India

India set to axe infamous retrospective tax provision

An August bill is repealing India's tax provision that allows New Delhi to impose retrospective taxes. Meanwhile, the Indian government is losing long drawn battles with Cairn and Vodafone on retroactive taxes.

"The Indian government is giving up claims on taxes due under such indirect transfers of Indian assets and is seeking to respect the original decision of the Supreme Court," said Aravind Srivatsan, tax leader at Nangia Andersen.

No tax will be levied on such capital gains up to May 28 2012, when the previous amendment came into effect. This comes with the condition of withdrawing litigation and an undertaking that no damages claims would be filed.

"The Bill proposes to amend the Income-tax Act of 1961 so as to provide that no tax demand shall be raised in future on the basis of the said retrospective amendment for any indirect transfer of Indian assets if the transaction was undertaken before May 28 2012," said the Finance Ministry in a public statement.

As per the bill, any taxes paid as a result of such claims in the past is now proposed to be refunded with the rider that the government would neither be liable for any interest due for any taxes adjusted or paid under protest nor liable for any costs payable following any awards.

This is good news for at least 17 companies including British energy company Cairn Energy and the telecom giant Vodafone that were embroiled in protracted litigation with the Indian government over the retrospective tax claims.

The 2012 retrospective tax provision had been a source of financial and reputational loss for India, severely damaging the country's reputation as an attractive place to do business. With international arbitration tribunals ruling against the Indian state in both instances, it's no surprise that the government decided to scrap the notorious tax.

An international arbitration tribunal ordered New Delhi to pay Cairn $1.7 billion in December 2020. India's legal standoff with Cairn culminated in the British company filing a lawsuit in a US court to seize aircrafts of state-owned carrier, Air India, in lieu of payment. Last month, a French tribunal ordered a freeze on property belonging to the Indian government in France as part of a guarantee of the amount owed to Cairn.

The amendment will enable a tax refund to Cairn, although without interest, while seemingly being settled under Indian law rather than complying with international arbitration rulings that India refused to honour.

"The reflection of this action shows a few things including that the government is willing to reverse a long held non-negotiable position and being pragmatic to business sentiments," said Srivatsan.

The ruling Bharatiya Janata Party (BJP) had fiercely criticised the retrospective tax law when the previous Congress party government pushed it through in 2012, describing it as "tax terrorism".

The move makes India attractive to foreign investors once again

The Indian government on August 5 introduced the Taxation Laws (Amendment) Bill 2021 in its lower house. The amendment would remedy a controversial 2012 retrospective tax law that allowed taxation of capital gains arising from indirect transfer of assets located in India through the transfer of the shares or interest in an entity registered or incorporated outside India.

By withdrawing the retrospective amendment to the 'indirect transfer' provision in Section 9 of the Income Tax Act – originally introduced in the 2012 Union Budget – the indirect transfer provision will apply prospectively.