TED: Insights on India Taxation

Explore Tax Implications for Businesses Investing in India

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India is set to remain as one of the bright spots of the uncertain world economy. The country's gross domestic product is expected to grow by 7.1%[1] in 2017, beating previous forecasts.

As foreign enterprises consider tapping into the huge Indian market, it is key to first understand the focus and mindset behind the wave of developments in order to benefit from the vast opportunities in the world's second most populated country. This was the overarching tip Accredited Tax Advisor (Income Tax) Rohan Solapurkar, Tax Partner, Deloitte Singapore, highlighted at a recent *Tax Excellence Decoded* session organised by the Singapore Institute of Accredited Tax Professionals (SIATP).

Infrastructure and manufacturing were two key focus areas in this year's India Budget. Foreign investments (FIs) in infrastructure, particularly in affordable housing, modernisation of transportation networks especially in rail and air transport, and high-speed broadband connectivity, are encouraged. To facilitate FIs, it was, for example, proposed that affordable housing be given infrastructure status. This would allow investors to gain easier access to credit, hence lowering the costs of borrowing for affordable housing projects. Other significant Budget proposals included the further liberalisation of the foreign direct investment (FDI) policy and the provision for INR100 billion (approximately S$2.18 billion) for recapitalisation of banks.

Forms of Business Presence in India

Foreign investors can set up a business presence in India using unincorporated entities (such as project office, liaison office or branch office), incorporated entities (such as subsidiary or joint venture) or limited liability partnerships (LLP). Of the six types of entities, Singapore investors may be less familiar with project office and liaison office.

In India, a project office can execute a specific project after its foreign parent has secured a contract from an Indian company. Upon completion of the project in India, the income generated by the project office will be taxed in India before the project office is closed down.

A liaison office, on the other hand, is a representative office and is not allowed to undertake any business activity or earn any income in India. It is in fact India's version of Singapore's representative office and acts as a channel of communication between its foreign Head Office and parties in India.

[1] Archana Chaudhary and Shruti Srivastava (2017) "India GDP to Slow Less Than Estimated As Cash Returns to Economy" (28 February 2017), Bloomberg; www.bloomberg.com

CORPORATE INCOME TAX

The effective corporate income tax rate for an Indian company with turnover of less than INR500 million has reduced from 34.61% to 28.84% since financial year (FY) 2015-16, while the effective rate for an Indian company with turnover of at least INR500 million and that for an LLP remains at 34.61%.

Unlike an Indian company or LLP, a foreign company with a taxable presence in India through a branch office, project or permanent establishments (PE) will continue to be subject to a tax rate of 43.26%.

CAPITAL GAINS TAX

Profits and gains derived from the disposition of capital assets other than those held for business purposes are taxed in India as capital gains. Starting from FY 2017-18, the minimum holding period to qualify as a long-term asset (which is generally subject to a lower tax rate) has been reduced from 36 months to 24 months for immovable property (being land or building or both).

GENERAL ANTI-AVOIDANCE RULE

The general anti-avoidance rule (GAAR) provisions will be effective from FY 2017-18. Essentially, the objective of GAAR is to deny tax benefits to any arrangement which has been entered into with the main purpose of obtaining tax benefits and which lacks commercial substance.

It has been clarified that if the law allows the taxpayer to select between two alternatives of implementing a transaction, GAAR cannot be invoked by the tax authorities to challenge the taxpayer's choice. It is also clarified that GAAR will not be invoked merely because the taxpayer is located in a tax-efficient jurisdiction.

Accredited Tax Advisor (Income Tax) Rohan Solapurkar, Tax Partner, Deloitte Singapore, shared his insights on the Indian tax system and recent updates.

INCENTIVES FOR MANUFACTURING

Foreign investors looking to set up manufacturing facilities in India should consider the plethora of tax and non-tax incentives offered by the Indian federal as well as state governments to set up and grow their business in India.

For example, the federal government allows enhanced tax deduction on additional wages paid to workmen, research and development expenses, investment in plant and machinery, etc, to incentivise the setting-up of manufacturing facilities. Separately, the state governments may (depending on the specific state) offer stamp duty exemption on transactions, tax incentives on value-added tax or even lower utility charges. Special economic zones with a myriad of incentives have also been set up in various states, attracting investments from different clusters of business sectors.

AMENDMENT TO THE DTA BETWEEN INDIA AND SINGAPORE

Following the amendment to the Avoidance of Double Taxation Agreement (DTA) between India and Mauritius to give India the taxing rights to capital gains arising from the sale of shares, the India-Singapore DTA has also been amended such that India will now have the right to tax capital gains arising from the sale of shares in an Indian company (if such shares have been acquired on or after 1 April 2017). As a transitional measure, a lower tax rate (at 50% of the capital gains tax rate) will apply for shares acquired on or after 1 April 2017 if such shares are sold before 1 April 2019. Full capital gains tax rate will apply for shares sold after 1 April 2019.

Separately, the India-Singapore DTA introduced an article which allows taxpayers to settle transfer pricing disputes through Mutual Agreement Procedure (MAP) or Bilateral Advance Pricing Agreement (APA). The new avenues for dispute resolutions will surely be welcomed by Singapore companies investing in India.

MOVE TOWARDS GOODS & SERVICES TAX

India is expected to introduce the long-awaited Goods & Services Tax (GST) in 2017. Various indirect taxes currently levied on goods and services by the central and state governments (such as excise duty, service tax, sales tax, value-added tax and entry tax) will be subsumed into the GST.

A dual GST model will be adopted where the central and state governments will concurrently levy the Central GST and State GST respectively on each transaction of supply of goods and services. It is expected that there will be four GST rates ranging from 5% to 28%. The lower rates are for essential items and the highest rate is for luxury and demerits goods (such as tobacco).

While the move towards GST will no doubt reduce the complexity of indirect tax compliance in the long run, the magnitude of this change will mean that companies operating in India will have to invest significant time and money now to overhaul their existing accounting and sales systems to ensure compliance.

SIATP board member Yee Fook Hong (left) was one of the various participants who actively engaged Accredited Tax Advisor (Income Tax) Rohan Solapurkar, Tax Partner, Deloitte Singapore, in a technical discussion about India's current tax regime.

RECENT TAX RULING

In a recent Indian tax case, the issue before the Court was whether a US company, which has a liaison office in India, has a PE in India. While a liaison office should strictly not create a PE for its foreign parent (as they are not allowed to undertake any business activity or earn any income in India), the Indian tax authorities discovered that in this case, the employees of the liaison office had full control over the US company's sales activities in India. Accordingly, the Court held that the US company had a PE in India and the income attributable to the PE should be subject to tax in India.

This case highlights the importance for multinationals to monitor the actual activities carried out by their overseas entities. This is to ensure that the overseas entities do not inadvertently create a taxable presence for the multinationals in foreign jurisdictions.

As the Indian economy continues to shine, it may be difficult for investors to ignore its allure for long. The Indian government has continued to keep tax predictability and the ease of doing business in India as its key focus. As you get ready to set foot in India, think carefully and plan thoroughly. Seize the right opportunities and you may just be part of India's success story.

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This technical event commentary is written by Felix Wong, Head of Tax, SIATP. This article is based on SIATP's Tax Excellence Decoded session facilitated by Accredited Tax Practitioner (Income Tax) Rohan Solapurkar, Tax Partner, Deloitte Singapore.

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