

# Cross Border India\*

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International Tax Newsletter

PwC-Bangalore

## Tax Thoughts

### √ Tax highlights of Budget 2010-11 for international companies

*Direct Taxes Code (DTC) / Goods and Services Tax (GST)* – The DTC and GST are to be introduced from April 1, 2011. The GST will miss its earlier introduction deadline of April 1, 2010.

*Corporate tax rate* – A proposed reduction in surcharge from 10% to 7.5% percent for companies would reduce the effective corporate tax rate from 33.99% to **33.22%**.

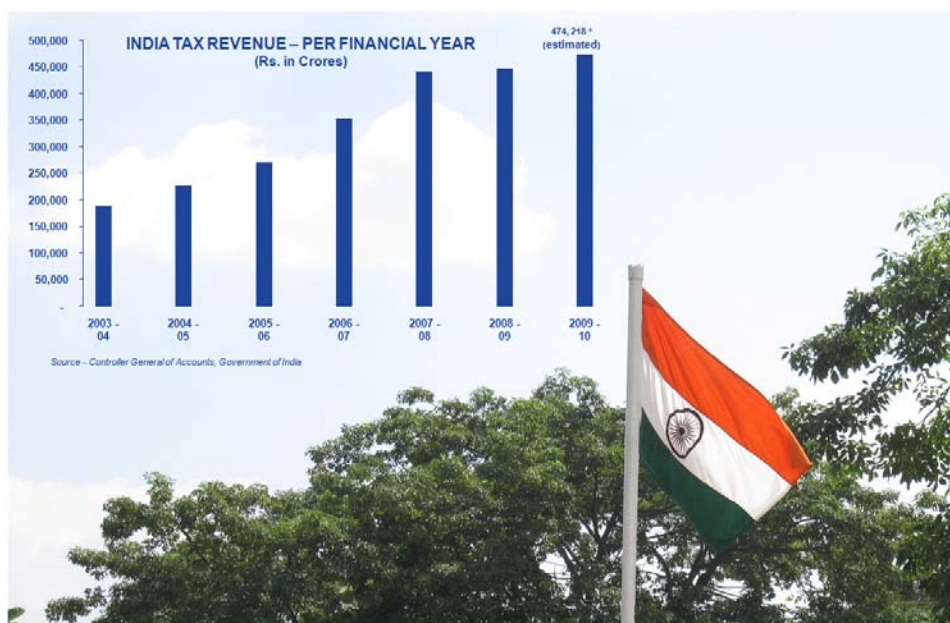
*Minimum alternative tax (MAT)* – Rate will increase from 15% to 18%.

*No STPI change* – There was no further extension to the income tax deduction for export profits of units covered by the STPI Act and those set up in EOUs, now scheduled to expire on March 31, 2011.

*Limited Liability Partnership (LLPs)* – From April 1, 2010, no capital gain may arise on conversion of certain small companies to LLPs.

*Special Economic Zones (SEZs)* – The Indian government is committed to ensure continued growth of SEZs. The Budget did not, however, address the proposed DTC, which would eliminate income tax benefits under section 10AA for export profits of an SEZ unit. A clarifying fix in calculating export profits is proposed to be effective from April 1, 2006.

*Gift of shares* – Receipt of shares by a company in the form of a gift is proposed to be treated as income in the hands of the recipient company, effective on or after June 1, 2010.



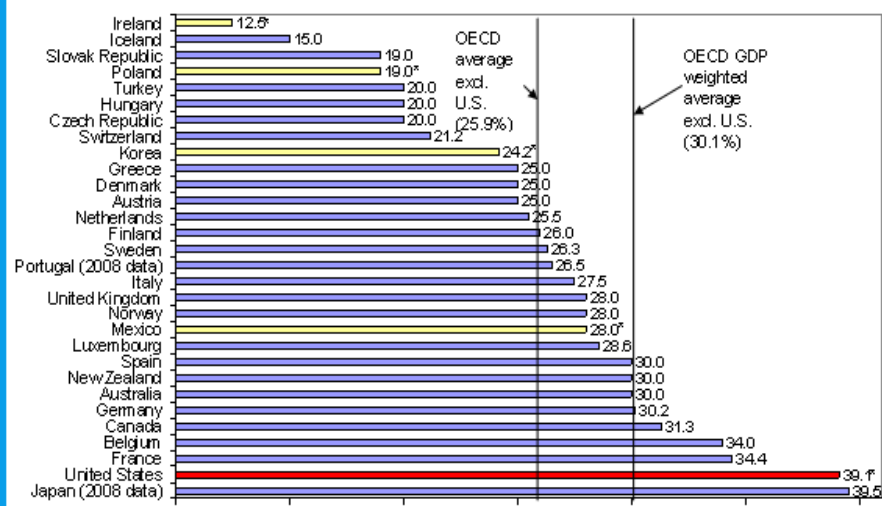
## Budget 2010-11: Taxing Times Ahead

Tax revenues in India have remained relatively flat for three years. However, that is expected to change soon, according to Finance Minister Pranab Mukherjee who announced India's 2010-11 Union Budget on Friday, February 26<sup>th</sup>, along with introduction of the proposed Finance Bill, 2010. With India's impressive recovery in growth over the past few months, the Finance Minister is focused on a return to a GDP-growth path of 9% and later to double digits. Current estimates of 7.2% GDP growth for 2009-10 are evidence of a "very encouraging" recovery in India. Gross tax revenues for 2010-11 are now projected to grow by about 16.5%.

For taxpayers in India, the burden going forward will continue to be heavily borne by Indian corporates, who will be responsible for about 40% of gross tax revenues. This remains consistent with trends over a 20-year period, and especially most recently, with the percentage of gross tax revenues generated from corporate payers increasing from 10% in 1990-91, to 25% in 2003-2004, and to over 40% today.

The Finance Minister noted that the process for building a "simple tax system" in India – i.e., with minimum exemptions and low rates – remains on target, with the planned implementation of the Direct Taxes Code from April 1, 2011. For Indian corporates, this may provide little solace. The tax uncertainty caused by introduction of the DTC last year will only continue with the tax proposals included as part of this year's proposed Finance Bill.

### Corporate Income Tax Rate - OECD Countries, 2009



U.S. rate of 39.1% is based on 35% federal tax and 6.3% deductible state tax  
 \*Indicates country taxes worldwide income. All other countries have territorial systems.

Source: Tax rates from OECD Tax Database, 2009; 2007 GDP weights.

### India lags at global tax competitiveness

India continues to provide a less competitive playing field for Indian-headquartered companies with its high corporate income tax rate (33.99%) and tax on worldwide income. However, the 25% rate proposed under the Direct Taxes Code could bring India more in line with global tax trends in other countries.

Since 1990, every OECD country (other than the U.S.) has lowered its corporate tax rate an average of 15 percentage points. The combined federal/state rate in the U.S. has actually increased during that same time.

## Other News

- IFRS convergence in India now appears effectively delayed until April 1, 2011, per a press note issued last month by the Ministry of Corporate Affairs. The initial group of Indian companies required to be compliant – Nifty 50, Sensex 30, listed companies outside of India, and listed/unlisted companies with a net worth in excess of Rs. 1,000 crores – will need to convert their opening balance sheets from Indian GAAP to International Financial Reporting Standards as of April 1, 2011 for financial years starting on or after April 1, 2010. Without requiring IFRS comparatives for 2010-11, companies may find themselves compliant with India rules for 2011-12, but still not fully compliant with IFRS.
- The U.S. has become more of an outlier in terms of its international tax system (as illustrated above), and it appears likely to continue. Tax proposals issued this month by the Obama administration as part of its 2011 budget continue to take aim at U.S. multinationals and outsourcing, with a series of tax measures designed to reduce the benefit of tax deferral for U.S. companies on offshore earnings. For Indian corporates, alarm was raised at the end of January, when President Obama stated in his State of the Union speech that his focus was to encourage businesses to stay within U.S. borders and that “it is time to finally slash the tax breaks for companies that ship our jobs overseas ...” However, the brunt of the latest U.S. tax proposals appears to remain on U.S.-headquartered companies. For a further discussion of the U.S. tax proposals, please see a recent article drafted by Eric Peden entitled “US government is hell bent on taxing firms’ offshore earnings,” appearing in *Daily News & Analysis* (Money Section, page 20, February 5, 2010).

## International Tax Team in Bangalore

PwC-India has a dedicated team in Bangalore within the Tax and Regulatory Services (Mergers & Acquisitions) group, providing international tax advisory services.



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