



Indian investing

Charles Gothard and Sanjeev Shah consider the main issues that can arise when planning for Indian investments or advising Indian clients

ABOUT THE AUTHORS (L-R)



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International focus on India has been increasing for the past few years. After periods of poor economic growth in the last three decades of the 20th century, India has made significant strides since the turn of this century. Today, India is one of the world's fastest growing and most dynamic economies (only lagging behind the Chinese economy).

Substantial increases in foreign direct investment flows into India have contributed to the boom in the Indian economy. Foreign direct investment into India increased by almost 300 per cent during the last financial year from USD5.5billion in the year ended 31 March 2006 to around USD16billion in the year ended 31 March 2007. Foreign direct investment into India now accounts for 6.8 per cent of its annual total investment, compared with just 0.5 per cent three years ago. Regulations governing foreign investment into India have been gradually relaxed by the Indian authorities during the past few years so that it is now much easier for a foreigner to make investments into India.

It is not just foreign investors who have benefited from the booming Indian economy. Resident Indians have also benefited from the positive economic conditions and there has been a marked increase in the level of entrepreneurial wealth in the country. The number of Indian billionaires ranked on the Forbes Rich List has increased every year since 2001. In 2007, India took over the title of the most number of billionaires in Asia from Japan. The number of Indian billionaires

in the Forbes 2008 Rich List increased by 12, bringing their total to 48 (this includes non-resident Indians). The total net worth of these 48 richest Indians is estimated to be USD271billion (having been USD191billion a year ago). In reality, it is likely that the total net worth of these billionaires is much higher.

Although the recent global economic downturn has affected the Indian stock market and the Indian economy, the Indian economy is still predicted to grow at a much faster rate than many of the major economies for the foreseeable future. Therefore, in the long term the outlook for India continues to be positive for foreign and domestic investors.

So, what are the main issues from an Indian perspective that you should be aware of when dealing with foreigners looking to make investments in India or Indian residents wishing to make investments overseas?

Indian tax exposure

Individuals who are resident in India for tax purposes are liable to Indian income tax on their worldwide income. Non-residents are liable to Indian income tax on income received or accrued in India or derived from a business controlled in India. 'Income' includes salaries, income from property, profits and gains realised from a business or profession, capital gains and other income for the purposes of Indian income tax. There is no estate tax in India at present but an annual wealth tax is charged on non-productive assets such as cash, motor cars, jewellery, yachts, boats and aircrafts not used for commercial purposes.

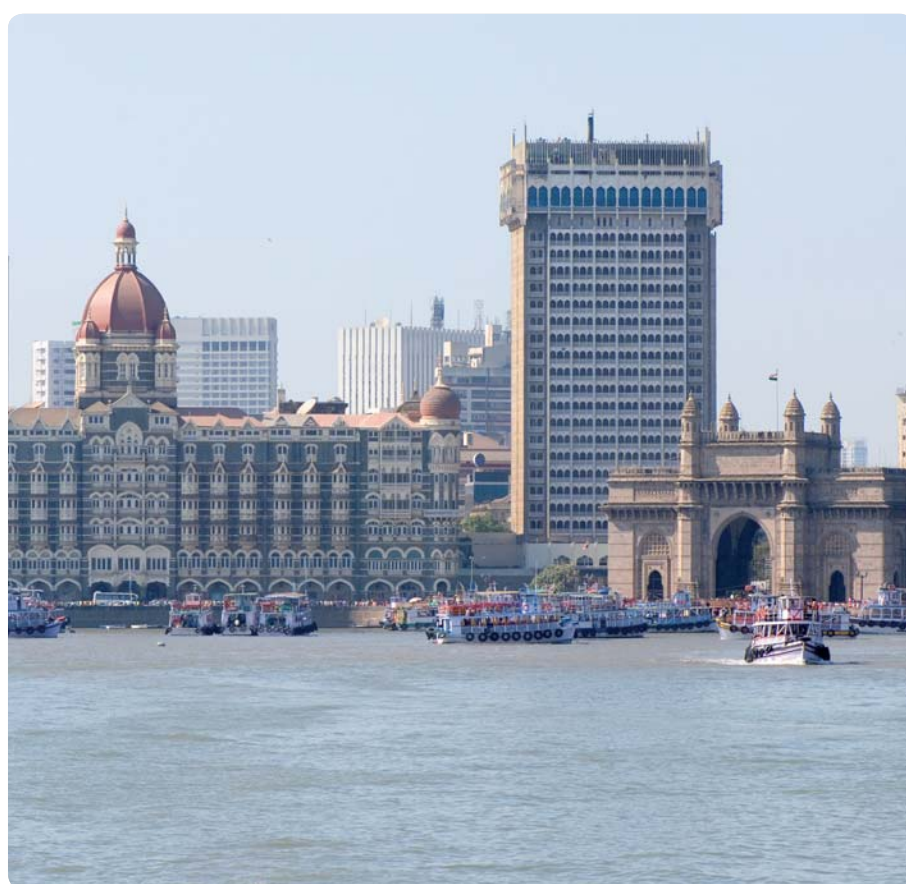
Many foreign investors avoid Indian tax on capital gains arising from the disposal of Indian investments through effective double tax treaty (DTT) planning. At present, India has favourable double tax treaties with Mauritius, Singapore, the Netherlands and Cyprus, for example. There has been some

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commentary in the press that the Indian government is seeking to renegotiate its DTTs with some of these jurisdictions, for example, to remove the exemption from Indian tax on capital gains and to include limitation of benefits provisions. However, the outcome of these negotiations remains to be seen. Recent statements from the Indian and Mauritian governments appear to suggest that they have temporarily agreed not to amend the Indian-Mauritian DTT. The pressure to amend it has come from the Indian government as a result of the number of foreign companies routing their investments into India via Mauritius. However, given the strong historical links between India and Mauritius, the consensus amongst the leading Indian and Mauritian advisors is that it is most unlikely that the treaty will be changed to any material extent.

The most appropriate route for investments into India

The most appropriate route for investment into India by a foreign investor will depend on whether or not he is a non-resident Indian (NRI) or a person of Indian origin (PIO) (as such persons are entitled to special concessions) and the nature of the asset to be acquired in India.



Institutional investors based outside India who wish to trade in Indian securities would normally do so via the FII route since an FII is subject to a lower rate of Indian income tax on capital gains realised. FII status is achieved through an application to the Securities and Exchange Board of India.

Indian residents looking to make investments abroad

The Indian authorities operate an exchange control regime that has been relaxed over the past few years. The regime applies to all Indian residents (individuals and companies) and restricts the amount of capital that can be transferred abroad.

At present, an Indian resident may transfer USD200,000 abroad in each Indian tax year for permitted capital and current account transactions, in addition to USD100,000 for 'education expenses' abroad and USD100,000 for medical treatment outside India.

For wealthy Indians, the use of an Indian company to make foreign investments continues to be popular as it can invest 400 per cent of its net asset value abroad. It is possible for the Indian company to implement strategies to ensure that any liability to Indian tax on these foreign investments is deferred as much as possible.

Advising foreigners who are considering making investments into India or Indian residents looking to diversify their assets by making acquisitions abroad, is not likely to be straightforward. It is essential that such clients take proper advice from suitable qualified professionals. As Indian families become wealthier and have increasingly internationally mobile family members, it is likely that they will become more interested in trusts and other vehicles as a means to preserve the family wealth and businesses for future generations. ■

An NRI is an individual living outside India who is an Indian citizen or a PIO. A person is of Indian origin if he is a foreign citizen (not being a citizen of Pakistan or Bangladesh) who held an Indian passport at any time or if he or either of his parents, grandparents or great grandparents was born in undivided India.

If the foreign investor is either an NRI or a PIO, then he can buy land and property directly in India. This is not possible for other foreigners. If an NRI or PIO is interested in purchasing shares in Indian quoted/unquoted companies, then special rules apply. Certain

methods such as the Foreign Institutional Investor (FII) route (see below) available to foreign investors generally are not available to NRIs or PIOs.

If a foreign investor (who is not an NRI or a PIO) is looking to acquire strategic shareholdings in quoted/unquoted Indian companies then the Foreign Direct Investment route is likely to be most suitable. If the foreign investor would like to invest in Indian real estate, then depending on the scale of the investment, either a joint venture with an Indian developer or a real estate fund is likely to be sensible.