India Budget 2025

Impact on MNCs in India

February 2025

Preface

On 1 February, the finance minister presented the first full budget of Modi Government 3.0. Towards its vision of Viksit Bharat (Developed India), the government identifies agriculture, micro, small and medium enterprises, investment, and exports at the macro level as its four powerful ‘engines’, with reforms as its ‘fuel’ and inclusivity as its guiding spirit. The budget focuses on various development measures, including boosting manufacturing, furthering ‘Make in India’, enabling employment-led development, investing in people, the economy and innovation, securing energy supplies, promoting exports, and nurturing innovation. The budget also aims to initiate transformative reforms across six domains, including taxation, the power sector, urban development, mining, the financial sector and regulatory reforms.

The big news in tax is the proposed introduction of a new and simplified tax law, a draft of which is to be shared in the next few days. The other themes in the tax proposals include supporting domestic manufacturing and value addition, promoting exports, encouraging voluntary compliance and ensuring ease of doing business amongst others. However, there is no mention about the introduction of Pillar-Two rules in response to the global tax reforms. It seems that the Indian Government is adopting a ‘wait and watch approach’ on this front.

The budget proposals were tabled in the Parliament on 1 February. After due debate and discussions in the Parliament, the budget, with any other amendments that may be required based on the process in the Parliament, is to be legislated and become law with effect from 1 April 2025, or from other relevant dates for specific proposals.

While the budget includes numerous tax amendments and changes, which of the budget proposals impact you, as a multinational corporation (MNC), in doing business with Indian third-party customers or dealing with your Indian subsidiaries and affiliates? We present a concise summary of these key changes for your reference.

Doing business with India

Tax rates

No change in the headline tax rate for foreign or Indian companies

There is no change in the headline income-tax rate for foreign and Indian companies.

Customs duty rates

The proposed changes in Customs duty rates are strategically aligned with the Make in India initiative, aiming to bolster domestic manufacturing and promote local value addition. The overarching theme is to award duty concessions on the import of capital goods and raw materials meant for manufacturing in India, and to introduce duty hikes on the import of finished goods. Certain notable duty rationalisation measures revolve around the following:

- Capital goods for the production of lithium-ion batteries for electric vehicles and mobile phones
- Solar modules, other semiconductor devices and photovoltaic cells for use in renewable energy
- Formulations used in the production of life-saving drugs or medicines

Another notable change is proposed in the tariff slabs. The Indian Customs Tariff had as many as 22 duty slabs until last year. The government reduced the duty slabs to 14 in the last Union Budget, which is now further reduced to only eight slabs.

Overall, the duty rationalisation measures aim at not only augmenting local value addition in India but also strategically placing India in the emerging global geo-economics.

Introduction of the new simplified tax code

India's current tax law was introduced way back in 1961, and it was largely modelled on a 1922 law. The current tax legislation is a comprehensive piece of legislation that includes 298 sections across 23 chapters. Over the decades, this legislation has been tweaked repeatedly to address the changing business paradigm, within the same overall construct that dates back almost a century. This has resulted in a complex law that creates ambiguity and uncertainty in the tax law, resulting in increased tax litigation.

To address this, the government is working towards a new direct tax code (DTC). This effort to overhaul the income-tax law has been ongoing for several years. The journey began in 2009 when the then finance minister proposed the concept of a DTC. A draft of the DTC was unveiled in August 2009 for public consultation, but it never saw the light of day.

In 2017, the Modi Government revived the DTC and constituted a task force to draft new direct tax legislation. The task force submitted its report on direct tax reforms in 2019. This report was not made public nor was it implemented. However, it is believed that some parts of the proposals were incorporated in the law over the years through the annual budget-making process.

This journey now seems close to culmination. The Modi Government 3.0, in its first budget in July 2024, announced that a new law is to be unveiled in six months. Consistent with this announcement, the finance minister again announced in her budget speech yesterday that a draft law is to be introduced in the next few days.

The new DTC is expected to be clear and direct. The expanse of the law is also expected to be significantly shorter with only half of the present tax legislation, in terms of both chapters and words. It is proposed to be simple for taxpayers and administration to understand, leading to tax certainty and reduced litigation.

If the government delivers on these expectations, it would be a bold reform measure to create a simplified tax law with the potential to create a more transparent, efficient and business-friendly environment.

We keenly await the draft law. It is also expected to be open for public consultation, and comments may be considered before being legislated.

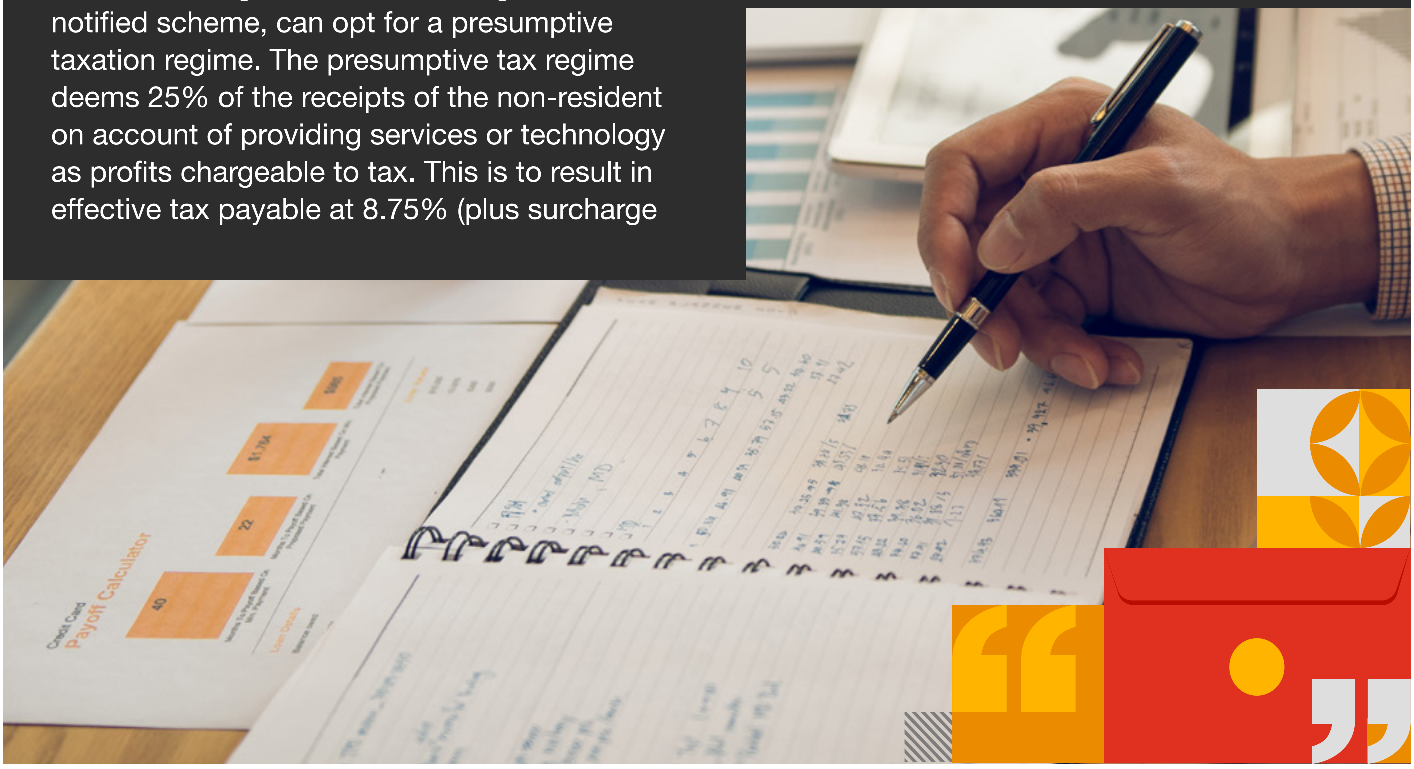
Presumptive tax regime for non-residents providing technology or service to India's electronics manufacturing Sector

India has been making significant strides in positioning itself as a global hub for electronics system design and manufacturing. It has been the prime minister's vision for India to become a global hub for semiconductor design, manufacturing and technology development. In line with this, the government has approved a comprehensive programme aimed at developing a robust ecosystem for semiconductors and display manufacturing. Under the programme, several schemes are introduced, including the production-linked incentive for large-scale electronics, Scheme for Promotion of Manufacturing of Electronic Components and Semiconductors, scheme for setting up semiconductor fabs in India and a design-linked incentive scheme.

In furtherance of the same, it is proposed that non-residents providing technology or services to Indian resident companies that are establishing or operating electronics manufacturing or connected facilities for manufacturing or producing electronic goods, articles or things in India, under a government-notified scheme, can opt for a presumptive taxation regime. The presumptive tax regime deems 25% of the receipts of the non-resident on account of providing services or technology as profits chargeable to tax. This is to result in effective tax payable at 8.75% (plus surcharge and cess) of the gross receipts. Non-residents opting for the presumptive tax regime cannot set-off any unabsorbed depreciation or brought forward losses for that year. The frequently-asked questions further clarify that provision of technical personnel is also eligible for the regime.

There seem to be a few drafting aspects that may need to be addressed before the law is enacted. The provision suggests that the regime will be available for technology or services provided 'in' India. This can give rise to a debate on whether this covers services or technology provided from outside India; hence, this should be clarified. In addition, the amount eligible for the presumptive taxation regime is the amount paid or payable to or payable on behalf of a non-resident 'and' the amount received or deemed to be received by or on behalf of the non-resident. The use of 'and' can create confusion, since the same amount can be paid as well as received by a non-resident and hence lead to double counting. We hope that these issues are addressed in the final law.

In addition, the finance minister in her speech also mentioned that a safe harbor is to be provided for non-residents who store components in India for supply to specified electronics manufacturing units. Details of the same are not provided yet.



International trade facilitation

Trade facilitation has been an area of policy focus for the government for the past several years. Continuing with the agenda, the government proposes a few trade-friendly measures in international trade laws.

Time-bound closure of provisional assessments

Indian Customs laws provide for provisional assessments of shipments wherever the Revenue authorities intend to seek further information from the importer, such as in the case of trade between related parties. The law does not prescribe any timelines for closure or finalisation of such provisional assessments. This creates ambiguity as the trade lacks certainty for several years until the assessment is finalised. The government has addressed this long-standing ask of the industry in this budget by prescribing a timeline of two years (extendable further by one year) to finalise such assessments, except in certain specified cases. It is also provided that for existing provisional assessments pending finalisation, the timeline of two years (extendable by one year) should start from the date of enactment of the budget proposals.

Having said so, the law does not clearly provide for the outcome where the Revenue authorities fail to finalise the assessment within the stipulated time period, i.e. whether the provisional assessment by the Revenue authorities is to be deemed to be finalised or the self-assessment made by the importer stands accepted. It is expected that the government will provide clarity on this issue in due course.

Voluntary disclosure of material facts post-clearance

The government has introduced a facility for voluntary revision of import and export declarations post-clearance (except in certain specified cases such as those involving ongoing investigations, audits and re-assessments). This provision allows businesses to either pay additional duty or seek a refund of duty, depending on the circumstances, without facing any punitive actions. This proposal is an example of the trust-based taxation regime the government has promoted.

Ease of compliance and provision of certainty in TP

Block audits

Currently, transfer-pricing (TP) audits are carried out every year along with the regular tax audit. The audit of each year in isolation puts constraints on the limited resources available with tax authorities, who then must complete many audits annually within a short time frame.

To streamline the process and provide an alternative to annual TP audits, the concept of block TP audits for a period of three years is proposed to permit multi-year arm's-length price determination, at the option of the taxpayer. It is proposed that the arm's-length price determined in relation to an international transaction or specified domestic transaction for a particular year (say Year 1) is to apply to similar transactions for two consecutive years (i.e. Years 2 and 3) immediately following the initial year (i.e. Year 1).

While the form, manner and time limit to opt for block TP audits are yet to be prescribed, this rationalisation measure is intended to ease the compliance and administrative burden on both the taxpayers and tax authorities.

Expanding the scope of SHR

The primary objective of the existing TP safe harbour rules (SHR) is to reduce TP disputes and provide more certainty to taxpayers. However, in its current form, SHR has not generated much enthusiasm among taxpayers due to various factors, such as limited coverage, perceived high margins and low thresholds for eligibility.

Similar to the announcement in the last budget, the finance minister in this budget once again reiterated the government's intention to expand the scope of the current SHR to reduce litigation and provide certainty in international taxation. While finer details on this proposal are still awaited, by rationalising the SHR, the government can usher in a more predictable and less litigious TP environment in India.

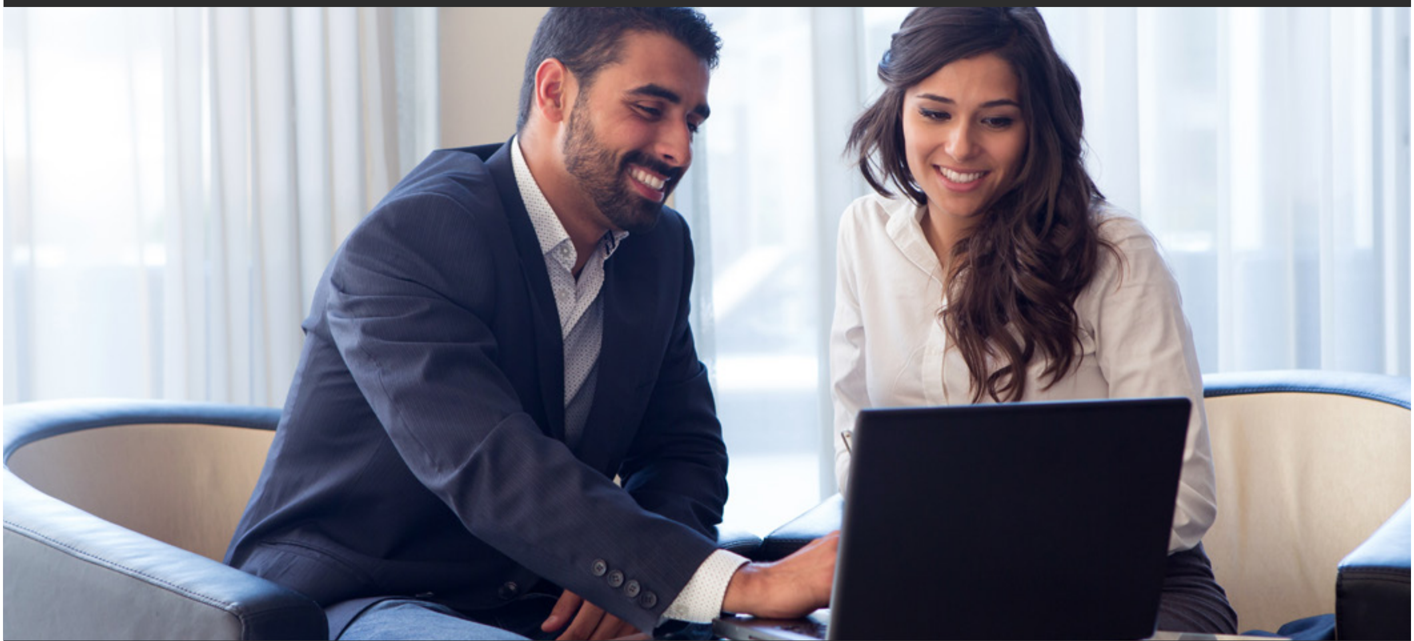
Investing in India

Incentives to the GIFT IFSC: A game changer

The current government continues to focus on reinforcing the International Financial Services Centre (IFSC) framework to solidify India's position as a prominent global financial hub.

The budget proposes a range of reforms designed to bolster the financial services sector, with specific attention to areas such as retail funds, insurance, ship leasing and treasury centres. These measures aim to enhance efficiency, attract investments and stimulate economic growth while ensuring a robust regulatory environment.

With these comprehensive reforms, the finance minister aims to attract a diverse range of businesses to the IFSC, reinforcing India's emergence as a formidable global financial hub and boosting investor confidence in the evolving financial landscape. A few key proposed incentives for the IFSC that may be relevant from the standpoint of MNCs are outlined below.



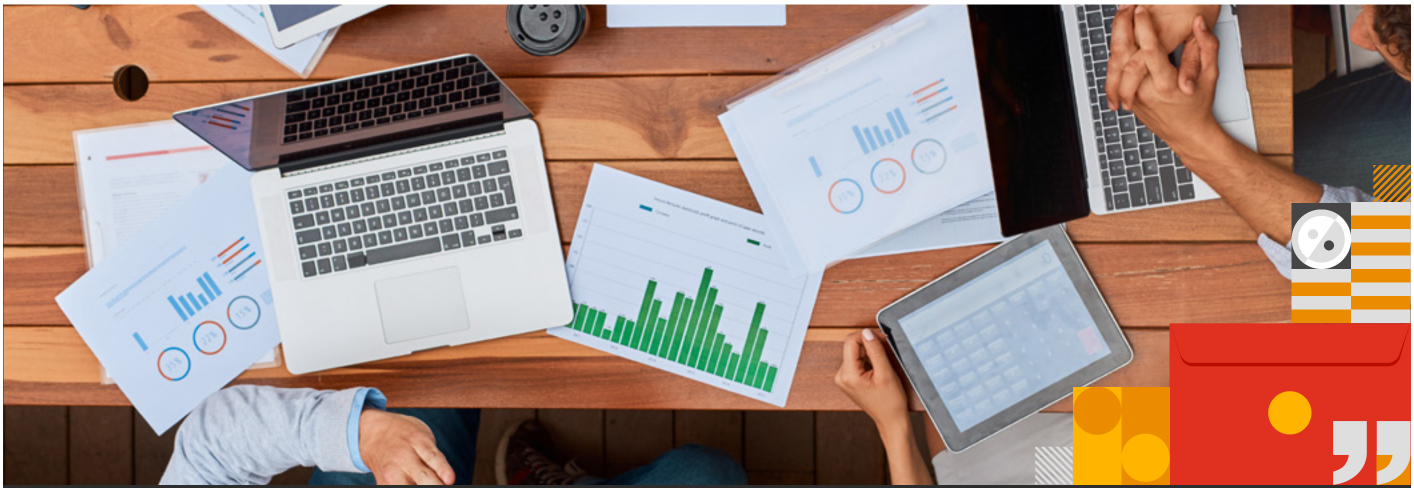
Relaxation from deemed dividend provisions for GTCs in IFSC

The budget introduces a significant change for MNCs looking to set up treasury operations in India. Currently, any loans or advances given by a closely held company to its shareholders or group entities are taxed as 'deemed dividend'. The budget now proposes to exempt such advances and loans between global treasury centres (GTCs) in the IFSC and other group entities of listed foreign parents or principal entities from the purview of 'deemed dividend'. Thus, it has made it much more attractive for MNCs to bring their treasury operations to the IFSC.

Extension of sunset dates prescribed in various Indian law

One key agenda of the government for the past several years is to provide tax incentives to businesses commencing operations in the IFSC. This is subject to certain sunset clauses. It is now proposed to extend these sunset clauses for the commencement of operations of IFSC units to 31 March 2030.

In addition, other measures for shipping and insurance are proposed. The proposals are transformative, significantly enhancing GIFT City's appeal as a global financial hub.



Unveiling the new 'India'

The budget has made a slew of policy announcements to accelerate the steady growth of last few years towards a 'Viksit Bharat'.

Start-ups

The government launched a fund of funds for start-ups in June 2016 with a corpus of INR100m. Under this scheme, the government provides capital to alternative investment funds, who in turn invest money in start-ups through equity and equity-linked instruments. With the support of this scheme, the alternative investment funds for start-ups have received commitments of more than INR910m.

Following the success of this scheme, this budget proposes two different initiatives: (a) a new fund of funds for start-ups with an expanded scope and a fresh contribution of another INR100m and (b) a DeepTech fund of funds to encourage next-generation start-ups from technical and non-technical backgrounds. These initiatives are to help provide seed capital to start-ups through domestic funding and also accelerate innovation and technological advancements in India.

The budget also proposes to extend the timelines to obtain a tax holiday for start-ups by another five years; i.e. the tax benefit is now to be available for eligible start-ups incorporated on or before 1 April 2030.

GCCs

Global capability centres (GCCs) in India are significantly transforming the corporate landscape and influencing global business dynamics. These centres are focusing on next-generation technologies and establishing artificial-intelligence centres of excellence, which are expected to drive innovation and solidify India's status as a global talent hub.

To leverage this opportunity, the budget has announced the creation of a national framework for GCCs. This framework aims to enhance talent availability and infrastructure by suggesting building-byelaw reforms to streamline regulatory processes and create a business-friendly environment. It also proposes collaboration mechanisms between the government and industry to meet the evolving needs of GCCs through coordinated efforts. By addressing these critical areas, the framework seeks to strengthen GCC capabilities; promote regional economic development, particularly in tier-2 cities; and reduce migration pressures on urban areas. This strategic initiative is expected to attract international investments, stimulate innovation and reinforce India's position as a global talent hub, contributing to the sustainable development of the GCC ecosystem in the country.

Make in India

In a significant move to bolster the country's manufacturing sector, the government has announced the establishment of a National Manufacturing Mission. This initiative is designed to accelerate the goals of the 'Make in India' campaign, aiming to transform India into a global manufacturing hub. The mission encompasses small, medium and large industries and focuses on providing comprehensive support across multiple dimensions, including policy frameworks, execution roadmaps and governance mechanisms. The mission ensures the creation of an enabling environment that facilitates business growth, attracts investment and drives innovation across the manufacturing ecosystem.

The mission's mandate focuses on five key areas to improve the ease and cost of doing business; build a future-ready workforce; foster a vibrant and dynamic micro, small and medium enterprises sector; prioritise the availability of cutting-edge technology; and ensure the production of high-quality products. With strong policy support and a clear execution framework, the mission is to play a pivotal role in driving sustainable growth and creating a competitive edge for India in the global marketplace.

CleanTech manufacturing

CleanTech manufacturing is driven by the need to address environmental challenges and the global shift towards sustainable development. The Indian Government has floated various schemes such as the National Solar Mission, National Electric Mobility Mission Plan, National Clean Energy Fund and production-linked incentive schemes. Continuing its path to foster a greener and more sustainable future for the country, the budget prioritises CleanTech manufacturing, targeting the production of solar photovoltaic cells, electric-vehicle batteries, motors and controllers, electrolysers, wind turbines, high-voltage transmission equipment and grid-scale batteries. These measures collectively aim to drive economic growth while fostering a sustainable and innovative industrial landscape in India.

Mergers and amalgamations

Mergers and amalgamations historically require a very time-consuming court approval process. With the enactment of the Companies Act, 2013, the concept of fact-track merger was introduced for the merger between a holding company and its wholly owned subsidiaries. In 2021, to promote start-up companies, the ambit of fast-track merger was extended to include the merger between two or more start-up companies and between one or more start-up company with one or more small company. As a next step, the budget proposes widening the scope of fast-track mergers and simplification of the existing company merger process, which is to result in speedy approvals and integration, realise synergies faster, and reduce legal and administrative costs.

Regulatory reforms

The budget proposes to set up a High-Level Committee for Regulatory Reforms for a review of all non-financial sector regulations, certifications, licences and permissions. The aim is to strengthen trust-based economic governance and take transformational measures to enhance 'ease of doing business', especially in matters of inspections and compliances.

In addition, significant announcements are made to increase foreign-direct investment to 100% in insurance (subject to some conditions) and measures aimed to make India a global hub for toy manufacturing.

All the above steps are poised to create a more conducive environment for business operations and foreign investments. With the objectives of accelerating growth, securing inclusive development, invigorating private sector investments, uplifting household sentiments and enhancing the spending power of India's rising middle class at its core, Budget 2025 has not just attempted but possibly accelerated the path to 'Viksit Bharat'. The measures are nearly all-encompassing (from the standpoint of sectors, demographics, etc.) and promise to ensure India's growth story follows only a skyward progression.

In summary

The budget proposals continue the theme of tax simplification, certainty and clarity, with a focus on encouraging voluntary compliance and reducing tax compliance. These have been the government's focus to provide the industry with a more tax-friendly environment—which has been the constant ask. Measures are also announced to attract investment and promote several focus sectors, including domestic manufacturing.

The finance minister has identified taxation as one of the domains of transformational reforms. This is very positive, and we hope that reforms will be implemented in all areas, including policy, compliances, systems, dispute resolution and tax administration, to provide a regime with easy compliance that provides certainty and a taxpayer-friendly approach. Against this backdrop, the DTC is awaited eagerly as it may set the tone for these reforms.

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