India reduces tax rates for Indian companies

Executive summary

On 20 September 2019, the Indian Government enacted[1] a significant reduction of the corporate income tax rate for certain Indian companies, repealed the higher surcharge applicable to non-corporate taxpayers on certain capital market transactions and provided an exemption from the share buyback tax for listed Indian companies that publicly announced share buybacks prior to 5 July 2019, but had not completed the share buyback by that date.

This Alert summarizes the key changes.

Detailed discussion

Reduction of the corporate income tax rate for Indian companies

Indian companies can elect to apply a 22% corporate income tax rate,[2] a reduction from 25% or 30%,[3] effective for taxable years beginning 1 April 2019. If the election is made, most tax exemptions or incentives can no longer be claimed.[4] Once the election is made, it cannot be revoked in subsequent years. Electing companies are exempt from Minimum Alternate Tax (MAT).

Lower corporate tax rate for new manufacturing companies

Indian companies incorporated on or after 1 October 2019 that commence manufacturing operations on or before 31 March 2023 can elect[5] to apply a 15% corporate income tax rate.[6] If the election is made, most tax exemptions or incentives can no longer be claimed. The election is subject to meeting certain company formation and other conditions.[7] Once made, the election cannot be revoked in subsequent years. Electing companies are exempt from MAT.

Reduction in MAT rates

The MAT rate is reduced from 18.5% to 15%[8] for all other companies.[9]

Repeal of increased surcharge on capital gains

The Indian Budget 2019 significantly increased the surcharge rates for certain non-corporate taxpayers;[10] however, the increased surcharge has been repealed for: (i) non-corporate taxpayers deriving capital gains from the transfer of listed equity shares, units of equity-oriented funds, and business trusts when such transfers are subject to securities transaction tax; and (ii) foreign portfolio investors[11] deriving capital gains from the transfer of any securities.

Exemption from share buyback tax

The Indian Budget 2019 expanded the application of the share buyback tax to listed Indian companies for share buyback transactions occurring on or after 5 July 2019. However, as transitional relief, the tax does not apply to share buybacks of listed companies that were publicly announced prior to 5 July 2019 but were not completed by 5 July 2019.

Endnotes

1. The law is technically enacted and in force; however, it is subject to ratification by the Indian Parliament. Failure for the Indian Parliament's ratification causes the law not to be effective on the first day immediately following the tax year, although the chances of the law not being ratified by the Indian Parliament are highly unlikely.
2. Effective tax rate of 25.17% including peak surcharge and cess.
3. Effective tax rate of 26% to 34.94% including surcharge and cess.
4. Companies claiming tax exemptions or incentives can make the election in any year before or after the expiration of the exemption or incentive period.
5. In the company's first tax return.
6. Effective tax rate of 17.16% including peak surcharge and cess.
7. The new company should not be formed from the restructure of an existing business and should not use second-hand assets (subject to a threshold).
8. Effective tax rate of 17.16% including peak surcharge and cess.
9. For example, companies claiming tax exemptions or incentives.
10. The term may include pass-through partnerships and trusts.
11. That are not organized as companies or partnerships for Indian tax purposes (e.g., trusts).

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