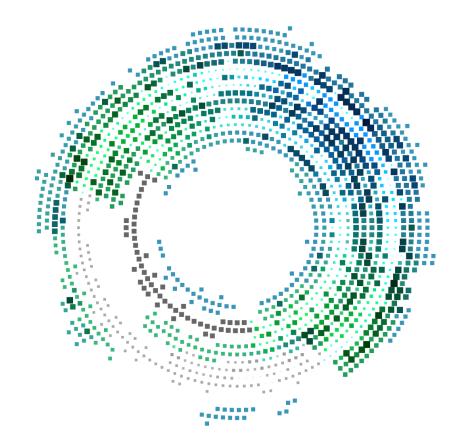
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Supply-chain shifts and some key India tax aspects

Pandemic-induced supply-chain shifts

One of the levers that forms the spine of a business is its supply chain, a process of flow of goods and services that transforms raw materials into finished goods. The objective is to maximise customer value through a network of organisations, people, activities, information, and resources. The availability of adequate infrastructure and technological deployment and an endeavour to minimise inventory and maximise customer satisfaction are indispensable for creating a robust supply-chain ecosystem.

As economies and businesses continue to experience the tumultuous ride owing to COVID-19, we have embraced a multitude of changes from the way we operate to how we live. The impact of this on the global supply chain was inevitable—creating in equal measure, situations of distress and of opportunities around it. The pandemic created at least two situations that have led to an evolution in the supply chain ecosystem: -

(1) Adverse political situations in major supply-chain countries, which pushed economies to look for alternative avenues, and

(2) Increased dependence on technology-driven businesses arising out of social-distancing practices.

The aforementioned factors have created a favourable environment for multinational companies to shift their supply-chain base to India and some other regions. These circumstances have tipped the scales in favour of having more than one supply-chain ecosystem, and not fretting much over the labour cost arbitrage amongst countries. India is being viewed as one of the most favourable destinations due to the vibrant features it offers.

What makes India an attractive destination for a supply-chain ecosystem?

India has a robust network of infrastructure ranging from roads, railways (including monorail, metro rail, etc.) airports and ports, to power and communication. India also has a largely favourable demographic composition of skilled labour. The budgetary allocation to infrastructure has been rising steadily. For instance, the Government of India in its Union Budget, 2020, announced the allocation of US\$24.3 billion to enhance the transport infrastructure. In addition, an amount of US\$1.4 trillion was allocated under the National Infrastructure Pipeline (NIP) for the period of 2019–25. Sectors such as energy (24 percent), roads (18 percent), urban (17 percent) and railways (12 percent) amount to approximately 71 percent of the projected infrastructure investments in

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India.¹ The pandemic has brought in the much-needed shift in the way business is conducted and the consumer's buying and consumption patterns. The much-needed push to the digital landscape is, in some measure, being provided by the Government of India's flagship schemes such as New India and Digital India.

Ease of setting up a business in India

The Indian economy has remained fairly open to foreign investments. Barring a few sectors such as agriculture (other than under controlled conditions), lottery, gambling, chit funds, cigarette or tobacco manufacturing, and sectors not open to private sector investments such as atomic energy and railways, Foreign Direct Investment (FDI) is allowed in most under the automatic route. Few sectors such as mining, defence, print media, telecommunications, and multi-brand retail trading require government approval. However, the Government of India has been progressively liberalising investments in some of these sectors.

Despite the slump in the global economy caused by the pandemic, India attracted an FDI of US\$27.1 billion during April–August 2020, with the services and computer software and hardware sectors receiving the highest share. These sectors are crucial contributors to the development of the country's supply chain.

India allows a diverse set of options to set up a business presence in India: private and public company, limited liability partnership (LLP), joint venture, liaison office, branch office, project office, venture capital funds, etc. One may also note the flexibility in funding the entities with options such as equity in the form equity shares, compulsorily convertible preference shares/debentures and debt in the form of foreign currency, or Indian Rupee-denominated bonds and loan simpliciter.

Taxation

The Government of India recently made news by introducing a host of taxpayer-friendly reforms. India's direct tax regime, coupled with the recent reforms, has created a favourable environment for the supply-chain ecosystem to thrive in India.

From an indirect tax perspective, India has transitioned into a comprehensive destination-based indirect tax framework in the form of Goods and Services Tax (GST) from a multi-tier tax structure. GST subsumes in itself several local taxes levied at various stages of the supply chain. With the advent of GST, certain duties of customs have also subsumed, which were earlier a cost to certain entities, reducing the overall tax burden in the value chain.

India's GST framework is akin to the globally accepted indirect tax environment implemented by several countries. GST was designed and implemented with an aim to overcome the limitations of the previous laws, thereby, allowing free flow of credit, cross-utilisation of credit between registrations in different jurisdictions, and reducing the tax burden at every stage. Similarly, customs laws and procedures are also regularly updated to keep in-line with the global rules of trade, which may aid in ease of doing business in India.

To adapt to technological advancements, the Government of India is also making successful efforts to move to a digitally stable economy. Introduction of faceless income-tax department for faceless tax proceedings, certain appeals, demands, rectifications, etc., are expected to bring greater transparency and accountability. The Taxpayers' Charter has been introduced to assure taxpayers of fair, courteous, and rational behaviour.

On the indirect tax front, an e-tax infrastructure has been developed, which includes implementation of integrated e-invoicing mechanism, e-filings, virtual hearings, automation of compliance system, maintenance of e-records, Turant Customs initiative which focuses on "faceless, contactless, and paperless customs" clearance processes.

While evaluating a tax optimum jurisdiction from a supply-chain perspective, analysis of the tax ecosystem and related incentives together are crucial. Echoing the motto of self-reliant India, the Government of India has promulgated several measures to incentivise and provide an added thrust to new and existing businesses in India. As India follows a federal structure, policies have been formulated at both the central and state levels.

Manufacturing in India

The Government of India has launched the initiative of Aatma Nirbhar Bharat Abhiyan/ self-reliant India, with the objective to endorse domestic manufacturing, attract investment, and promote ease of doing business. It has formulated and implemented various schemes and policies to make India an attractive destination for businesses looking for a new geography to shift their supply chain.

The Government of India has identified 24 sectors including electronics, automobiles, telecom, and pharma, which have the potential to scale-up operations and enhance India's share in the global trade and value chain. Thus, focused incentive schemes, in the form of fiscal and non-fiscal benefits, are being launched or proposed for these sectors. The schemes aim to provide financial assistance incentives linked to production. For instance, on 11 November 2020, the Government of India introduced production-linked incentive schemes for 10 key sectors—advance chemistry cell battery, electronic/technology products, automobiles and auto components, pharmaceuticals drugs, telecom and networking products, textile products, food products, high-efficiency solar PV modules, speciality steel, and white goods (air conditioners and LED)—worth INR 1.46 lakh crores.

To top it up, India offers one of the lowest corporate income tax rates in Asia—the headline corporate tax rate for new domestic manufacturing companies is 15 percent and for other domestic companies is 22 percent (both subject to fulfillment of the conditions). Further, year-on-year tax incentives are available for generating employment in India to as much as 30 percent of additional wages per year, subject to conditions.

Some other incentives in the form of eligible capital expenses are available to businesses not accessing the aforementioned special lower tax rates such as that of cold-chain facility, infrastructure facility, certain warehousing facility, fertiliser plants, and semi-conductor wafer fabrication manufacturing facilities. Besides these, the carry forward of business losses is allowed for a period of eight years and carry forward of unabsorbed depreciation for an indefinite period. Abolishment of dividend distribution tax on companies, waiver of income tax return filing for non-residents, and foreign companies with only royalty, fee for technical services, dividend or interest income, if subject to prescribed tax withholding, are complimentary to moving India towards becoming a global supply-chain hub.

On the international tax front, India benefits from its relationships with numerous countries. It has an extensive tax treaty network—94 comprehensive agreements, 8 limited agreements, 6 limited multilateral agreements, and 19 Tax Information Exchange Agreements. The tax treaties provide for beneficial/reduced tax rates, as low as 10 percent,

¹ India Brand Equity Foundation, September 2020

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on certain incomes, subject to conditions. India is also a signatory to the multilateral instrument and deposited the instrument of ratification in June 2019. Also relevant is that India endeavours to conclude all mutual agreement procedures between competent authorities within 24 months (average) and has a mature and and advanced transfer pricing regime for global businesses to consider on their inter-company arrangements.

For the promotion of investments in certain specified jurisdictions such as north eastern states, a special policy "North-eastern Industrial Development Scheme, 2017" has been devised to urge companies to relocate to these regions by providing concessions and incentives at par with other states.

In addition to Central Government incentives, within India, State Governments also formulate policies to attract investments by providing various fiscal and non-fiscal benefits. Under these policies, applicants negotiate various fiscal and non-fiscal benefits with the state governments within the policy framework. These benefits inter alia include single-window swift clearances, infrastructural facilities, refunds, and concessions spread over a designated period of time, subject to conditions.

Therefore, businesses intending to relocate/set up supply chains in India can explore the benefits offered at the central level, coupled with incentives and support offered at the state level.

While several leading international businesses have already set up manufacturing facilities in India, some others have entered into agreements with domestic and international contract manufacturers to establish supply chains in India. Toll manufacturing has also elicited interest, given its financial advantages, but there are some tax imperatives that businesses need to bear in mind, especially on the aspect of exposure to permanent establishment. Contract and toll manufacturing are an active area of interest in several secondary or brownfield investment projects. Most large international businesses are also eyeing the twin advantage of supply and demand in one geography, given the demographic profile of the country and the flexibility of scaling operations.

Imports in India

For incentivising businesses on the procurement side and thereby, reducing the burden of taxes/duties, customs laws provide for several concessions and exemptions on import of goods for thrust sectors such as solar, defence, and aviation. India has also entered into several multilateral and bilateral Free-Trade Agreements (FTAs) with various countries to allow imports at concessional customs duty rates. Key FTAs executed by India are with Japan, Korea, Singapore, Indonesia Malaysia, Bhutan, Sri Lanka, etc.

India's Foreign Trade Policy (FTP) also aims at promoting export and trade. Under the presently operational FTP, several schemes have been prescribed which inter alia include Export Promotion Capital Goods Scheme and Advance Authorisation Schemes, allowing duty-free import of inputs and capital goods for use by exporters.

The customs law provides the option of duty deferment to importers by permitting storage or manufacturing operations on imported goods without the payment of customs duty. Likewise, customs law also provides for duty drawback, i.e., refund of the customs duty, chargeable on any imported material used in the manufacture of specified goods exported out of India.

Amongst the sector-/jurisdiction-specific incentives, there are also several tax-free zones set up across the country in the form of special

economic zones, export-oriented units, and free-trade warehousing zones, which permit duty-free imports for exports outside India.

Exports from India

Extending the erstwhile ideology put forth by the "Make in India" initiative to "Make for World", the government aims to promote exports by allowing zero-rating of supplies of goods and services exported out of India. For the service sector, various companies are setting up "Global Inhouse Centres (GICs)" or "in-house R&D centres" in India to enjoy the benefits of zero-rating, which is granted on the export of services out of India. Benefit is extended by either allowing export without payment of taxes and refund of accumulated credits or by refunding the taxes paid on export of such goods or services.

In addition to the benefits under GST, various rewards in the form of duty credit scrips or refunds are provided to goods and service exporters under the FTP to offset infrastructural inefficiencies and associated tax costs. Merchandise Export from India Scheme (MEIS) for the export of goods and Rebate of State and Central Levies and Taxes Scheme (RoSCTL) for the export of made-up articles and garments have been designed to promote the export of notified goods to notified markets. Along similar lines, the Service Export from India Scheme (SEIS) is designed to encourage and maximise the export of notified services from India by issuing freely transferable duty credit scrips.

Present FTP is operational until March 2021. Therefore, the government is in the works to replace MEIS and RoSCTL schemes with the Scheme for Remission of Duties and Taxes on Exported Products (RoDTEP). The RoDTEP scheme would allow reimbursement of taxes and duties, which are not exempted or refunded under any other scheme in accordance with the World Trade Organization (WTO) norms. Continuity of SEIS beyond the operational period of FTP is also currently under deliberation.

While there are several positive moves by the Government of India, some others like the introduction of equalisation levy on e-commerce operators, and provision expansion on tax collection at source have created some investor concerns. International businesses need to carefully evaluate these several dimensions while setting up a business presence in India.

Also, GST is still evolving, and the Government of India is regularly seeking feedback from the trade and working towards promoting a conducive environment for the businesses to ensure ease of doing business in India. The overall vision is to simplify the indirect tax environment by reducing compliance burdens, shifting gradually into faceless and paperless processes, and reducing the tax burden for a seamless experience for businesses.

India's time to shine

In conclusion, given the advantages offered by India and its forwardlooking policies, one may expect multinational companies looking for an alternate supply chain to shift to India. An affirmation of this thought comes in the form of the recent announcement of the India-Japan-Australia agreement towards achieving supply-chain resilience in the Indo-Pacific region. The economic shift in terms of business and trade, will be interesting to follow as India plays an important role in a parallel network of supply-chain linkages.

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