

## **BUDGET 2015 NEWS FLASH – KEY PROPOSALS CONCERNING FOREIGN INVESTMENTS IN INDIA**

In his budget speech, the finance minister Mr. Arun Jaitley presented budget containing various policies and schemes with central target of eliminating poverty and upliftment of Indian youth from 'Job seeker' to 'Job creator'. With concentration on 'Make in India' & 'Skill India', the budget clearly conveyed idea of the government to increase public investment to catalyze private investment.

The government showed plan to decrease fiscal deficit from 3.9% in 2015 – 16 to 3.5% in 2016 - 17 to 3% in 2017 – 18. The Government has set goal at two digit growth rate which looks reasonably achievable with transparent economic policies and empowerment of manufacturing sector with additional development in R&D and Infrastructure.

The budget aims to take India to a fastest growing economy. The announcement of various policies and reform measures specifically for the foreign investors will surely make India a better place to invest and trade.

Some of the announcements concerning foreign investors are summarized below:

### **1. General**

- Establishment of a mechanism to be known as SETU (Self-Employment and Talent Utilization). SETU will examine all aspects of start-up businesses, and other self-employment activities, that could also address to concerns such as a more liberal system of raising global capital and ease of doing business in India. Appointment of an Expert Committee for the purpose of examining the possibility and preparing the draft legislation where the need for multiple prior permissions can be replaced with a pre-existing regulatory mechanism.
- Government to introduce appropriate regulation in March 2015 to establish International Finance Centre (IFC) at GIFT, Gujarat. It has been visualized that IFC should actually become as good an International Finance Centre as Singapore or Dubai.
- Setting up a Public Debt Management Agency (PDMA) which will have External Commodity Borrowings (ECB) and domestic debt under one roof. This will promote investments in India, including in the Indian infrastructure.

### **2. Foreign Exchange Regulations**

- Amendment to allow Foreign Investments in Alternative Investment Funds (AIFs).
- Proposal to do away with the distinction between different types of foreign investments. Foreign Portfolio Investments (FPI) and Foreign Direct Investments (FDI) to be merged with one composite route.

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- Amendments to Foreign Exchange Management Act (FEMA) to provide that control on capital flows as equity will be exercised by the government. This is to ensure that Capital Account Control is a policy, and not a regulatory, matter.

### 3. Direct Tax Proposals:

- No change to the existing income tax rates for foreign companies.
- Tax on Royalty and Fees for Technical Services (FTS)  
Rate of tax provided under section 115A on Royalty and FTS payments made to non residents has been reduced to 10% from 25%.
- Minimum Alternate Tax (MAT) Provisions for FIIs  
In order to rationalize the MAT provisions for FIIs, profits corresponding to its income from capital gains on transactions in securities, which are liable to tax at a lower rate, shall not be subject to MAT.
- Provisions of section 194LD of the Income-tax Act is amended to extend the period of applicability of lower rate of tax at 5% in respect of income of Foreign Investors (FIIs and QFIs) from corporate bonds and government securities from 31<sup>st</sup> May, 2015 to 30<sup>th</sup> June, 2017.
- General Anti Avoidance Rule (GAAR) has been proposed to be deferred by 2 years.
- Residential Status
  - ❖ It has been proposed to amend the provisions of section 6 to provide that a person being a company shall be said to be resident in India if its Place of Effective Management' (POEM) at any time, is in India. It is proposed to define the Place of Effective Management to mean a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance made. A set of guiding principles to be followed in determination of "POEM" would be issued.
  - ❖ With a view to provide a uniform method of computation of period of stay in India for the purposes of determination of 'resident' status in the case of an India seafarer, whether working on an Indian-ship or foreign-ship, it is proposed to provide an enabling power to CBDT to prescribe the same in the rules.
- Tax Pass through status to Alternative Investment Funds (AIFs)  
It is proposed to provide Tax Pass through status to all the sub-categories of category-I and also to category-II AIFs governed by the regulations of Securities and Exchange Board of India (SEBI).



- Fund management activity and PE in India
  - ❖ The proposed regime provides that in the case of an eligible investment fund, the fund management activity carried out through an eligible fund manager acting on behalf of such fund shall not constitute business connection in India of the said fund. Further, it is proposed that an eligible investment fund shall not be said to be resident in India merely because the eligible fund manager undertaking fund management activities on its behalf is located in India. This specific exception from the general rules for determination of business connection and 'resident status' of off-shore funds and fund management activity undertaken on its behalf is subject to specific conditions.
  - ❖ It is further proposed that every eligible investment fund shall, in respect of its activities in a financial year, furnish within ninety days from the end of the financial year, a statement in the prescribed form to the prescribed income-tax authority containing information relating to the fulfillment of the specified conditions or any information or document which may be prescribed. In case of non furnishing of the prescribed information or document or statement, a penalty of Rs. 5 lakhs shall be leviable on the fund.
  - ❖ It is also proposed to clarify that this regime shall not have any impact on taxability of any income of the eligible investment fund which would have been chargeable to tax irrespective of whether the activity of the eligible fund manager constituted the business connection in India of such fund or not. Further, the proposed regime shall not have any effect on the scope of total income or determination of total income in the case of the eligible fund manager.
  
- Real Estate Investment Trusts (REITs) and Infrastructure Investments Trusts (InvITs)  
 It's proposed that sponsor will be given the same treatment on offloading of units at the time of listing as would have been available to him if he had offloaded his shareholding through IPO. STT shall be levied on sale of such units of business trust which are acquired in lieu of shares of SPV, the benefit of concessional tax regime of tax @15 % on STCG and exemption on LTCG under section 10(38) of the Act shall be available. Tax Pass through has been provided on rental income from real estate property directly held by REITs.
  
- Clarification to Indirect Transfer  
 After taking into account recommendations of Expert Committee as well concerns raised by various stake holders, few amendments have been proposed to the provisions of the Act, so as to provide that.
  - ❖ The share or interest shall be deemed to derive its value substantially from the assets located in India, if on the specified date, the value of such assets represents at least fifty per cent of the fair market value of all the assets owned by the



company or entity. However, the indirect transfer provisions would not apply if the value of Indian assets does not exceed ` Rs. 10 crore. Further, the principle of proportionality will apply to the taxation of gains arising from indirect transfer of Indian assets.

- ❖ The Indian entity shall be obligated to furnish information relating to the offshore transactions having the effect of directly or indirectly modifying the ownership structure or control of the Indian company or entity. In case of non-compliance, a penalty is also proposed.
- ❖ The indirect transfer provisions shall not apply in a case where the transferor of share or interest in a foreign entity, along with his associated enterprises, neither holds the right of control or management nor holds voting power or share capital or interest exceeding five percent. of the total voting power or total share capital in the foreign company or entity, directly or indirectly, holding the Indian assets.
- ❖ The capital gains shall be exempt in respect of transfer of share of a foreign company deriving its value, directly or indirectly, substantially from the shares of an Indian company, under a scheme of amalgamation or demerger.

- Direct Tax Code (DTC)

DTC not to be implemented.

- Domestic Transfer Pricing

The threshold limit for applicability of transfer pricing regulations to specified domestic transactions increased from RS.5 crore to Rs. 20 crore.

- It is proposed to amend the provisions of section 195 (dealing with obligation of withholding of taxes while making payment to Non-residents) of the Income-tax Act so as to provide power to the CBDT for capturing information about prescribed foreign remittances which are claimed to be not chargeable to tax.

- Source rule in respect of interest received by the non-resident

- ❖ It is proposed to amend the Act to provide that, in the case of a non-resident, being a person engaged in the business of banking, any interest payable by the permanent establishment in India of such non-resident to the head office or any permanent establishment or any other part of such non-resident outside India shall be deemed to accrue or arise in India and shall be chargeable to tax in addition to any income attributable to the permanent establishment in India and the permanent establishment in India shall be deemed to be a person separate and independent of the non-resident person of which it is a permanent establishment and the provisions



of the Act relating to computation of total income, determination of tax and collection and recovery would apply .

- ❖ Accordingly, the PE in India shall be obligated to deduct tax at source on any interest payable to either the head office or any other branch or PE, etc. of the non-resident outside India. Further, non-deduction would result in disallowance of interest claimed as expenditure by the PE and may also attract levy of interest and penalty in accordance with relevant provisions of the Act.

- Foreign Tax Credit

It is proposed to amend section sub-section (2) of section 295 of the Income-tax Act so as to provide that CBDT may make rules to provide the procedure for granting relief or deduction, as the case may be, of any income-tax paid in any country or specified territory outside India, under section 90, or under section 90A, or under section 91, against the income-tax payable under the Act.

- Global Depository receipts (GDRs)

In order to continue with the present tax benefits with regard to income arising from the transfer of GDR (issued under the erstwhile scheme of 1993 of the Government of India) and purchased in foreign currency, in favour of underlying shares & DRs, as per the new scheme of 2014 notified by the Government, necessary amendment has been carried out to the definition of GDR.

- Wealth Tax Act to be abolished.

