

# Cross Border India\*

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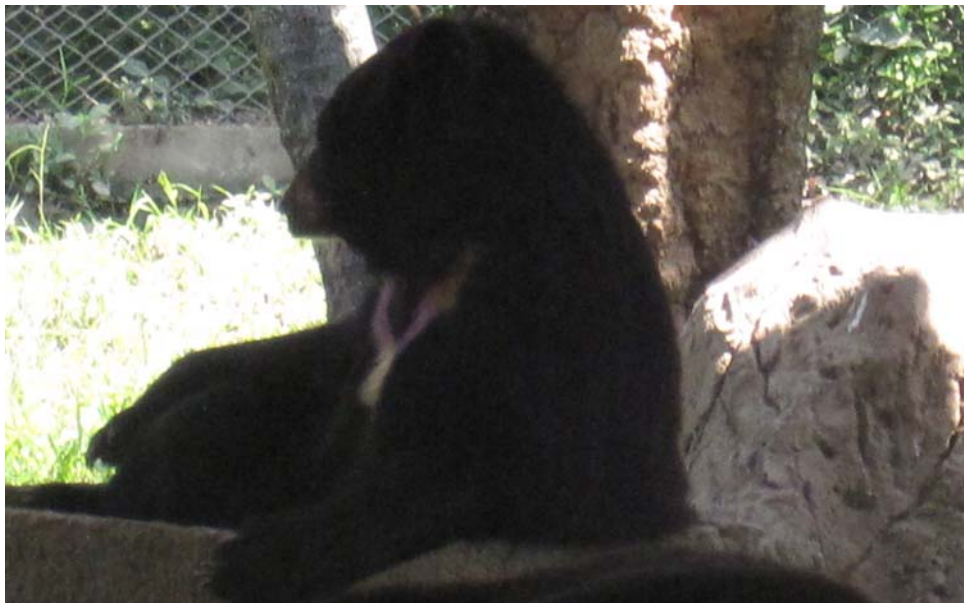
## Tax Thoughts

### √ *India withholding tax on cross border supply of goods*

Payments to foreign suppliers of goods have not been previously thought to be subject to income tax withholding in India. In light of a recent Karnataka High Court ruling, mandatory withholding on any payment to a non-resident for the cross border supply of goods may be the default rule going forward. A resident taxpayer not wanting to withhold tax may be required to first approach India revenue officials for relief in the form of a dispensation order. With the shift in understanding triggered by the court's ruling, taxpayers may need to review their current withholding tax compliance policies and procedures. Potential negative consequences include a demand for tax not withheld, as well as a disallowance of expenses in a tax assessment.

### √ *Ongoing tax cloud for indirect transfers of India assets*

Non-resident investors continue to deal with the uncertainty caused by the ongoing *Vodafone* controversy. Only recently has the India tax department followed up after an interim Supreme Court order handed down in January. With any foreign share transfers or group restructurings, non-residents should consider potential India tax risks and planning alternatives.



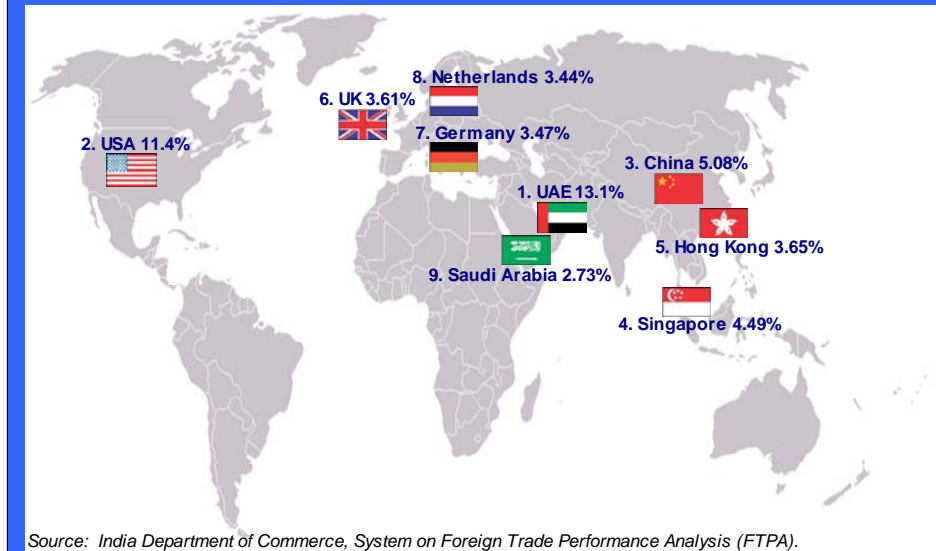
## Exporters Wait; No Recovery Yet

India's overall economy continues to rely heavily on its domestic market for good health, which has proven favorable given the ongoing global recession. Exports account for only about 14% of India's total GDP, but have played an important role in fueling India's economic growth in recent years. Robust growth in exports for the prior five years propelled India to a 1.64% share in total global trade in 2008-09 - up from .92% in 2003-04.

India's exports have now fallen for 12 consecutive months through September 2009 (over the prior year's monthly figures), according to data of the Ministry of Commerce & Industry. Nevertheless, India remains focused on high export growth going forward. Union Minister of Commerce & Industry Anand Sharma indicated that India would like to return to positive export growth by next year (2010-11), with a target growth of 15%. Thereafter, Sharma feels that India should be able to resume high export growth of about 25% per annum. His expectation is that India's exports of goods and services will double by 2014, with a long-term objective to double India's share in global trade by 2020.

As for now, exporters must wait and see, while looking overseas for signs of economic life remains problematic. India's second largest export market, the U.S., continues to deal with its own problems of record deficits, high unemployment and plummeting tax revenues. A widespread drop in sales tax revenues through September 2009 evidences a continuing reduction in spending by U.S. consumers. Even with double-digit gains in equity markets year-to-date, an economic mirage is suggested by the mirror-like correlation between the rise in equities and the fall of the U.S. dollar during the year.

### Top Markets for India Exports 2008-09



Source: India Department of Commerce, System on Foreign Trade Performance Analysis (FTPA).

## India's exports continue to fall in 2009-10

Exports have fallen in each of the first six months of the current fiscal year. From April to September 2009, the cumulative value of India's exports was US\$77.855 billion or Rs. 378196 crore – representing **negative growth** of 28.5% in dollar terms and 18.6% in rupee terms over the same period last year.

For September alone, the value of exports fell by 13.8% (dollar terms) and 8.4% (rupee terms). By contrast, India has seen robust export growth over the last five years – US\$63 billion in 2003-04 and US\$185 billion in 2008-09.

## Other News

- With no draft legislation for the new Goods and Services Tax ("GST") yet publicly available, the proposed implementation date of April 1, 2010 remains in doubt. However, a white paper released this month by a committee of state finance ministers does provide additional information on India's proposed GST. The new GST would be a comprehensive value-added tax ("VAT") on the supply of goods and services in India, generally replacing other indirect taxes now separately imposed (e.g., VAT / sales tax / service tax / excise tax). Tax would be imposed at both federal and state levels, although specific rates are not yet known. For goods, a two-tier rate structure would apply at both central and state levels, while a single rate is expected to apply for services at both central and state levels.
- A recently-approved proposal initiated by the Ministry of Commerce & Industry would freely apply the automatic route under FEMA ("Foreign Exchange Management Act") to all outbound payments for royalties, lump-sum fees for the transfer of technology, and payments for the use of trademarks / brand names.
- According to a recent article in *The Economic Times*, Finance Minister Pranab Mukherjee has asked the revenue department to open negotiations with all of its 77 treaty partners in order to have a real-time exchange of information on tax evasion and tax avoidance, with Switzerland being one of the first stops.

## 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.



**Eric Peden**  
eric.peden@in.pwc.com  
Phone: +91 (80) 4079 6018  
Mobile: +91 97414 88277



**Ranjith Pathiyil**  
ranjith.pathiyil@in.pwc.com  
Phone: +91 (80) 4079 6035  
Mobile: +91 99801 45622



**Surya Dutta**  
surya.dutta@in.pwc.com  
Phone: +91 (80) 4079 6035  
Mobile: +91 99029 29754