

Tax Exemptions For Offshore Fund Management & Offshore Banking In India At IFSC | Union Budget 2022

written by Soumen Ghosh | March 11, 2022



IFSC has announced Tax Exemptions For Offshore Fund Management. Since 1991, India has made serious strides towards the policy of economic liberalisation and towards offering clear and navigable pathways into investing in the country. The government has introduced several investment-friendly initiatives because it recognises the value of making India an attractive hub of investment for individuals, both national and foreign. Some steps have involved offering special privileges such as tax exemptions, healthy corporate ecosystems and access to one of the largest consumer bases in the world.

Tax Exemptions For Offshore Fund Management & Offshore banking in India Statistics reflect the effectiveness of these steps. According to reports, India attracted foreign investments up to 81.72 billion USD in FY 2020 – 2021 – a figure 10% higher than the previous year. To do so during the peak of the pandemic is certainly indicative of a worldwide economic shift away from China and further, of the generous investment policies offered by India. Key contributors to foreign direct investments (FDIs) are Singapore and USA and the states that attracted the most investment were Gujarat, Maharashtra and Karnataka. The government is keen to expand on these figures and one of the proposed moves is the development of the GIFT City and the IFSC (Indian Financial System Code) in Gujarat.

What Is the GIFT City?

The City, which is still under development, is purported to be the next big global financial hub much like New York or Singapore. The idea has been in development for more than a decade now. The City aims to focus on integrated development of 886 acres with 62 million square feet of built-up area constituting 67% of commercial space, 22% of residential space and 11% of social space. [1] It will notably consist of a conducive Multi-Service SEZ and an exclusive Domestic Tariff Area (DTA).

What's the IFSC?

An IFSC (International Financial Service Centre) is a jurisdiction providing financial services to both residents and non-residents, in foreign currency. The IFSC in Gujarat is the multi-service SEZ (Special Economic Zones) in the GIFT City which is being situated to provide easy access to the Indian economy. In January 2017, Prime Minister of India, Narendra Modi inaugurated

India's first international exchange in IFSC. This exchange includes trading across all asset classes such as equities, currencies, commodities, and fixed-income securities.

The GIFT City SEZ is the only place in India to be designated as an IFSC and the IFSC is India's first offshore financial centre. Currently, there are more than 125 licensed financial entities in IFSC. Over the years, it has witnessed dozens of vital regulatory developments such as the issuance of IFSC operating guidelines for Indian and foreign insurers by IRDAI (Insurance Regulatory and Development Authority) in 2017, to the setting up of India's first International Bullion Spot Exchange in 2020 and the issuance of the framework for aircraft operating leases by the IFSCA in 2021.

It also offers demarcations for domestic and export-oriented units; resident individuals are permitted to invest in foreign securities via IBUs. Recently, further light was shed on the status of tax exemptions regarding offshore fund management & offshore banking in India at IFSC in the Union Budget 2022. The Finance Minister has emphasised, via the following points discussed below, that the IFSC is intent on providing a very competitive cost of operations with various tax benefits, single-window clearance and CSR relief under various company law provisions.

Income Tax Exemptions to Promote Offshore Banking in India, Ship Leasing & Other Financing

The government's proposed income tax incentives aim to promote various business activities such as ship leasing & financing, offshore fund management & offshore banking in India activities at GIFT City. The union budget seeks to provide that income of a non-resident from offshore derivative instruments, or over the counter derivatives issued by an offshore banking in India unit, income from royalty and interest on account of lease of ship and income received from portfolio management services in IFSC shall be exempt from tax, subject to specified conditions.

Highlights in Brief:

- Section 10(4E) of the Income-tax Act, 1961 (IT Act) provides for tax exemptions on income accruing from/arising to/or received by a non-resident as a result of the transfer of non-deliverable forward contracts entered into with an Offshore Banking Unit (OBU) of an IFSC. *[This exemption is not extended to income accrued or arisen to or received by a non-resident as a result of the transfer of 'offshore derivative instruments' or 'over-the-counter derivatives' entered into with an OBU of an IFSC.]*
- Section 10(4F) of the IT Act provides tax exemption on royalty and interest income of a non-resident on the lease of an aircraft if it is paid by a unit in IFSC.
- Such tax exemptions are also extended to royalty and interest income of a non-resident on the lease of a 'ship' if it is paid by a unit of IFSC. (A 'ship' is defined to mean a ship or an ocean vessel, an engine of a ship or an ocean vessel, or any part thereof.)
- Additionally, Section 80-LA of the IT Act provides for the deduction of certain income of an IFSC Unit for 10 years out of the 15 years. This deduction is proposed to be extended to income arising from the transfer of asset being a 'ship' which was leased by a unit of IFSC to any person.
- It is proposed to introduce Section 10(4G) to provide exemption on income of a non-resident from a portfolio of securities or financial products or funds, managed or administered by any portfolio manager on behalf of such non-

resident, in an account maintained with an OBU in an IFSC, to the extent that such income accrues or arises outside India and is not deemed to accrue or arise in India.

- Deemed gift rules provided in Section 56(2)(viib) of the IT Act shall not apply to excess share premium received by an Indian Company from a Category I or Category II Alternate Investment Funds regulated under the International Financial Services Centre Authority Act, 2019.

IFSC AIF: Simple Vanilla Structure

Impact & Insights

These measures are expected to give offshore fund managers sufficient breathing room with regard to structuring funds based on negotiations with investors to improve upon returns. The tax exemption incentives provided in IFSC would encourage foreign investments in the financial services sector in India and enhance transacting with OBUs set up in IFSC. The incentives provided to aircraft leasing activities in IFSC had seen a lot of traction with many aircraft leasing companies setting-up operations in IFSC. Providing

similar incentives to ship leasing operations is likely to see the same result.

The Government has been consistently providing income tax incentives to encourage setting-up units in IFSC, which at the moment is located in the GIFT City. Carrying forward such a trend, the Union Budget 2022 has also laid down a plethora of proposals to provide incentives to units setting up in and doing business in IFSC.

The creation of state-of-the-art infrastructure would further augment this initiative. Providing tax exemptions on various instruments issued by OBUs would attract non-resident investing in India, thus strengthening the Indian financial services sector. Incentivizing 'ship' leasing activity would boost shipping companies to carry out ship leasing through IFSC as against any other overseas jurisdiction with which India has a favourable tax treaty.

[1]

<http://www.giftgujarat.in/documents/GIFT-City-Doing-Business-Booklet-April2021.pdf>

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