



# Global Tax Update

India

Deloitte Tohmatsu Tax Co.

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## 1. CBDT<sup>1</sup> directive on phasing out of deductions/ tax holidays under the Indian domestic tax law

The Indian Finance Minister in the Budget 2015 had declared the intention to reduce rate of corporate tax from 30% to 25% over the next four years starting from the year 2016-17 along with corresponding phasing out of deductions/ tax holidays. This was proposed to simplify tax laws thereby bringing about transparency and clarity.

The CBDT has now issued a press release<sup>2</sup> detailing its broad plan to implement the above tax reduction. CBDT invited comments from the public on the aforesaid phasing out plan till 31st December 2015. The key highlights of the phasing out plan are summarized below:

- Profit linked, investment linked and area based deductions/ tax holidays will be phased out for both corporate and non-corporate tax payers.
- No modification/ advancement/ extension of sunset dates for deductions/ tax holidays where they have already been prescribed in the domestic tax law.
- Sunset date of 31.3.2017 will be provided either for commencement of the activity or for claim of benefit in cases where no sunset date has been prescribed.
- There will be no weighted deduction with effect from 01.04.2017.

We will discuss the provisions again once they are finalized by the CBDT based on the comments received from public. The reduction of corporate tax rate coupled with withdrawal of various tax deductions could impact present and future business plans of Japanese subsidiaries in India.

## 2. Amendments to Foreign Direct Investment (FDI) Policy<sup>3</sup>

The Indian Government has been taking multi-pronged policy decisions for inclusive development. These decisions are aimed at improving ease of doing business in India and making India an attractive destination for entrepreneurs and global businesses.

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1 Central Board of Direct Taxes

2 Dated 20.11.2015

3 Press Note dated on 10 November 2015 and Press Note 12 (2015 Series) dated 24 November 2015 issued by Department of Industrial Policy & Promotion and hosted on its [website](#)

To boost investment environment and to attract foreign investments, the Government announced, on 10 November 2015, FDI reforms relating to many sectors of the economy. The amendments in FDI Policy announced by DIPP<sup>4</sup> will be effective from 24 November 2015<sup>5</sup>.

Key highlights of the amendments have been summarized below:

Sl. No.	Sector/ Particulars	Changes / Amendments (likely rationale / impact)
1.	Manufacturing	<ul style="list-style-type: none"> <li>Manufacturers, having FDI, can now sell their products through wholesale and/or retail, including through e-commerce without government approval. Under the existing FDI Policy, there were no specific guidelines for e-commerce by manufacturing sector.</li> </ul>
2.	Single Brand Retail Trading (SBRT)	<ul style="list-style-type: none"> <li>In case of FDI in the 'state-of-art' and 'cutting-edge technology' segments in SBRT, condition of 30% local sourcing may be relaxed with government approval.</li> <li>Entities undertaking SBRT through physical stores will be permitted to undertake e-commerce activities.</li> <li>It has been clarified that Indian brands are equally eligible for undertaking SBRT.</li> <li>In case of FDI in companies owning Indian brands and carrying on SBRT, conditions viz. products to be sold under the same brand internationally and investment by non-resident entity/entities as the brand owner or under legally tenable agreement with the brand owner, will not be applicable.</li> <li>100% FDI is now permitted under automatic route in Duty Free Shops located and operated in the Customs bonded areas.</li> </ul>
3.	Wholesale and SBRT	<ul style="list-style-type: none"> <li>A single entity is now permitted to carry both SBRT and wholesale trading subject to compliance of respective FDI policy conditions.</li> </ul>
4.	Construction development	<ul style="list-style-type: none"> <li>Existing condition of development of minimum floor area of 20,000 sq. meter per project and minimum FDI of USD 5 million within 6 months of commencement of project has been removed.</li> <li>Each phase of the construction development project would be considered as separate project for the purpose of FDI.</li> <li>Foreign investor can exit and repatriate foreign investment before the completion of project under automatic route on the condition that investment has been locked-in for 3 years calculated with reference to each tranche of foreign investment.</li> <li>Transfer of shareholding from one non-resident to another non-resident, without repatriation of investment will neither be subject to any lock-in period of 3 years nor would any government approval be required.</li> <li>Condition of 3 years lock-in period will not apply to hotels and tourist resorts, hospitals, special economic zones, educational institutions, old age homes and investment by Non-Resident Indian (NRIs).</li> </ul>

4 Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India  
5 Press Note 12 (2015 Series) dated 24 November 2015 issued by DIPP and hosted on its [website](#)

		<ul style="list-style-type: none"> <li>If the project or trunk infrastructure is completed before the 3 years lock-in period, then exit under automatic route will be permitted any time without waiting for 3 years to get completed.</li> <li>It has now been also clarified that earning of rent/ income on lease of the property, not amounting to transfer, will not amount to real estate business which is prohibited.</li> </ul>
5.	Defense	<ul style="list-style-type: none"> <li>FDI up to 49% is now brought under automatic route.</li> <li>FDI proposal in excess of 49%, which is likely to result in access to modern and "state-of-art" technology in the country, will now be considered by Foreign Investment Promotion Board (FIPB) instead of Cabinet Committee on Security (CCS).</li> </ul>
6.	Banking – Private Sector	<ul style="list-style-type: none"> <li>Full fungibility introduced for investment by various categories of foreign investors like FDI<sup>6</sup>, FII<sup>7</sup>, FPI<sup>8</sup> and QFI<sup>9</sup>.</li> <li>FDI (including FII/ FPI/ QFI) allowed up to 74% (earlier FII / FPI/ QFI holding was allowed only up to 49%) provided that there is no change of control and management.</li> </ul>
7.	Civil Aviation	<ul style="list-style-type: none"> <li>FDI up to 49% now allowed for regional air transport service (RSOP) under automatic route (Improving air connectivity and boost tourism).</li> <li>FDI in non-scheduled air transport service and ground handling services enhanced from 74% to 100% under automatic route (as against earlier government approval route for FDI beyond 49% and up to 74%).</li> </ul>
8.	Limited Liability Partnerships (LLPs)	<ul style="list-style-type: none"> <li>100% FDI is now permitted under the automatic route (as against earlier Government approval route) in LLPs operating in sectors/ activities where 100% FDI is allowed under automatic route and there are no FDI-linked performance conditions. This would also include conversion of a company with FDI into an LLP.</li> <li>LLPs having FDI can now make downstream investments in another company / LLP in sectors in which 100% FDI is allowed under the automatic route and there are no FDI-linked performance conditions.</li> <li>Other conditions applicable to FDI in LLP such as, receipt of only cash consideration towards capital, designated partner nominated by body corporate to be only from an Indian Company is removed. Some other conditions have also been relaxed.</li> </ul>
9.	Establishment, transfer of shares and swap of shares	<ul style="list-style-type: none"> <li>Establishment and transfer of ownership and control of Indian companies will require government approval if the company concerned is operating in sectors / activities which are under government approval route rather than capped sectors.</li> <li>No government approval will be required for swap of shares in sectors under automatic route.</li> </ul>

6 Foreign Direct Investment

7 Foreign Institutional Investor

8 Foreign Portfolio Investor

9 Qualified Foreign Intermediaries

### **3. Karnataka High Court<sup>10</sup> holds that transfer of shares of a loss making Indian company by a shareholder company to its another subsidiary does not result in denial of business loss to be carried forward of the loss making subsidiary**

As per the domestic tax laws<sup>11</sup>, brought forward business losses lapse on change in the beneficial ownership of 49% or more of the equity shares in closely held companies<sup>12</sup>.

The controversy arose as the term “beneficial shareholding” has not been defined for this purpose. In the present case, the shareholder had transferred the shares of loss making Indian company to its wholly owned subsidiary.

The question before the High Court was whether the loss making Indian company was entitled to carry forward and set-off business losses (as the shares continued to be held and controlled by the same group) despite the change in its immediate shareholding.

The High Court held in favor of the Indian company that:

- The provisions should be applicable in cases where there is change in shareholding resulting in change in control of the company.
- The purpose of the provisions is that benefit of brought forward losses should not be misused by new owner, who may purchase the shares of the company, only to get the benefit of past losses.
- The provisions should not be attracted in cases where the control over 51% of the voting power remains with the same owner.

The ratio of this ruling will have to be considered in structuring transactions. Further, this ruling would also lead to a possibility of the tax authorities contending that any change in shareholding at holding company level (i.e. indirect transfer) may result in lapse of losses at the step down subsidiary level since the same has resulted in change in control of the subsidiary even if the immediate shareholding of the step down subsidiary is kept intact.

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<sup>10</sup> Source: Commissioner of Income-tax, Bangalore vs AMCO Power Systems Ltd. [2015] 62 taxmann.com 350 (Karnataka)

<sup>11</sup> Section 79 of the Income-tax Act, 1961

<sup>12</sup> Closely held company means companies in public are not substantially interested – generally the private and unlisted public companies

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