**Taxation regime and Investment: Emerging Issues**

**Submitted by**

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**Chapter-1**

1. Introduction-

To begin with the above named topic let us first understand what Investment is and why is there a need for Taxation. Investing involves placing money away in the hope of earning a return in the future. An asset or object purchased with the purpose of producing income or appreciation is referred to as an investment. The aim of investing is to generate income and increase the value of an asset over time. Any method for producing potential profits can be referred to as an investment. This involves, for example, the buying of shares, securities, or real estate property. A tax system is said to be administratively effective if it is able to raise revenue from different segments of society based on their ability to pay at a low cost. India has made considerable strides in terms of taxes over the last six decades. It is important to ensure that the taxation system is compatible with our economic and social priorities when developing it. Income tax, as a source of revenue and a measure of reducing economic inequality, is critical in today's economic system.

Capital formation is a key factor in economic growth. If domestic investments contribute to an economy's capital stock, foreign direct investment (FDI) fills the gap between domestic savings and investment, contributing to overall capital accumulation. Foreign Direct Investment (FDI) plays an important role in the early stages of a country's overall growth, and many developing countries are now attempting to attract more and more FDI in various sectors. Incentives are used by both developing and developed countries to try to attract FDI, but the types and frequency of incentives vary. India is a country that has been ranked as a desirable destination by numerous international rating organizations. Multinational companies can invest in India because of its highly qualified and cost-effective workforce. The Government of India has extended incentives in the form of tax holidays, deductions, rebates, expenditure tax exemptions, depreciation allowances, and other business taxes in order to promote the growth of the Indian economy. Foreign investors and multinational corporations are typically interested in taking advantage of tax rate gaps between countries. As a result, there has been increased competition among governments to entice foreign investors by offering tax incentives.

Tax holidays are granted to a select group of companies – new entrants into a sector – rather than to all businesses operating in the jurisdiction. The tax breaks then give new businesses a competitive advantage over established businesses who have a longer-term view of the economy. Governments are being pushed to include more incentives so that non-holiday businesses can compete with tax-free businesses. Foreign investments have increased in India recently, but strict FDI policies have limited the potential growth in the sectors listed above.

“The introduction of the GST is a game-changing tax reform in India in terms of FDI. Reduced lawsuits and improved investor confidence would result from increased tax enforcement. In a slowing global economy, GST would provide the requisite boost to foreign trade and FDI, assisting the country's economic growth. GST is a destination-based tax that will make doing business in India simpler for multinationals. The world will eventually become one common market, with uniform pricing across states and optimal resource distribution, increasing the competitiveness of our products. A stable, open, and consistent tax regime in India would attract both domestic and foreign investment, resulting in significant job creation.”[[2]](#footnote-2)

**Chapter-2**

1. **Statement of the Problem-**

The aim of this study is to add to the existing data on the Taxation Regime and investment and their emerging issues. This research claims to include a detailed examination of India's Taxation Regime and investment.

This study would also look how tax system attracts more of foreign investments.

The stated problem in this research topic is to determine whether or not Taxation system plays a vital role in attracting investments. This question will be addressed in this study with the aid of several papers.

1. **Objectives of the study-**
* The main objective of the present study is to see whether Tax regime and Investment are interconnected or not.
* To see whether the taxing system in India suitable enough to attract FDI.
* To evaluate the above-mentioned objectives and come to a definitive conclusion about the objectives and the issue statement.
1. **Research Question-**
* Whether the GST is been of any use with regards to FDI?
* Whether the recent developments in taxation system attracting more FDI?
1. **Limitations-**

Because we have to limit our topic to only 2500 words, it becomes quite difficult to cover every aspect of the area in a comprehensive manner, and here in the given project, only a cursory glance of what the author is attempting to convey in the particular topic can be achieved, and also because it is a very fast topic, it became quite difficult at the outset as to how to begin the topic and what all areas to cover to make the present given topic apt and concise.

1. **Hypothesis-**

That tax system and the investment specifically the FDI are correlated with each other. GST is a major step to attract more FDI.

**Chapter-3**

**Research Methodology-**

The analysis methods used in this paper are a combination of empirical and doctrinal.

In order to conduct an empirical review, one must first analyses the available general facts, or information, and then use them to conduct an explanatory analysis of the topic.

This research uses doctrinal methodology. This method is used by a student to provide a descriptive and systematic study of legal rules found in primary sources such as books and records. The law is collected, organized, and defined using this method.

The aim of this research review is to add to an existing body of information. As a consequence, qualitative research is conducted to complement or add to the existing study.

To conduct a thorough review of the subject, various books and articles were used. I've even listened to a few theses and applied my general legal expertise to them. I've given credit to the author of any books I've used.

Empirical legal analysis is a form of qualitative, or non-numerical, legal analysis that involves gathering data from court documents, analyzing and organizing the text into categories, and then applying the information to recognize patterns, as the name implies.

**Chapter-4**

**Review of Literature-**

1. ***“A review of Tax Incentives and its impact on Foreign Direct Investment in India by Dr. Vinay Kandpal”[[3]](#footnote-3)*:** This paper tries to discuss that what are the tax incentives available on Foreign Direct Investment in India. The author after researching extensively came to a conclusion that Tax and Investment goes hand in hand and plays a major role in attracting big corporation for investing in countries and these investments play a major role in upliftment of the economy as a whole. In the present Article author even tries to discuss what led to liberalization in India during the period of 1991 and what led to the opening to markets and how FDI started inflowing the nation.
2. ***Impact of GST on FDI by Dr. Vivekshukla***[[4]](#footnote-4): The author of the said article attempts to address how FDI becomes even more important for a developing country like India, because FDI is the only way for India to provide industrial, fiscal, infrastructural, and employment-related solidarity in a country where 22 percent of the population is below the poverty line and 7.2 percent of the population is still unemployed.
3. For Indian planners and economists, the degree to which GST succeeds or fails in meeting this need is a source of great interest and study.

**Chapter-5**

**Recent Developments-**

A host of improvements have occurred in India's FDI fields over the last few years. Changes have occurred at both the national and international levels. On the domestic front, India's FDI strategy has undergone a range of changes, including the opening of several new sectors to FDI and the increase of FDI limits in some sectors. According to the findings of this report, India eventually amended its DTAAs with Mauritius, Singapore, and Cyprus in 2016 after nearly a decade of negotiations. The effective tax rates on investments in India from these jurisdictions would adjust as a result of these amendments.

The amended DTAAs have a grandfathering clause, which means that although these new rates were announced and will be enforced on April 1, 2017, fund flows between April 1, 2017 and March 31, 2019 will only be expected to pay 50% of the applicable rate, and only after that will all provisions of the amended DTAAs become fully applicable.

For e.g., if the new applicable rate is 15%, the rate for flows until the 31st of March will be 7.5 percent, and only from the 1st of April 2019 will the rate of 15% be payable. While the full effect of these reforms

can only be known until the new rates are fully enforced, based on the results of this report, the amendments could result in a decrease in the amount of money routed across more than three countries.

In terms of the effect of these amendments on FDI, practical FDI inflows are unlikely to be substantially impacted because their focus would not be on capital gains, since capital gains taxes are only applicable to inflows that have a primary focus on asset value appreciation. Changes in capital gains taxes, on the other hand, are unlikely to influence FDI inflows that are here for market access, production, or services.

The topic of bilateral investment treaties is another critical dimension that we have not addressed here (BITs).

India has recently begun the process of renegotiating BITs by ending existing treaties with 58 countries and requesting that 25 more countries sign joint interpretative statements to explain ambiguities in the treaty texts. One of them, by the way, is the Netherlands.

Another major global development is in the area of knowledge sharing. Countries share details with one another in order to tackle tax evasion and avoidance. Two signatory jurisdictions share information about their taxpayers with each other under this arrangement. For instance, if country A and country B have an exchange of information agreement, country A would provide country B with information on B's taxpayers who have assets in country A, and vice versa. Beginning in 2017, the Global Forum will automate the exchange of information among its member countries.

**Chapter-6**

**Tax Impact on FDI-**

India, like many other countries around the world, has re-examined its corporate tax rates in order to bring them into line with those of other countries, especially those in the ASEAN region. The Indian government has consistently matched its desire to have a fair tax climate for FDI with the need to ensure that multinationals pay an acceptable share of domestic tax.

With the implementation of Action Plan 4 of the OECD's Base Erosion and Profit Shifting Project in the Financial Year 2018, Section 94B was added to the Income Tax Act. This clause limits the amount of EBITDA that can be deducted for interest or other related expenses charged to non-resident affiliated entities to 30% of EBITDA. The provisions do not extend to banking companies, and the threshold cap for others is Rs. 1 crore. Furthermore, interest above the 30% cap can be carried forward for up to 8 years for set-off. Any Indian company that takes out foreign currency loans from related parties must be aware of the above provisions and properly prepare their debt-equity arrangement to avoid being penalized for paying too much interest.”[[5]](#footnote-5).

According to recent amendments, if a loan is obtained in foreign currency from a foreign lender before July 1, 2020, the interest payable on the loan will be taxed at a reduced rate of 5%, which will be determined in addition to the surcharge and education cess, as applicable from time to time under Section 194LC of the Income Tax Act. In light of the ECB's liberalisation, it's likely that the government will extend the 2020 deadline as well, in order to increase foreign inflows.

Furthermore, lenders who are tax residents of countries with which India has signed a Double Taxation Avoidance Agreement (“DTAA”) can demand a lower rate of tax on interest income as per the terms and conditions of the DTAA, with the tax rate usually varying from 0 to 15% if the income is derived and beneficially held by a tax resident of the respective country.

GST is a well-defined scheme of input tax credits that runs the length of the supply chain. The GST was created as a collection of much clearer tax rules on goods and services across India, with uniformity in tax rates and structures. Taxpayers can complete all procedures electronically, making enforcement simple and requiring minimal bureaucratic interference.

With the introduction of GST, foreign investors who were hesitant to invest in India would gain interest to do so, as the taxation mechanism would become more predictable. GST would necessitate less paper-work and document-work at the intermediary level, reducing red-tapism and corruption and increasing corporate accountability in terms of foreign investment done in India.

**Chapter-7**

**Analysis & Conclusion-**

With the GST reform, India is on the right track to unifying its internal market, increasing the ease of doing business, enhancing the country's prospects as a manufacturing base, and opening up new business opportunities for both Indian and foreign companies. GST can have both negative and positive impact on the mind of the Investors specifically foreign ones as they see how complex the GST laws are in India and we as a nation charge the second highest slab rates as per GST. So, this particular Act can be beneficial and at the same time not so helpful for foreign investors. Now, talking about the recent developments happened in India we can see how these developments are really helpful for a foreign investor who is looking to invest in India as discussed above. So we can conclude it by saying that Investors after proper due diligence of Tax reforms can invest in India.

**Chapter-8**

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