

Did you know?



British
High Commission
New Delhi



Taxation of indirect transfers may adversely affect mergers and acquisitions, thereby affecting investments.

Issue 6: Ambiguity on indirect transfer rule in section 9

The Finance Act, 2012, amended section 9(1) (i) of the Act retrospectively (w.e.f. 1 April 1962) to insert an explanation that seeks to clarify that the situs of capital assets being shares/interest in a foreign entity, directly or indirectly deriving value 'substantially' from assets located in India, shall be deemed to be in India.

However, there are various open issues in this regard. For example, it is unclear what is 'substantial' (in the context of shares of overseas companies deriving 'substantial' value from assets located in India), exemptions for small holdings overseas, etc.

The Direct Taxes Code, 2013, issued by the government for public comments does address most of these aspects after taking into account the recommendations of the Standing Committee of the Parliament. Owing to the lack of clarity in section 9 of the Act on many aspects relating to the indirect taxation rule, foreign companies acquiring overseas companies (with subsidiaries in India) or undertaking overseas mergers and acquisitions are unclear on providing for Indian taxes.



Impact

The overall merger and acquisition climate may be adversely affected.

Proposed solution

- The meaning of the term 'substantial' should be clarified by way of legislative amendments in an objective and unambiguous manner. This would provide certainty to the taxation regime governing indirect transfers.
- The term 'substantial' has been clarified by the Delhi High Court in the case of Copal Research Limited to include only cases where the transfer of shares of a company incorporated overseas derive more than 50% of their value from assets situated in India, and not otherwise. This may be used as guidance for suitable issuing clarification.
- The method of computation of the cost and sale consideration allocation needs to be prescribed.

PwC-India British High Commission joint tax project seeks to understand direct tax issues faced by UK-based companies in India