Snapshot of Indian Regulatory Environment…

Exchange control Regime (in brief'):

- **Investor categories:**
  - **Corporate – up to 400% of net worth**
  - **Partnerships / Proprietorships**
  - **Individuals – US$ 2,00,000 scheme**
- **Permitted Financing:**
  - **Equity**
  - **Debt**
  - **Guarantee**
- **Special Purpose Vehicles allowed**
- **Automatic approval for investment**
- **Automatic approval for divestment / transfer**
- **Liberalized regime – setting up of overseas branch / offices**

Snapshot of Indian Regulatory Environment

Income Tax Regime

- **Taxation of foreign source investment income**
  - **Classical System of taxation of foreign dividends**
  - **Provisions related to 'Deemed Dividend'**
  - **Capital gains on divestment**
- **Transfer pricing regulations**
- **Phased out tax exemptions for exports**
- **No CFC regulations**
- **No detailed regulations on Foreign Tax Credits**
- **Extensive tax treaty network**

Compulsions for businesses to structure overseas investments in tax efficient manner

International Taxation of Foreign Dividends

DOUBLE TAX CREDIT or **PARTICIPATION EXEMPTION**

Parent

Foreign Sub

DOUBLE TAX CREDIT

PARENT TAX	
Profit	100
Tax (34%)	34
Double Tax Credit	(35)
Additional Tax	**Nil**

SUB TAX	
Profit	100
Tax	35
Net Dividend	65

PARTICIPATION EXEMPTION

PARENT TAX	
Profit	65
Tax	**Nil**

SUB TAX	
Profit	100
Tax	35
Net Dividend	65

Indian Taxation of Foreign Dividends

India

Foreign Sub

INDIA TAX	
Profit	65
Tax	22
Distributable Profits	43
Effective Tax Rate	**57%**

FOREIGN TAX	
Profit	100
Tax	35
Net Dividend	65

Branch Vs Subsidiary

India

Foreign Sub

India

Foreign Branch

FOREIGN TAX	
Profit	100
Tax	35
Net Dividend	65

INDIA TAX	
Profit	65
Tax	22
Distributable Profits	43
ETR	57%

FOREIGN TAX	
Branch Profit	100
Tax	35
Net Branch Profit	65

INDIA TAX	
Branch Profit	100
India Tax	34
Credit	34 (max)
Additional India Tax	NIL
ETR	35%

Issues Underlying Tax Structuring

- **Tax Residency**
- **Permanent Establishment**
- **Transfer Pricing**
- **Substance**
- **Due Diligence**
- **Anti Avoidance/Abuse/Tax Risk Management**
- **Treaty Shopping/WHT issues**

Holding Company Structures

Benefits

- Financing reinvestments
- Capital gains tax relief on exit/ internal re-organization
- WHT planning for dividend/ interest/ royalty payouts
- Reduction in tax costs associated with subsequent shareholding migration

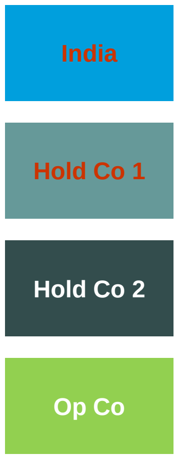
Issues

- Indian/ Foreign Anti-Avoidance Provisions

Holding Company Structures

- Type A -Cyprus, Mauritius, Singapore
- Typical features of these Hold Co jurisdictions
  - 0% WHT on outbound dividends
  - Dividend income taxed in India at 34% but underlying tax credit / tax sparing credit available under treaty
  - Capital gains tax exemption in Hold Co's jurisdiction on sale of shares in the Hold Co; taxed in India at 22%
  - Foreign sourced income is tax exempt/ taxed at a very low effective rate in Hold Co's jurisdiction
  - Capital gains tax exemption in Hold Co's jurisdiction on sale of shares in a Op Co

Holding Company Structures (Cont'd)



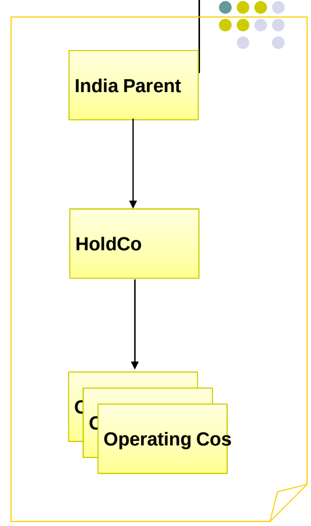
- Type B- Brazil, Greece
- Typical features of these Hold Co jurisdictions
  - Inbound dividends are tax exempt in India
  - 0% Dividend WHT on outbound dividends
  - Capital gains on sale of shares in a Hold Co 1 could be taxed in both countries, hence, 2nd tier Hold Co required
- Singapore,Mauritius ,Spain, Austria, Netherlands, Cyprus, could be considered for 2nd tier Hold Co jurisdictions

Typical jurisdictions for locating Hold Co

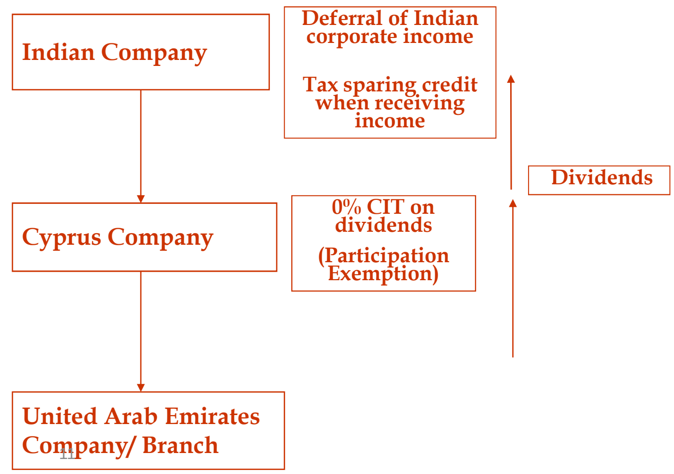
- Netherlands, Switzerland, Singapore, Luxembourg

Benefits

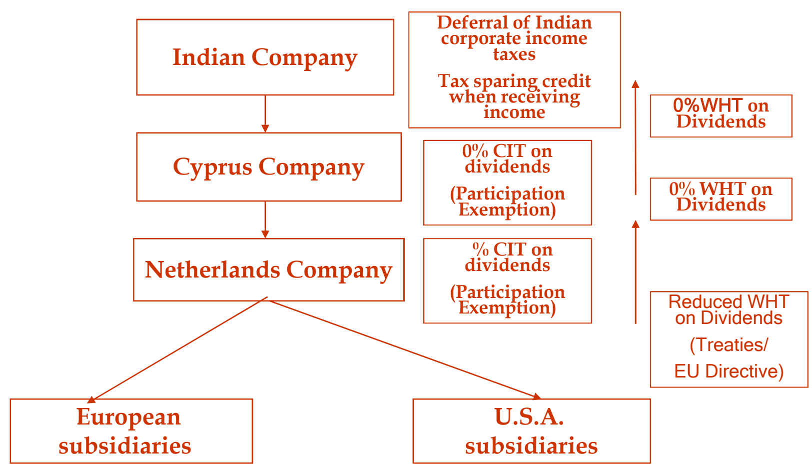
- Low/ nil tax in Hold Co on dividends from Operating Cos
- Low/ nil WHT on dividends paid by Hold Co
- India tax deferral – no tax until repatriated
- Possibility of redeploy funds within foreign structure without
- India tax cost



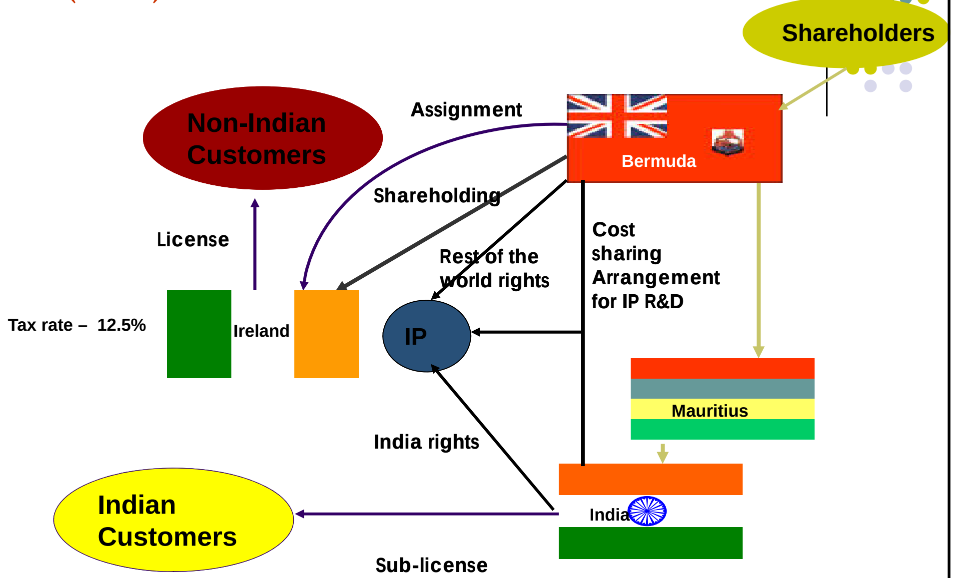
OUTBOUND INVESTMENTS INTO UAE THROUGH A CYPRUS COMPANY



OUTBOUND INVESTMENTS CYPRUS – NETHERLANDS STRUCTURE

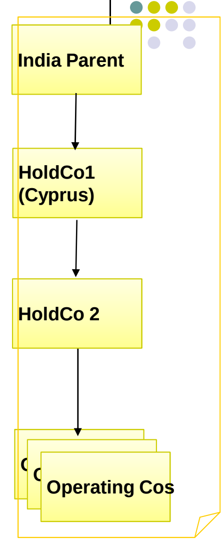


IP (R&D) Structure – Ireland

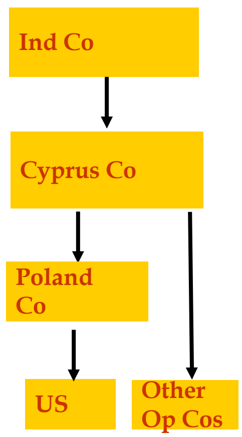


Two-tier Hold Co structure

- Hold Co 1 located in Cyprus
- Hold Co 2 located in Netherlands, Belgium or Luxembourg
- **Benefits**
- Low/ nil tax in Hold Co 2 on dividends from Operating Cos
- Nil WHT on dividends paid by HoldCo 2 under EU Directive
- Foreign Source dividend exemption in Cyprus and absence of
- WHT
- Tax sparing credit under India/ Cyprus tax treaty can reduce India tax on dividends to approx. 23%
- India tax deferral – no tax until repatriated
- Possibility to redeploy funds within foreign structure



Acquisition Technique.



Description

- **Ind Co sets up a Cyprus Company**
- **Cyprus Co invests in Polish for US investments Cyprus Co to make direct investments in all other jurisdictions**

Benefits

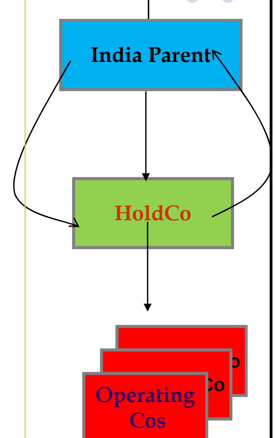
- **Absence of LOB clause in US-Poland treaties**
- **5% WHT on dividends from US. 0% WHT on interest & royalties**
- **Capital gains derived on sale of shares in US Op Co would be tax exempt in US but taxable in Poland at 19%**
- **0% WHT on dividends and interest from Poland to Cyprus**

Issues

- **Re-negotiation of tax treaty to introduce LOB clause**
- **Conduit financing rules would apply in certain cases of debt funding for a US Op Co**

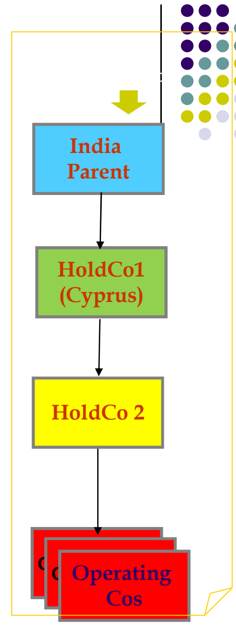
Use of Hybrid Instruments

- Investment structured by way of redeemable preference shares
- Repatriation structured by way of preference shares redemption
- **Benefits**
- Preference share redemption characterized as capital gains in India
- Capital gains taxed at lower rate if redemption takes place after 12 months (as compared to 30% for dividends)
- Ability to step-up cost basis of the shares based on indexed cost of acquisition for purpose of computation of taxable capital gains

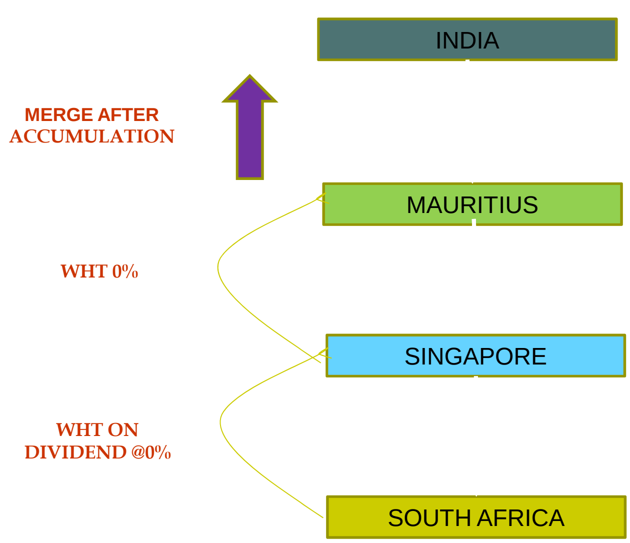


Leveraged Acquisition

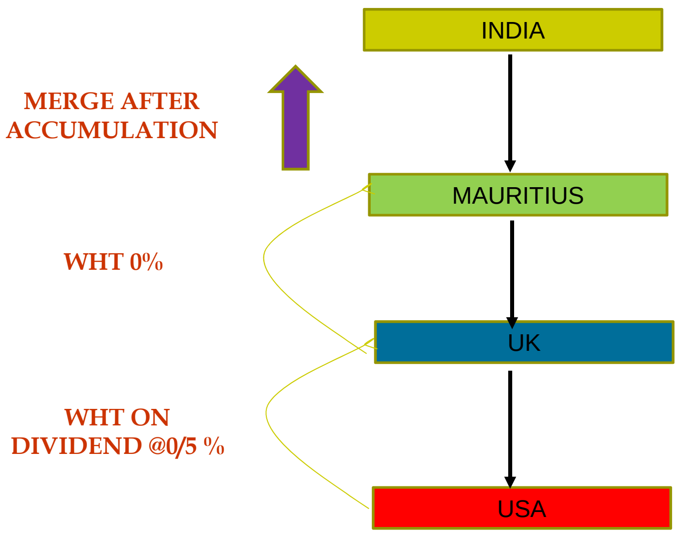
- Indian Parent incurs third-party debt for acquiring shares in Hold Co
- Hold Co uses funds for acquiring operating Cos
- Benefits
- Interest tax deductible for Indian Parent against its operating income
- Interest deductible whether or not Indian Parent earns dividends from Hold Co1
- Possibility of tax arbitrage – interest deduction at effective tax rate of 30%, dividends from Hold Co 1 taxed at approx 20% after considering tax sparing credit



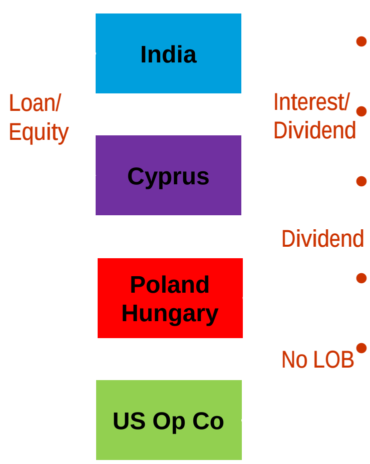
MULTI LAYER



MULTI LAYER



US : A Different Approach Needed



- Absence of stringent LOB clause allows treaty benefits to Poland or Hungary
- 0% dividends WHT from Poland/Hungary to Cyprus under EU directive
- Underlying tax credit granted in Poland/Hungary for taxes paid on income from which dividends are paid by US
- 0% interest WHT from US to Poland/Hungary
- 0% WHT on dividends, interest and royalty from Cyprus to India; tax sparing credit available at 10% / 15% in India