals, undertaken in the normal course of business, are freely permitted, except in the following cases of remittances being made by corporate organisations:

- Remittances towards consultancy services procured from outside India for infrastructure projects of up to USD 1,00,00,000 per project and of up to USD 10,00,000 per project for other projects
- Pre-incorporation expenses of up to 5% of investment brought in or USD 1,00,000, whichever is higher
- Donations of a maximum of USD 50,00,000 for a specified purpose or up to 1% of forex earning in the preceding three financial years
- Commission per transaction to agents abroad for sale of residential flats or commercial plots of up to USD 25,000 or 5% of inward remittance, whichever is higher

Any remittance in excess of USD 250,000 and the limits given above for the specified purposes mentioned will require the prior approval of the RBI.

Capital account transactions

The general principle for capital account transactions is that these are restricted unless specifically or generally permitted by the RBI, which has prescribed a number of permitted capital account transactions for individuals resident in or outside India. These include the following:

- Investment made in foreign securities by a person resident in India
- Investment made in India by a person resident outside the country
- Borrowing or lending in foreign exchange
- Deposits between persons resident in India and persons resident outside the country
- Export or import of currency
- Transfer or acquisition of immovable property in or outside India

Under the LRS, resident individuals can remit up to USD 2,50,000 per financial year for any permitted capital account transactions. The permissible capital account transactions of an individual under the LRS include:

- Opening of a foreign currency account outside India
- Purchase of property outside the country
- Making investments in foreign countries
- Setting up wholly owned subsidiaries and JVs outside India
- Giving loans, including in Indian rupees, to NRI relatives

With respect to overseas investments in a JV or wholly owned subsidiary, the limit for a financial commitment is up to 400% of the net worth of an Indian entity as on its last audited balance sheet date. However, any financial commitment exceeding USD 1 billion (or its equivalent) in a financial year requires the prior approval of the RBI, even when the total financial commitment of the Indian entity is within the eligible limit under the automatic route (i.e. within 400% of its net worth according to its last audited balance sheet).

In order to set up offices abroad, AD banks are permitted to allow remittances by Indian entities towards initial expenses of such offices. The limit set is 15% of their average annual sales, income or turnover during the previous two financial years or up to 25% of their net worth, whichever is higher. Remittances of up to 10% of an entity's average annual sales, income or turnover are allowed for the recurring expenses it has incurred on its normal business operations during the previous two financial years.

Repatriation of capital

Foreign capital invested in India is usually repatriable, along with capital appreciation, after payment of taxes due, provided the investment was originally made on a repatriation basis.

Acquisition of immovable property in India

Foreign nationals of non-Indian origin, who are resident outside India, are not permitted to acquire any immovable property in the country unless this is by way of inheritance. However, they can acquire or transfer immovable property in India on a lease, which does not exceed five years, without the prior permission of the RBI.

Foreign companies that have been permitted to open branches or POs in India are only allowed to acquire immovable property in the country that is necessary for or incidental to their carrying out such activities. Foreign enterprises that have been permitted to open LOs in India can only acquire property by way of a lease (that does not exceed five years) to conduct their business in the country.

Royalties and fees for technical know-how

Indian companies can make payments against lump sum technology fees and royalties without being subject to any restrictions under the automatic route.

5

Global Mobility Services

International assignments to India

Taxation of foreign nationals working in India is based on their residential status during the relevant financial year (referred to as FY or tax year), which depends on the number of days these individuals were physically present in India. The tax year in India runs from 1 April to 31 March of the succeeding year.

Under domestic tax law, individuals are considered to be tax residents in India on satisfaction of either of the following conditions:

- They have been physically present in India for 182 days or more in the relevant tax year (referred to as the '182 day rule').
- They have been physically present in India for 60 days or more during the relevant tax year and for 365 days or more in the preceding four tax years (referred to as the '60 day rule').

However, only the 182-day rule is applicable in a situation where a citizen of India leaves the country as a member of the crew of an Indian ship or for the purpose of employment outside India, or is an Indian citizen or person of Indian origin living outside India and on a visit to the country. Hence, for such individuals, the 60-day rule will not be applicable to determine their tax residency in India in a given tax year

If individuals do not satisfy either of the conditions given above, they qualify as non-residents (NRs) of India for the particular tax year.

In addition to the above, resident individuals are treated as Residents but Not Ordinarily Residents (RNORs) of India if they satisfy either of the following conditions:

- They are NRs for nine of the ten tax years preceding the relevant tax year.
- They were physically present in India for 729 days (or less) during the seven tax years preceding the relevant tax year.

If individuals do not satisfy both the conditions listed above, they qualify as Residents and Ordinarily Residents (RORs) of India for the specific tax year.

In determining the physical presence of individuals in India, it is not essential that their stay in the country is continuous or at the same place. Furthermore, their date of arrival in India and date of departure from India are both included to determine their period of stay in the country. The purpose of their stay in India is irrelevant, and even if it is for a visit to their families or for tourism, it is counted to determine their stay in the country. If individuals qualify as tax residents of India as well as of other countries (if they are employed in multiple countries), the conditions prescribed under the tie-breaker test of the relevant DTAA between the relevant contracting states need to be referred to in order to determine the residency of such individuals in the contracting states.

Scope of taxation

Under Indian tax laws, the scope of taxation for each category is as follows:

- ***ROR:*** The global income of individuals, i.e. income accruing or deemed to accrue or arise, as well as income received or deemed to be received in or outside India is liable to tax in the country.
- ***RNOR:*** Income received in India, accruing, arising or deemed to accrue or arise in the country, derived from business controlled from India or from a profession set up in the country is liable to tax in it.
- ***NR:*** Income received in India or accruing, arising or deemed to accrue or arise in India is liable to tax in the country.

Taxation of employment-generated income

Employment-generated income for services rendered in India is taxable in the country, irrespective of where it is received.

Taxable income includes all kinds of payments received, either in cash or kind, from an office of employment. Apart from sources such as fees, bonuses and commissions, some of the most common modes of remuneration include allowances, reimbursement of personal expenses, payment for education and the perquisites or benefits provided by employers, either free of cost or at concessional rates. All such payments are to be included, whether paid directly to employees or by employers on the former's behalf.

Housing-related benefits provided by employers are generally taxed at 15% of their salaries or on the actual rent paid for accommodation, whichever is less. Hotel accommodation is taxable at 24% of the salary or the actual amount paid, whichever is less. The cost of meals and laundry expenses is fully taxable.

The value of any specified security, or sweat equity shares allotted or transferred directly or indirectly by employers or former employers, free of cost or at a concessional rate, and the contribution of employers to an approved superannuation fund (if this exceeds INR 150, 000), are taxable as perquisites in the hands of employees. Car and driver facilities provided by employers are also taxable as perquisites, although at a concessional value as per prescribed Income-tax Rules.

There are several issues relating to taxation of employment-generated income, which depend on the facts and circumstances of each case as well as on the tax authorities' views. Therefore, it is advisable to seek professional advice on a remuneration package as a whole, for appropriate estimation of tax costs.

Withholding Tax

With respect to employment-generated income, employers are required to withhold taxes at source (TDS) on earnings from employees' salaries at applicable rates, and deposit such withheld taxes to the account of the Government's treasury within seven days from the end of the month during which the salaries were paid (except for the month of March when the date of deposit is extended up to 30 April).

Employers are required to comply with the Withholding Tax mechanism, even if the employees are NRs of India. The details of taxes deducted by the employer need to be reported in the form of a Withholding Tax return (TDS return). A TDS return is a quarterly statement submitted by the employer or deductor of tax with the Indian Income-tax Department, providing the details of income paid and taxes deducted or deposited. In addition to TDS returns, it is mandatory for the employer to issue annual tax certificates, Form 16-Part B and 12BA (Form 16), to its employees. These certificates provide a detailed summary of the amount paid or credited to the employee and TDS deducted.

CBDT has introduced online filing and processing of applications for obtaining NIL or lower Withholding Tax certificates in relation to payments to be made to non-residents.

Double Taxation Avoidance Agreement (DTAA)

In situations where individuals are treated as tax or treaty residents of other countries, they may qualify for relief under Indian tax law under the respective DTAAs signed between India and these countries. For most agreements currently in force, various tests are conducted to determine the actual residential status of individuals.

Many agreements include clauses that exempt residents of specific countries from tax on employment-generated income earned in India if they have been residing in the country for less than 183 days in the given tax year, and if other conditions relating to salary chargeback and payment of salaries by NRs, etc. are satisfied.

However, to avail of the benefits of a treaty, individuals need to obtain a Tax Residency Certificate (TRC) from tax authorities in their home countries, certifying that they are tax residents of these countries. Short stay exemption, as per the provisions of Indian tax laws, may be availed by foreign nationals from countries with which India does not have treaties in force, provided their stay in India during that particular tax year does not exceed 90 days and they meet certain other specified conditions.

It is important to note that appropriate advice should be taken with respect to specific facts before adopting such positions.

Tax rates

Taxes are levied at progressive rates in India. The rates applicable for tax year 2019-20 are as follows:

Taxable income (INR)	Tax rate
Up to INR 250,000	NIL
INR 2,50,001 to INR 5,00,000	5%
INR 5,00,001 to INR 10,00,000	20%
Above INR 10,00,000	30%

The basic exemption limit for resident individuals above 60 years but less than 80 years of age at any time during the tax year is INR 0.3 million and for resident individuals who are 80 years of age or more, it is INR 0.5 million. Resident individuals with a total income up to INR 0.5 million are not required to pay any taxes.

Surcharge (if applicable) will be levied at the following rates in addition to income tax:

Taxable income (INR)	Surcharge (%)
Up to 5 million	NIL
Above 5 million but up to 10 million	10
Above 10 million but up to 20 million	15
Above 20 million but up to 50 million	25
Above 50 million	37

Health and Education Cess (HEC)

Health and Education Cess at the rate of 4% of the income tax and surcharge (if applicable) will be levied to compute the final tax liability of individuals.

Maximum marginal tax rate (MMR)

Based on the above, the MMR for individuals are provided below:

Taxable income (INR)	Maximum marginal tax rate (%)
Up to 5 million	31.2
Above 5 million but up to 10 million	34.32
Above 10 million but up to 20 million	35.88
Above 20 million but up to 50 million	39
Above 50 million	42.744

Tax registration

Individuals need to apply for and obtain their tax registration number, Permanent Account Number (PAN), in India. It is mandatory for them to quote PAN on their return of income and all other correspondence with any Indian Income-tax authority. Employers are required to quote the PAN of individuals in the TDS returns and Form 16 issued to them.

Filing of tax returns

At the end of every tax year, a personal tax return needs to be filed by an individual with the Income tax authorities in the prescribed format. The due date for salaried individuals filing returns is typically 31 July of the year immediately following the relevant tax year (a different date may apply for individuals with business or professional income).

A tax return can be filed even after the due date in the form of a belated return, but this needs to be filed no later than one year from the end of the relevant tax year. There are some monetary implications, which are detailed below:

Particulars	Fees
Return furnished after due date, but on or before 31 December of the relevant assessment year*	INR 5,000
Return furnished after 31 December, but on or before 31 March of the relevant assessment year*	INR 10,000

***Assessment Year (AY):** An AY is the year immediately following the financial year wherein the income of the FY is assessed, e.g. the AY in relation FY2019–20 will be 2020-21.

This fee is capped at INR 1,000 for taxpayers earning a total income of up to INR 0.5 million.

An Income-tax return filed (original or belated) can be revised within one year from the end of the relevant tax year.

Mandatory furnishing of return of income

It is mandatory to file return of income in the following cases:

- An individual qualifying as an ROR, owning foreign assets (as a beneficial owner or otherwise) or with signing authority in any account located outside India
- A person depositing more than INR 10 million in one or more current accounts maintained with banks or co-operative banks
- A person incurring expenditure exceeding INR 0.2 million for self or any other person for travel to a foreign country
- A person incurring expenditure exceeding INR 0.1 million towards consumption of electricity
- A person fulfilling other conditions as may be prescribed

Those who are 80 years old or more and qualify as RORs of India have the option to file their tax returns manually in ITR 1 or ITR 4. It is mandatory for such individuals to file tax returns electronically in the following cases:

- Where there is a claim of refund
- Where the total income exceeds INR 0.5 million
- Where an individual qualifies as an ROR and has foreign assets or signing authority for any of his or her accounts located outside India (So technically, this includes spouses of expatriates who qualify as RORs of India and hold assets outside the country, even if they earn no income from it.

If individuals qualify as RORs, detailed disclosures are needed in their returns in relation to their foreign assets. Non-disclosure or inaccurate disclosure can result in severe penalties, including prosecution, under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015.

Individuals with a total income exceeding INR 5 million need to report the details of their assets and corresponding liabilities at the end of the relevant financial year on an Income-tax return form. These details include assets such as immovable property; movable assets such as jewellery, bullion, archaeological collections, drawings, paintings, sculptures or any works of art, vehicles, yachts, boats and aircraft; financial assets such as bank shares and securities, insurance policies, loan advances given and cash in hand, and interest held in the assets of a company or association of persons (**AOP**) or its member.

Other matters

Visa

Foreign nationals wanting to come to India need to have valid passports and visas. Visas are issued by Indian Consulates or High Commissions in their home countries. The type of visas that need to be obtained depends on the purpose and duration of their visit. Foreign nationals are not permitted to take up employment in India unless they hold valid employment visas, which are issued to highly skilled individuals or professionals, provided they earn salaries exceeding the specified limit. Such visas are generally issued for a period of one to two years and can be subsequently extended.

Registration with Foreigners' Regional Registration Officers

Foreign nationals visiting India, who either have valid employment visas or intend to reside in the country for more than 180 days, must register themselves with Foreigners' Regional Registration Officers (FRROs) within 14 days of their arrival in the country. FRROs issue residential permits to such foreign nationals on their submitting the prescribed documents. The Government of India has digitised the process of FRRO registration by introducing an e-FRRO portal in certain Indian cities to provide faceless, cashless and paperless services to foreign nationals.

Exit-related compliance requirements

On completion of their assignments in India, foreign nationals are required to obtain a No Objection Certificate (NOC) from the Indian tax authorities at the time of their departure from the country.

Payment of salaries outside India

Current exchange control regulations permit foreign nationals, who are employees of foreign companies and are on secondment or deputation to their offices, branches, subsidiaries, JVs or group companies in India, to open, hold and maintain foreign currency accounts with banks outside the country. They can remit their salaries to their bank accounts outside India, provided they have paid tax on their salaries in the country.

Social security in India

Foreign nationals holding passports of foreign countries are required to contribute to social security schemes in India, provided they are working for establishments to which Indian social security laws apply. However, if such foreign nationals belong to countries with which India has a Social Security Agreement (SSA) and they contribute to social security schemes in their home countries, they are exempt from contributing to Indian social security schemes, provided they obtain a Certificate of Coverage (COC) from their home countries' social security authorities.

India has signed SSAs with 19 countries, and most of these are operational, except for its SSA with Brazil, which is not yet operative.

Similarly, International Workers (IWs) from countries with which India has entered a bilateral Comprehensive Economic Cooperation Agreement (CECA) prior to 1 October 2008 are exempted from India's social security regulations if they meet the following criteria:

- They contribute to their home countries' social security systems, either as citizens or residents.
- The CECA specifically exempts naturalised individuals of contracting countries from contributing to the social security system in India.

Singapore is the only country with which India signed a CECA before 1 October 2008.

IWs, who are not exempt for the reasons given above, are required to contribute 12% of their salaries to India's social security system. Employers need to deduct this amount from their employees' monthly salaries, and after making a matching contribution of 12%, deposit the amount with India social security authorities.

Currently, for any IW coming to work in India for a covered establishment, and drawing a salary of more than INR 15,000 per month, the employer's contribution of 12% is deposited in their Provident Fund accounts and no allocation is made towards their Pension Funds. However, for IWs who joined work before 1 September 2014 and are still working in India, an amount equal to 8.33% of their salaries is allocated to their Pension Funds and the balance is deposited in their Provident Fund accounts.

IWs can withdraw the accumulated balance in their Provident Fund accounts under the following circumstances:

- On their retirement from service in the organisation for which they are working or after reaching the age of 58 years, whichever is later
- On their retirement on account of permanent and total incapacity to work due to bodily or mental infirmity, as certified by a prescribed medical or registered practitioner
- In a situation where they are suffering from certain diseases, which are detailed under the terms of the scheme
- On ceasing to be employees of a covered establishment (if the international employees are from SSA countries)

The amount withdrawn from an IW's PF account before completion of five years of his or her service in India attracts tax. In the case of international employees from SSA countries, withdrawal from their Provident Fund (PF) accounts can be directly credited in their bank accounts in their home countries. To simplify the process of withdrawal, an option is available whereby IWs from SSA countries can provide details of their overseas bank accounts in which they wish to receive their Provident Fund. Thereafter, the Provident Fund authorities, after completing the requisite formalities and documentation, can facilitate payment to these overseas bank accounts.

In all other cases, the amount they withdraw is credited to their Indian bank accounts.

The accumulated amount in Pension Funds is paid as pension to employees on their retirement or in certain other circumstances, as specified in the Pension Scheme. International employees are not entitled to pension benefits from Pension Funds unless they have rendered eligible service for a period of 10 years in a 'covered' establishment in India. However, the option of early withdrawal of pension contributions before completing 10 years of service is available to international workers from SSA countries.

Secondment-related documentation

Secondment-related arrangements need to be supported with appropriate and robust documentation, and reviewed, keeping in view the following considerations:

- Corporate Tax implications (e.g. exposure to Permanent Establishment)
- Withholding Tax implications
- Transfer Pricing regulations
- Goods and Services Tax (GST) implications
- Indian social security regulations
- Exchange control regulations
- Company Law regulations

Black Money Act

The Black Money (Undisclosed Income and Foreign Assets) and Imposition of Tax Act, 2015 (the Black Money Taxation Act) covers all persons who were resident of India, in accordance with the provisions of the Income-tax Act, 1961 (the Act), either in the tax year to which the income relates or in the tax year in which the undisclosed asset located outside India was acquired. Any undisclosed foreign income or assets detected are taxed at 30% under this law. In addition, there is a provision in this law for a penalty of 300% of the tax amount and imprisonment of up to 10 years. Non-disclosure or inaccurate disclosure can attract a penalty of INR 1 million and imprisonment of up to seven years.

6 Financial Services

Overview

India's Financial Services sector is expected to dominate the country's economy over the next few decades. Banking, capital markets, asset management, etc. are expected to grow significantly in the next few years. And Foreign Portfolio Investors (FPIs) are again keen to invest in India in the long term. In addition, large players in the Fund Management industry are exploring investment opportunities and are setting up their business presence in India.

India's Financial Services sector is operating in a fast-evolving and dynamic regulatory and tax landscape with an ever-growing demand for transparency and efficiency. This makes it extremely important for industry players or new entrants to understand the tax and regulatory framework. This could make an impact on their business goals. We have discussed below certain key vehicles that drive India's Financial Services sector.

Banking and finance

The Banking sector in India is regulated by the Reserve Bank of India (RBI), the country's central bank, which is the regulatory and supervisory authority for all banking operations in the country. The RBI has put in place a regulatory framework and guidelines to not only regulate banking companies in India, but also non-banking financial companies, asset reconstruction companies, investment holding companies, etc.

India's Banking sector is broadly represented by public sector banks (most of which are mainly owned by the Government of India), private sector banks, foreign banks operating in the country through their branches, subsidiaries, etc. While taxation of these banks is similar to that applicable for general corporate entities or the branches of foreign companies in India, there are certain provisions under India's Income-tax law that specifically relate to banks in India, e.g. the following:

a) Deduction of provision for bad and doubtful debts in the range of 5% to 8.5% of the total income computed in the prescribed manner, depending on the type of bank

b) Flexibility to offer interest income on non-performing assets for levy of income-tax on a cash basis (instead of on an accrual basis)

c) Application of RBI guidelines for computation of income from securities including derivatives and forward foreign exchange contracts

There is no tax deduction at source (TDS) for interest received by Indian banks and in the case of the Indian branches of foreign banks, TDS is not applicable if they have obtained TDS exemption certificates issued by the Indian revenue authorities.

Similarly, there are specific tax provisions for Non-banking Financial Companies (NBFCs) in India, which *inter alia* include:

a) Deduction for provision for bad and doubtful debts of 5% on the total income computed in the prescribed manner

b) Deduction for amount transferred to special reserve created by specified non-banking financial companies engaged in specified businesses

Furthermore, as per the recently amended Finance Act, 2019, interest income earned on non-performing assets by deposit-taking NBFCs and systemically important but non-deposit-taking NBFCs will be taxed on a cash basis (instead of an accrual basis).

While a service provided by banks and non-banking financial companies to grant deposits, loans and advances (in so far as the consideration is represented by way of interest or discount) is exempt from the Goods and Services Tax (GST), GST at the rate of 18% is applicable for other services provided by them. Banks and non-banking financial companies have the blanket option to avail 50% of Input Tax credit instead of availing t, based on their ratio of taxable output supplies to total output supplies. For inter-branch services within India, 100% input tax credit is available to banks.

While the GST is applicable on services including purchase and sale of foreign currency, based on their notional values, it is not applicable for inter-se purchase and sale of foreign currency between banks or authorised dealers. Purchase and sale of securities including derivatives do not attract GST either.

Alternative Investment Funds (AIFs)

In 1996, Venture Capital Fund (VCF) regulations were framed by the Securities and Exchange Board of India (SEBI) to encourage funding of entrepreneurs' early-stage companies. However, it was found over the years that VCFs were being used as a vehicle for many other funds such as private equity, private investment in public equity and real estate. Therefore, in 2012, VCF regulations were replaced by the SEBI's Alternative Investment Funds regulations with the intention of regulating unregistered pooling vehicles, to avoid regulatory gaps and offer a level playing field to funds or industries.

An AIF is a privately pooled investment vehicle, established or incorporated in India, and can be set up in the form of a trust, company or limited liability partnership. Pooling of funds by domestic and foreign investors is permissible, and investments need to be made in line with a defined investment policy, depending on the category of AIF, on the basis of the AIF regulations.

AIFs are divided into three categories, based on their investment-related focus:

- **Category I AIFs** include funds that invest in start-up or early stage ventures, social ventures, small and medium enterprises (SMEs), infrastructure or other sectors regarded as socially or economically desirable. These comprise venture capital funds, SME funds and infrastructure funds.
- **Category II AIFs** include funds that do not specifically come under either Category I or Category III. A typical private equity fund or a debt fund comes within this category.
- **Category III AIFs** include funds that employ diverse or complex trading strategies and leverage, including through exposure to derivatives. Hedge funds typically come under this category.

An AIF can be set up if it satisfies the following minimum criteria:

Parameter	Particulars
Minimum fund size	INR 200 million
Minimum investment by an investor	INR 10 million
Number of investors	1,000 (max)
Mode of raising capital	Private placement

Category I and II AIFs are regarded as (i) 'tax transparent' vehicles for all investment income, i.e. the AIF pays no tax, and such income earned by the AIF is taxable directly in the hands of an investor at applicable tax rates; and (ii) 'tax opaque' vehicles for all its business income.

Prior to 1 April 2019, the benefit of 'pass through' of losses was not available to investors. Such losses were allowed to be carried forward and set off by the AIF.

However, as per the recently amended Finance Act, 2019, the pass through status will also be granted to investors in Category I and II AIFs for losses in the following manner:

- The business loss of the AIF will continue to be carried forward by it and not the investor.
- Losses other than business losses:
  - Losses as on 31 March 2019 will be available to the investor. These losses will be allowed to be carried forward for 'set off' by the investor for the unexpired period.
  - After 1 April 2019, such losses will only be available to investors if units are held for 12 months or more.
  - Irrespective of whether the losses are available to an investor, they will not be allowed to be carried forward by an AIF.

The following table summarises the taxability of each income stream:

<table>
<tr><th>Type of income</th><th>Taxability in the hands of Category I and II AIFs</th><th>Taxability in the hands of investors</th></tr>
<tr><td>Dividend</td><td>Exempt</td><td rowspan="3">Tax in an investor's hands at the applicable rates;
AIF to withhold tax:
At 10%, for all residents
At applicable rates for non-residents (except exempt income)</td></tr>
<tr><td>Capital gains</td><td>Exempt</td></tr>
<tr><td>Interest</td><td>Exempt</td></tr>
<tr><td>Business income</td><td>30% (plus applicable surcharge and cess)</td><td>No further tax for investors</td></tr>
</table>

Tax transparency enables investors to pay taxes, based on their individual status, rather than pay tax in India at 30% (with additional applicable surcharges and cesses). For non-residents, this also includes any benefits or concessions that may be available under a tax treaty between India and the country of residence of the investor.

Currently, no pass-through status has been accorded to Category III AIF, and accordingly, the general principles of trust taxation applies to it. Taxation of a trust depends on the nature of a transfer or contribution made by an investor (revocable or irrevocable), and whether beneficiaries and their respective interests in the AIF are identified or determined upfront (determinate or indeterminate trust) and the nature of activity undertaken by the AIF (i.e. whether any business activity has been undertaken).

From the perspective of exchange control in India, foreign investment is permitted in AIFs under the automatic route. Furthermore, there are no restrictions on downstream investments by AIFs if the sponsor or investment manager of the AIF is not controlled and owned by resident Indian citizens. In this scenario, AIFs are regarded as Indian resident vehicles, regardless of their investor base. As Indian resident vehicles, AIFs have no restrictions on their choice of investment instrument and sectors in which they can invest. Where the sponsor or investment manager of an AIF is not owned and controlled by an Indian, it is treated as a 'nonresident'. In this case, the AIF's investments are subject to India's prevailing Foreign Direct Investment policy.

Furthermore, AIFs are permitted to make overseas investments, subject to certain conditions.

Foreign Portfolio Investors (FPIs)

In a bid to encourage and simplify foreign portfolio investments in India, the SEBI introduced FPI Regulations in 2014, which considerably eased entry-related norms for access growing Capital Markets in India. The FPI regulations replaced the erstwhile SEBI Foreign Institutional Investor Regulations and Qualified Portfolio Investors framework.

An FPI has been defined to mean a person who satisfies the prescribed eligibility criteria and is registered under the FPI Regulations. The primary condition for applicants desirous of seeking FPI registration is that they should not be resident in India or non-resident Indians.

FPIs are divided into three categories, based on the perceived risk attached to each category:

Category	Type of investors
Category I (low risk)	Government and government-related investors such as central banks, governmental agencies, sovereign wealth funds and international or multilateral organisations or agencies
Category II (moderate risk)	a) Appropriately regulated* broad-based funds such as mutual funds, investment trusts and insurance companies b) Unregulated broad-based funds, which are able to register if their investment managers are appropriately regulated c) Mutual funds, investment trusts, insurance and reinsurance companies d) Banks, asset management companies, investment managers or advisors, portfolio managers, university funds and pensions funds
Category III (high risk)	Residuary category, such as endowments, charitable societies, charitable bodies, foundations, corporate bodies, trusts, individuals** and family offices

**Regulated or supervised by the banking regulator or the securities market regulator of home country or another country (Need for regulator to permit investment-related activities in India)*

*** Non-resident Indians not permitted to register as FPIs, but can invest in FPIs subject to certain conditions*

FPIs invest primarily in listed Indian securities such as shares, perpetual debt instruments, government securities, commercial papers, unlisted non-convertible debentures (subject to certain conditions), security receipts, derivatives, units of mutual funds, real estate and infrastructure investment trust, Indian depository receipts, overnight index swap, interest rate swap, etc. Notably, FPIs cannot invest in unlisted equity shares. The following policy announcements were made in the Union Budget 2019:

1. FPIs will be allowed to subscribe to listed debt securities issued by Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs) that are collectively referred to as Investment Trusts.
2. FPIs will be allowed to transfer or sell debt securities issued by Infrastructure Debt Fund-NBFCs to any domestic investors within the lock-in period.
3. The FPI investment limit has been increased from 24% to the permitted sectoral limit at the option of the concerned investee company.

FPIs can also invest in securities listed on a stock exchange located in an Financial Service Centre (IFSC) in India. SEBI-registered FPIs can invest through IFSC without additional documentation and/or prior approval. Presently, certain derivative products are listed on the IFSC stock exchange.

With respect to debt investments, in consultation with the SEBI, the RBI has made certain changes in the operations of FPI investments. The key changes include ease in minimum residual maturity period, increase in limit for investment in government securities and discontinuation of the auction mechanism. The RBI has also imposed concentration- and investor-related limits.

Furthermore, the RBI, in consultation with the Government of India and the SEBI, has introduced a separate scheme, called the Voluntary Retention Route (VRR), to enable FPIs to invest in debt markets in India, free of the macro-prudential and other regulatory norms applicable to FPI investments in debt markets.

FPIs are subject to a special tax regime under Indian tax laws. The tax rates applicable to the typical income streams earned by an FPI are as follows:

Nature of income	Rate of tax (%)
Dividends declared, distributed or paid	Nil
Interest other than interest on government securities and Indian Rupee-denominated bonds of Indian companies	20
Interest on government securities and Indian Rupee-denominated bonds up to 30 June 2020 (subject to prescribed conditions)	5
Short-term capital gains on: • Listed securities on which Securities Transaction Tax has been paid	15
• Other securities	30
Long-term capital gains	10
Business income and any other income	40 – (corporate FPI) 30 – (non-corporate FPI)

The tax rates mentioned above need to be increased by applicable surcharge and cess. The tax regime (mentioned above) will be subject to any relief the FPI may be entitled to under the applicable tax treaty.

Furthermore, capital gains arising to FPIs from transactions undertaken on IFSC stock exchanges are exempt from tax in India.

Asset Reconstruction Companies (ARCs)

Asset reconstruction companies were conceptualised as a specialised vehicle under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act) with a view to facilitate resolution of the non-performing loans of banks and financial institutions.

ARCs are authorised to take non-performing loans from banks and financial institutions and securitise these loans under a securitisation trust structure. They act as the trustee and manager of securitisation trusts.

In view of the gravity of the problem of rising Non-Performing Assets (NPAs), the Indian Government has brought about several changes in relation to ARCs. FDI of up to 100% is permissible under the automatic route in setting up ARCs. The SARFAESI Act was amended to liberalise various conditions regarding setting up of ARCs and their operational aspects. In addition, FPIs are allowed to acquire security receipts issued by securitisation trusts set up by ARCs without any limit with regard to the proportion of investments.

From the Income-tax perspective, securitisation trusts set up by an ARC to hold stressed loans are given a complete pass through status. The income earned by such trusts is exempt from tax and is taxed in the hands of the contributor-beneficiaries directly. This should ensure a single-level taxation regime vis-à-vis the investment structure.

It seems to be a fallout of the various steps taken by the Government and regulators that interest in ARCs has increased significantly over recent years. Of the 29 ARCs registered with the RBI so far, about 15 have obtained registrations in the last three years.

Separately, from a macro perspective, the Indian stressed assets space has emerged as an attractive destination for global private equity and strategic investors. Several path-breaking reforms undertaken by the Indian Government and regulators, coupled with successes seen under the new Insolvency and Bankruptcy Code, 2016 (IBC) regime, have caught the attention of several investors, who seem to be confident about the overall turnaround potential of Indian borrowers.

Real estate investment trusts and infrastructure investment trusts

Infrastructure and Real Estate are the two most critical sectors in any developing economy. A well-developed infrastructural setup propels the overall development of a country. It also facilitates steady inflow of private and foreign investments, and thereby augments the capital base available for the growth of its key sectors as well in a sustained manner. A robust Real Estate sector, comprising sub-segments such as housing, retail, hospitality and commercial projects, is fundamental to the growth of an economy and helps several other sectors develop significantly through the multiplier effect.

However, both these segments need a substantial amount of continuous capital for their development. In view of their importance in India and the paucity of public funds available to stimulate their growth, it is imperative that additional channels of finance are put in place. Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs) are investment vehicles that can be used to attract private investment in the Infrastructure and Real Estate sectors, and also relieve the burden on formal ban king institutions.

S. no.	Key stakeholders	Features/Benefits
1	Sponsor (person who sets up a REIT)	Generally developers or financial investors Exit opportunities for developers Availability of last-mile funding for stalled projects
2	Investors	Participation in asset class not easily accessible Diversification of investment holdings helping in management of overall risk Ease of entry and exit option for investors in the Real Estate sector

Key aspects of SEBI's regulations

The main eligibility criteria for setting up of Investment Trusts

To set up an Investment Trust, the sponsor needs to meet the following criteria and have the following:

- Asset size of INR 5,000 million
- Offer size of INR 2,500 million
- Minimum public float 25% (other than private InvITs)
- Minimum number of investors —200 in the case of REITs and 20 in the case of public InvITs

Furthermore, the sponsor is required to make a contribution, as prescribed under SEBI's regulations, in order to set up an Investment Trust.

Regular distribution of cash flows

Investment trusts need to distribute a significant portion of their net distributable cash flows as dividends to unit-holders on a regular basis.

Foreign investments in Investment Trusts

Foreign investments in Investment Trusts have been allowed by the Government in an attempt to provide Indians additional avenues from which they can access funds. Investments in Investment Trusts have been allowed through the FDI route by the introduction of the concept of an ‘investment vehicle’, which *inter alia* includes REITs and InvITs. While FDI is prohibited in the ‘real estate’ business, in order to enable foreign investments in REITs, it has been specifically excluded from the definition ‘real estate business’. As mentioned above, FPIs will be allowed to subscribe to listed debt securities issued by Investment Trusts.

Similar to AIFs, the sponsor, investment manager and asset manager of an investment trust is owned and controlled by an Indian citizen or citizens. An investment made by an investment trust in special purpose vehicles is treated as domestic investment. Moreover, sale, redemption or repatriation of the units of investment trusts is permissible under the automatic route.

Overview of taxation of investment trusts

	Setup	Income recognition & distribution	Exit
Sponsor **Investor**	Capital gains - Exempt# MAT deferred	Dividend – exempt^ Interest – taxable (Domestic @ 30%, Foreign @ 5%)	STCG -15% LTCG – 10% (without indexation)## (equity shares + units, held for more than 36 months in aggregate)
Investment Trusts		Tax exempt^ WHT on interest paid	Gains on sale of securities - taxable
Asset SPV		Income Tax / MAT / AMT No DDT* (in case of single-tier structure) No WHT on interest	Gains on sale of assets - taxable

 # On exchange of shares of company for REIT units

^ exposure of dividends above INR 10,00,000 being taxed at 10%

on gains above INR 100,000

**Dividend Distribution Tax (DDT) is not applicable if Investment Trusts holds 100% of equity share capital of the Asset SPV and dividend is paid out of current income*

Note: Rates are excluding surcharge and education cess

7

Mergers and Acquisitions (M&A)

India's M&A framework

India's regulatory framework facilitates acquisitions, transfers or hive-offs through different modes, each with its distinct tax-related characteristics and varying regulatory ease of conducting deals. Common modes of executing transactions include:

- Share purchase
- Business or asset purchase
- Amalgamations or demergers

Transactions through share transfer

Implications for sellers

Transfer of the shares of an Indian company is taxable as capital gains, subject to any tax treaty-related benefits that may be available for a seller. Taxability varies for listed and unlisted shares. This is summarised in the table below:

Nature of capital gain	Unlisted shares/shares of private company	Listed shares
Long Term Capital Gains (LTCG) (gains from shares held for more than: *12 months* in the case of listed shares *24 months* in the case of unlisted shares	For residents – *20%[1] (with indexation)* For non-residents – *10%[1] (without indexation and the effect of conversion of currency)*	• If sold through a stock exchange: Gains in excess of INR 100,000 will be taxable in the hands of residents and non-residents at the rate of 10%[1] *(without indexation).* However, gains up to 31 January 2018 are grand-fathered and exempt. • If sold by other means than a stock exchange: – Resident – *10%[1] (without indexation) and 20%[1] (with indexation), whichever is beneficial to the taxpayer* – Non-residents: • When acquired in foreign currency – 20%[1] (without indexation, but with the benefit of currency conversion available) • When acquired in INR – 10%[1] (without indexation) and 20%[1] (with indexation), whichever is beneficial to the taxpayer
Short Term Capital Gains (STCG) (gains that do not qualify as long term gains)	For resident companies, LLPs and firms – *30%[1] and 25%[1] (in the case of companies with a turnover of up to INR 250 crores in the previous year– 2016-17)* For resident individuals – taxable according to applicable slab rates For non-resident companies – *40%*	• If sold by paying Securities Transaction Tax – *15%[1]* • If sold otherwise – tax implications similar to treatment of sale of unlisted shares

The Income-tax Law includes anti-abuse provisions wherein there is additional taxation both in the hands of the seller and the buyer on the difference between the fair market value (FMV) and the sale consideration on transfer of unquoted equity shares at lower than their FMV in the manner prescribed. For example, where an asset is sold at lower than its FMV, the seller has to pay additional Capital Gain Tax of 23.3% and the buyer needs to pay a recipient tax of 35% on the difference between the FMV and the sale consideration.

However, it has been proposed in the Finance Bill, 2019 that these anti-abuse provisions should be amended to empower the Central Board of Direct Taxes (CBDT) to restrict the applicability of prescribed transactions undertaken by a prescribed class of persons to eliminate the issues faced by them.

Taxability of indirect transfer

Transfer of the shares of a foreign company with underlying assets in India is also taxable in the hands of the seller in India, if the shares of the company derives substantial value from its assets in India (i.e. the fair market value of Indian assets (a) exceeds INR 10 crore and (b) represents at least 50% of the value of all the assets owned by the company, as prescribed).

However, no taxation on indirect transfer applies if the transferors hold minority stakes (of 5% or less) and have no right of management or control in the foreign company. Additionally, in the event of a merger or demerger of the foreign company, exemption from Capital Gains Tax is available in India on fulfilment of the prescribed conditions.

Implications for buyers

- According to SEBI's Takeover Code, acquisition of 25% shares (or more) or control of a listed company obligates the acquirer to make an offer to its remaining shareholders.
- Funding costs, i.e. interest charged on a loan for acquisition of shares, may not be tax-deductible, since the corresponding income from dividends is tax-exempt in the hands of the shareholders.
- In the case of non-resident sellers, a buyer (including a non-resident) is required to withhold Indian tax arising to the sellers, and therefore, needs to obtain a tax registration number in India. The parties can seek clarity on the aspects of Withholding Tax by obtaining a No Objection certificate from the Tax authorities in advance.
- Furthermore, it was proposed in the Finance Bill, 2019 that income of the nature referred to in section 2(24)(xviia) of the Act received by a non-resident on or after 5 July 2019 from a resident, without or for inadequate consideration will be deemed to accrue or arise in India.

Stamp Duty

- Stamp Duty at 0.25% of the value of the shares is levied if they are physically transferred.
- The Interim Finance Bill 2019 proposed to levy Stamp Duty at the rate of 0.015% on transfer of shares (whether physical or dematerialised) on the value of the consideration mentioned in the instrument.

Preservation and carry-forward of tax losses on a change in shareholding[29]

- There is no impact on the carry forward or set off of losses on a change in the shareholding of a listed company.
- Unlisted companies are not entitled to carry forward and set off their tax business losses (excluding unabsorbed depreciation), if any, if there is a change of 50% or more in their shareholding.
- However, the recent amendments made in the Income Tax Act allow an exception if a shareholding changes on account of a resolution plan approved under the Insolvency and Bankruptcy Code.

Valuation of shares

The RBI regulates the pricing of every transaction between residents and non-residents in the shares of an Indian company. It has standardised the valuation methodology so that the parties can value the shares according to internationally accepted methodologies.

29. Provisions not applicable on unabsorbed depreciation

Business or asset purchase model

In India, businesses can be acquired through (a) the asset purchase model, where the buyer can cherry-pick the assets, leaving the liabilities and certain other assets behind with the seller entity or (b) the business purchase model, where the buyer acquires an entire business undertaking, with all its assets and liabilities, for a lump sum consideration on a going-concern basis.

Asset purchase model

Implications for the seller

- Gains are individually computed for every asset and are taxable as a short-term capital gain (STCG) or long-term capital gain (LTCG), depending on the period during which they were held. Sale of depreciable assets always results in STCG. Gains for all assets other than capital assets are taxable as business income.
- Capital gains are determined by reducing the acquisition cost of assets from the sale consideration. In the case of LTCGs, the cost of acquisition is indexed, based on the cost inflation index notified by the tax authorities every year. For self-generated intangible assets, the cost of acquisition is taken as 'nil' for calculation of capital gains.
- On transfer of movable property, the seller is liable to charge the Goods and Services Tax (GST) at specified rates.
- If the sale consideration is less than its FMV on transfer of immovable property, the FMV is deemed to be the value determined by the stamp valuation authorities on the date of the agreement.

Implications for the buyer

- On transfer of immovable property, buyers are liable to pay stamp duty at the rate applicable in the state in which the property is located.
- Depreciation can be claimed on the purchase value of assets acquired.

Stamp Duty

- Stamp Duty may also be chargeable on transfer of movable property.

Business purchase model

Implications for the seller

- Capital gains are determined by reducing the net worth of a business undertaking (determined in the manner prescribed) from the sales consideration.
- Capital gains are taxable as LTCGs if the business undertaking is held for more than three years. However, no indexation benefit is available.
- Capital gains are taxable at 20%[1] if long term or at 30%[1] if short term.
- Business transfers on a 'going concern' basis are not subject to the GST.

Implications for the buyer

- The purchase cost in the hands of the buyer is computed by allocating the lump sum purchase consideration along with the value of the liabilities proportionately on each asset on the basis of its fair value.
- Interest on loans taken for acquisition of assets or business undertakings through a slump sale is generally tax-deductible.
- Expenses incurred in connection with business purchase are not deductible as business expenditure.
- In the case of a business purchase, the tax losses of the business undertaking are not transferred.

Amalgamations and demergers

In some situations, an acquired or to be acquired entity can be integrated into the buyer's group through an amalgamation or demerger. The procedure for this is governed by specific provisions in the Companies Act, 2013, and typically requires the approval of the National Company Law Tribunal (NCLT).

Amalgamations and demergers normally attract Stamp Duty at varying rates prescribed in state laws. Clearance may be needed from other statutory authorities such as stock exchanges and the Securities Exchange Board of India (SEBI) in the case of a listed company, the RBI and other regulatory bodies. An amalgamation or demerger may be tax-neutral when it is compliant with the prescribed conditions. The following are the relevant provisions:

Basis	Amalgamation	Demerger
Definition under Income-tax Act	Merger of one or more companies with another company, or merger of two or more companies to form one company, subject to the following conditions: • All the assets and liabilities of the transferor should be transferred to the transferee. • Shareholders holding at least 75% of the shares (in value) in the transferor become shareholders in the transferee company.	Transfer by a demerged company of one or more of its undertakings to any resulting company pursuant to the scheme of arrangement under Section 230-232 of the Companies Act, 2013, subject to the following conditions: • All the assets and liabilities of the transferor's business undertaking are transferred to the resulting company at its book values. • Shareholders holding at least 75% of the shares (in value) in the demerged company become shareholders in the resulting company. • The consideration is discharged by issuance of the shares of the resulting company to the shareholders of the demerged company on a proportionate basis. • The transfer is on a 'going concern' basis.
Carry forward of losses and unabsorbed depreciation	If the amalgamating company owns an industrial undertaking, its losses and unabsorbed depreciation is to be carried forward by it, provided specified conditions, e.g. continuance of business and holding of assets, are met.	Accumulated losses or unabsorbed depreciation directly related to the undertaking being demerged are transferable for the unexpired period. Proportionate common losses are also transferable.

Cross-border mergers

The Ministry of Corporate Affairs (MCA) has notified the provisions for cross-border mergers under the Companies Act, 2013.

Bringing about a significant change from the old regime under the Companies Act, 1956, where only the merger of a foreign company with an Indian company was permitted (i.e. inbound mergers), the notified provisions of the Companies Act, 2013 confer a legal status on both inbound and outbound mergers.

Outbound mergers (i.e., the merger of an Indian company with a foreign one) are only permitted if the foreign company is incorporated in the specified jurisdiction.

Valuation of the Indian company and the foreign company should be conducted by valuers who are members of a recognised professional body in the jurisdiction of the transferee, and such valuation is in accordance with internationally accepted principles of accounting and valuation.

Any transaction on account of a cross-border merger undertaken in accordance with Foreign Exchange Management (Cross Border Merger) Regulations, 2018 is deemed to have the approval of the RBI, as required under the provisions of the Companies Act, 2013.

In the Union Budget 2019, the Government reiterated its thrust on ‘minimum government and maximum governance’, and its continuing focus on ‘ease of doing business’ and promotion of start-ups. Moreover, it has proposed tax amendments to make its goals a reality. The Government’s initiatives will go a long way in ironing the creases in tax laws and should open new avenues for the different industries in India.

8

Transfer Pricing

Globalisation is one of the most crucial aspects of the commercial world. With the integration of the global economy, more and more multinational enterprises (MNEs) are making foreign direct investments and establishing subsidiaries abroad. This expansion requires transfer of tangible and intangible goods and/or services between related group entities. Consequently, pricing of such cross-border transactions has become a critical issue.

A separate code for Transfer Pricing (TP) has been applicable in India since 1 April 2001 under sections 92 to 92F of the Indian Income-tax Act, 1961 (the Act). The code mandates that pricing of international related party transactions between related parties needs to be computed with regard to the Arm's Length Price (ALP). The ALP is broadly based on the guidance provided under the Organisation for Economic Cooperation and Development's (OECD's) TP rules for MNEs. The rules elaborate on various TP methodologies and include robust documentation-related requirements.

TP is not an exact science and has been evolving over a period of time. It is one of most contentious and litigious areas of taxation. Furthermore, Indian revenue authorities have been recognised as one of the most aggressive in the world that stringently scrutinise cases. To address this issue, the Government of India has introduced a number of dispute resolution mechanisms in the recent past to curb TP-related litigation and provide much needed certainty to stakeholders. Moreover, Indian courts have passed judgments on complex issues pertaining to TP, such as marketing intangibles, intra-group services and financial transactions.

To tackle the issue of Base Erosion and Profit Shifting (BEPS), the OECD and a group of 20 major economies (G20) have published the BEPS Action Plan. The Plan comprises 15 action items, which include interest deduction, Permanent Establishment and guidance on three-tier TP documentation.

Detailed below are the key TP-related highlights of the Financial Year (FY) 2018-19:

Bilateral Competent Authority Agreement (BCAA) for exchange of CbC report signed between India and the USA[30]

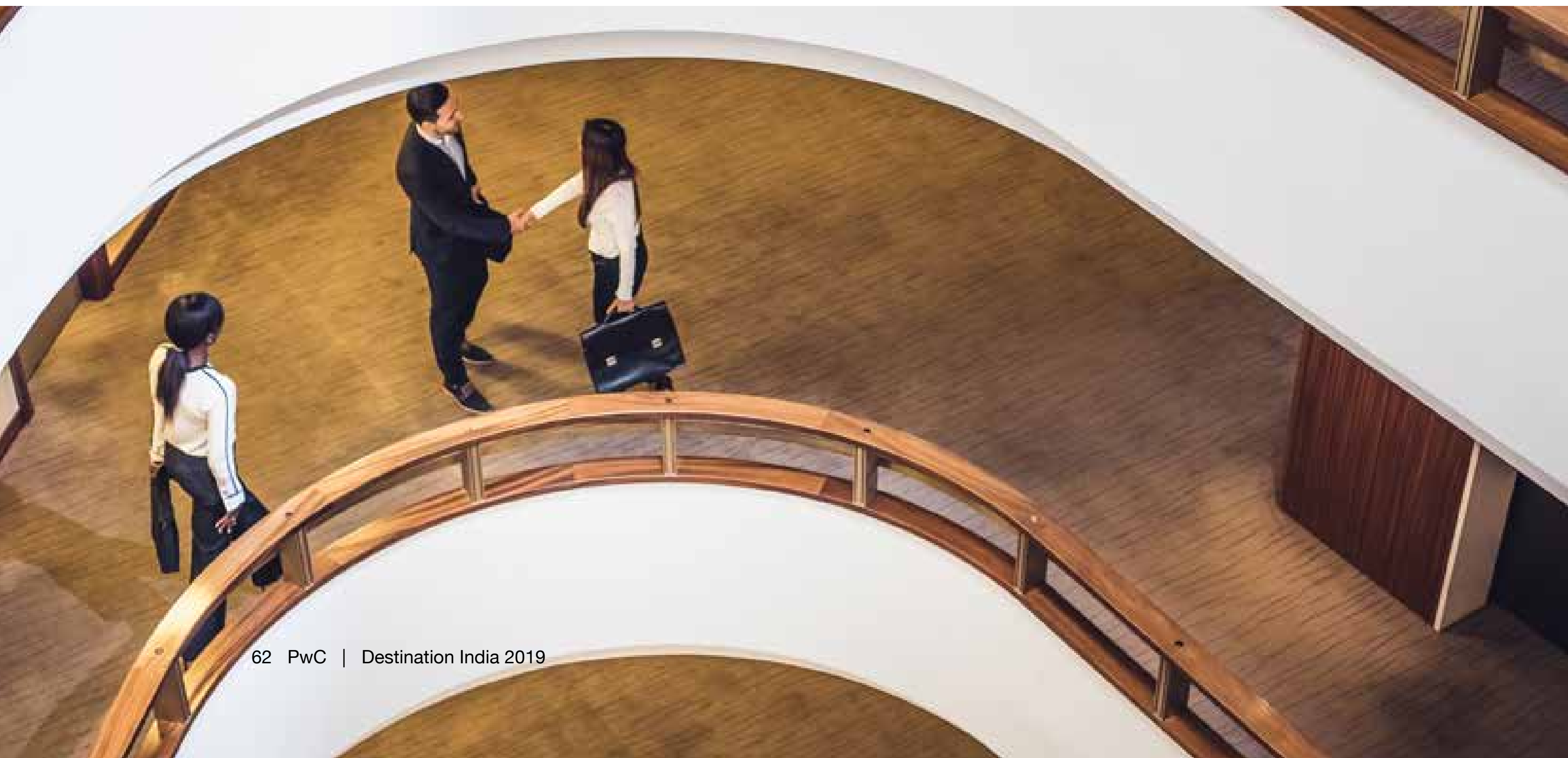
On 27 March 2019, India and the US signed an inter-governmental agreement for exchange of CbC reports. This has enabled the countries to automatically exchange CbC reports pertaining to years commencing on or after 1 January 2016 that have been filed by the ultimate parent entities of MNEs in their respective jurisdictions. This will eliminate duplication and compliance-related issues, since the Indian subsidiary companies of US MNEs will not be mandatorily required to file CbC reports in India.

India has also signed the Multilateral Competent Authority Agreement (MCAA) for exchange of CbC reports. This has led to exchange of CbC reports between India and 62 jurisdictions.

General Anti-Avoidance Rules (GAAR)

GAAR codifies the principle of substance over form and brings into law principles that several landmark cases have dealt with over the years. An Impermissible Avoidance Arrangement (IAA) has been defined, but only for transactions where the main purpose is to obtain a tax benefit.

30. www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/751/PressRelease_Signing_Inter__India_USA_27_3_19.pdf



GAAR provisions apply to investments made after 1 April 2017 and are applicable for arrangements where tax benefits exceed INR 30 million. Once GAAR is invoked, tax treaty benefits may be denied for such arrangements.

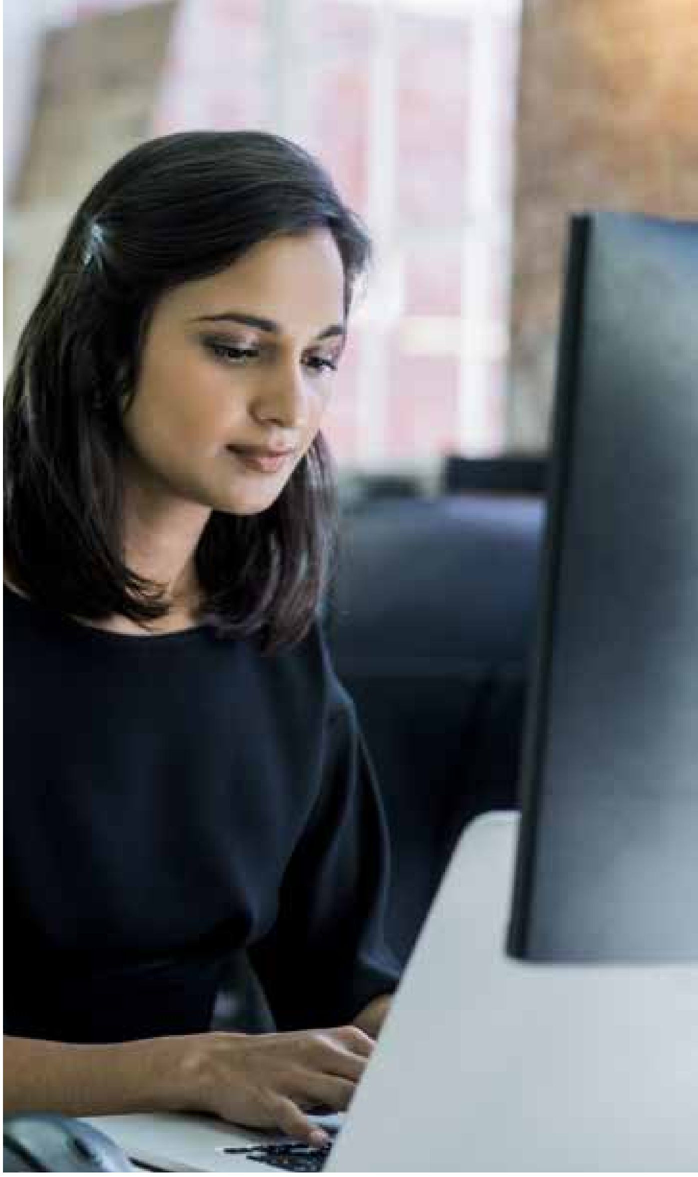
Thin Capitalisation

India has always demonstrated its commitment to OECD's BEPS initiative and introduced several reforms in its domestic tax legislation. Its intention has always been to plug existing loopholes, strengthen information-sharing between contracting states and help to prevent double non-taxation. In line with its commitment, the Indian Government had earlier introduced measures to curb thin capitalisation in India. In other words, there is a limit on deduction of interest-related expenditure incurred by an Indian company or a permanent establishment of a foreign company in India. As a rule, there is a 30% Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) cap on claims for payment of interest to overseas related parties. Excess interest that is disallowed in one year will be eligible for carry forward up to eight consecutive years. However, it is pertinent to note that this provision is only applicable when the interest-related expenditure exceeds INR 1 crore.

TP audits

Some key issues scrutinised during TP audits include international transactions such as the creation of marketing intangibles, management cross charges and financial transactions. The following are some of our observations on recently concluded TP audits:

- **Advertising, Marketing and Promotion (AMP) expenses:** AMP is one of the hot topics in India's TP litigation scenario today. Indian TP Officers (field officers) claim that Indian taxpayers are helping their parent or group entities create or promote the brand names owned by the parent entities, which leads to the creation of marketing intangibles. Field officers expect Indian taxpayers to earn an appropriate arm's length return for assistance provided for the creation of marketing intangibles. Several taxpayers have filed Special Leave Petitions before the Supreme Court, challenging the rulings of lower courts, claiming that incurrence of AMP by taxpayers cannot be considered an international transaction. However, despite the courts' decisions in some of the cases, Indian field officers are trying to make additions to increase AMP expenses on different counts.



- **Managements' cross charges:** Justification of the arm's length price of managements' cross charges is a subjective area that has made such transactions litigious. Indian Revenue authorities insist on provision of need- and benefit-related documents that furnish evidence of receipt of such services and claims that the arm's length price is nil. And although it has been decided in multiple judicial precedents that the Revenue authorities cannot object to the commercial expediency of such services, field officers continue to raise queries on their business need.
- **Corporate Guarantee Fee:** This is one of the most highly disputed issues faced in the battleground of TP litigation. Income-tax authorities often accept external comparable guarantee rates provided by banks as the comparable uncontrolled price for benchmarking guarantee fee-related transactions. However, at the Tribunal level, a bank guarantee, generally referred to as a 'naked guarantee', has been differentiated from corporate guarantees. Tribunals have held that 'naked quotes' need to be adjusted for factors including risks, functions, terms and periods, and cannot be directly compared with corporate guarantee transactions.

Advanced Pricing Agreement (APA)[31]

On 3 April 2019, the Central Board of Direct Taxes (CBDT) issued a press release on APA for FY 2018-19. The press release highlighted some of the key aspects of the Indian APA regime, claiming that the total number of concluded APAs had reached 271, of which 240 were unilateral APAs and 31 bilateral APAs. Among the signed APAs, FY 2018-19 witnessed signing of 52 APAs (41 unilateral APAs and 11 bilateral APAs). According to the press release, taxpayers should be upbeat about the continuing efforts of the CBDT to expedite conclusion of APAs.

There were a number of fresh APA applications filed by taxpayers during FY2018-19. The APAs entered during this period pertain to various sectors and sub-sectors of the economy, e.g. BPOs, IT/ITes, risk management solution platforms, and industrial and institutional cleaning and hygiene products.

A noteworthy development is the shift in focus from unilateral APAs to bilateral APAs. The progress made in implementation the APA scheme has strengthened the Government's resolve to foster a non-adversarial tax regime. India's APA programme has been appreciated in the country and around the world for its ability to address complex TP-related issues in a fair and transparent manner.

Country-by-Country (CbC) Report

The Indian Government had introduced a three-tier TP documentation process, and taxpayers are now required to prepare master files, local files and CbC reports.

CbC report-related requirements are applicable for international groups with consolidated revenue exceeding INR 55, 000 million in the preceding year. The timeline for furnishing a CbC report is 12 months from the end of the reporting accounting year, compared to the earlier timeline of the return filing date. A CbC report needs to be filed in India by the Indian affiliates of MNEs headquartered abroad if they are not required to file it in their home jurisdictions, and the parents have not designated any 'Alternate Reporting Entity' outside India.

Key proposals in Union Budget 2019

Provisions related to secondary adjustment

Provisions relating to secondary adjustment stipulate that in specific cases of primary TP adjustment (voluntary adjustment, adjustment in pursuance of an APA/Safe Harbour/Mutual Agreement Procedure or adjustments accepted by taxpayers), the primary adjustment amount is not repatriated to India. In this case, interest is to be imputed on the primary adjustment (according to the specified method) and taxed in India. The following amendments have been proposed in section 92CE of the Income Tax Act, 1961 to address concerns relating to effective implementation of these provisions:

- The amendments clarify that these provisions do not apply if the primary adjustment does not exceed INR 10 million or the amount pertains to AY 2016-17 or earlier years. These two conditions are not cumulative.
- It is proposed that interest should be imputed on the primary adjustment or part thereof that is not repatriated to India.
- There is a proposal that relief should be provided for secondary adjustment for APAs signed before 1 April 2017. However, taxes already paid under existing provisions will not be refunded.
- The primary adjustment amount may be repatriated from any Associated Enterprise (AE) that is not resident in India and not necessarily from transacting AEs.
- It is proposed that taxpayers should be given the option to pay additional Income-tax at 18% of the primary adjustment in addition to a 12% surcharge and not be taxed on the imputed interest. This additional tax will not be allowed as a deduction nor will credit be allowed against a tax liability.

The first four amendments mentioned above are clarificatory in nature and have been effective from AY2018-19 onwards. The last amendment will be effective from 1 September 2019.

31. www.incometaxindia.gov.in/Lists/Press%20Releases/Attachments/754/PressRelease_Indian_Advance_Pricing_Agreement_3_4_19.pdf

Tax Officers' powers in relation to modified return of income pursuant to APA

Section 92CD(3) of the Income-tax Act, 1961 deals with situations in which assessment or re-assessment has already been completed before expiry of the period allowed for filing modified returns pursuant to the APA for an Assessment Year (AY). According to the existing sub-section, the tax officer is to "assess, reassess or re-compute" taxable income for such years with regard to the APA. This has given rise to apprehensions in relation to fresh assessment or re-assessment of such cases.

It is proposed that this sub-section is amended to clarify that in such cases, tax officers will pass orders for modification of the relevant AY's total income, in accordance with the APA. Therefore, they will not have the power to initiate fresh assessments or re-assessments for such AYs. The amendment mentioned above will be effective from 1 September 2019.

Maintenance of Master File

Section 92D of the Income Tax Act, 1961 provides that taxpayers that are a part of an international group and have international transactions and a group turnover exceeding specified thresholds need to maintain and furnish their Master Files. This is a requirement under BEPS Action Plan 13, and encapsulates details of the supply chain and the key business drivers of the international group, among other important information.

It is proposed that the Tax Officer and Commissioner (Appeals) will not have the power to make a request for a Master File, which will need to be filed with the prescribed authority. The amendment given above will be effective from AY2020-21 and onwards.

Accounting year for Country-by-Country Report (CbCR) filing

Section 286 of the Income Tax Act, 1961 provides that when the parent entity or Alternate Reporting Entity (ARE) is resident in India, it is required to file its CbCR in India for the accounting year (the previous year). The CbCR, which is a part of the BEPS Action Plan 13 requirement, comprises the country-wide details of the revenue, profit, employees, etc. of an international group.

In respect of an ARE, there is a concern that since the parent entity is not resident in India, there should not be a need for the CbCR to be filed for the previous year. Instead, it should be filed on the basis of the parent's accounting year. Consequently, the Government seeks to amend this section by clarifying that in the case of an ARE, its CbCR will need to be filed on the basis of the accounting year of its parent entity. The amendment will take effect retrospectively from AY2017-18 and onwards.

Other key developments

India-Hong Kong Tax Treaty[32]

India signed its Double Taxation Avoidance Agreement (DTAA) with the Hong Kong Special Administrative Region (HKSAR) Authorities on 19 March 2018. The agreement came into force from 30 November 2018. It is expected to stimulate the flow of investment, technology and personnel between India and the HKSAR, prevent double taxation and facilitate exchange of information between the two countries. And most importantly, it will increase transparency in tax-related matters and help curb tax evasion and avoidance.

India-China Tax Treaty[33]

On 26 November 2018, India and China signed a protocol to amend the existing DTAA between the two countries to check tax evasion. The protocol inter-alia updates existing provisions for exchange of information according to international standards. It also incorporates changes required for implementation of the minimum standards (relating to the treaty) prescribed under the 'action report' of the BEPS project, which enables enhanced transparency in tax-related information pertaining to MNEs on a country-by-country basis.

32. https://taxguru.in/income-tax/dtaa-india-hong-kong.html
33. http://pib.nic.in/newsite/PrintRelease.aspx?relid=185951

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