MARKET ENTRY BRIEFING

TAXATION IN INDIA

What Should a New Business Expect?

A Practical Guide for Foreign Business Leaders

Article 5 of the Doing Business in India series.
Previous editions covered Why India, Business Structures, Incorporation and Registrations & Compliance.

GUIDE STRUCTURE

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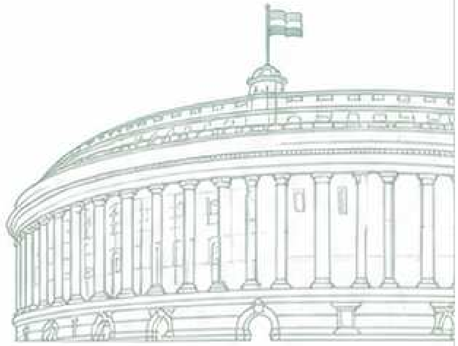
ADVISORY NOTE

This document is prepared for strategic orientation. Market entry decisions should be supported by localised due diligence and professional advisory services.

01 | THE TAX QUESTIONS THAT MATTER



Foreign businesses often begin with:
"What is the corporate tax rate?"

It matters. But it does not determine the full tax cost of operating in India.

The more important questions are:

- Which entity will conduct the India business?
- How will it earn revenue?
- Will goods, software, services or intellectual property move between group companies?
- How will the operation be funded?
- How will profits return to the foreign parent?
- Will the business operate in one Indian state or several?
- Could local employees, agents or digital activity create tax exposure for the foreign parent?

A business may have a competitive corporate tax rate and still lose cash through:

- incorrect GST treatment
- blocked input tax credit
- withholding tax gross-ups
- delayed overseas payments
- unsupported group charges
- an unplanned taxable presence

Tax should be designed into the operating model — not added after transactions begin.

India's current direct-tax framework is governed by the **Income Tax Act, 2025** for tax years beginning on or after 1 April 2026.

02 | CORPORATE TAXATION

An Indian subsidiary is taxed separately from its foreign parent. It maintains its own accounts, calculates taxable profit, files its own tax return and pays Indian corporate tax.

Concessional Corporate Tax Regime

Domestic companies may opt for a:

22% base tax rate

After surcharge and 4% health and education cess, the effective rate is approximately: **25.17%**

This regime is commonly used by foreign-owned subsidiaries because it offers:

- a predictable rate
- no turnover-based eligibility ceiling
- exemption from Minimum Alternate Tax
- simpler long-term forecasting

Important: The 22% concessional regime is not automatic. It requires a formal opt-in by the company. Once elected, certain deductions and exemptions under the standard regime are permanently foregone. The election should be evaluated with professional advice based on the specific nature of the business.

Practical View: The 22% regime is often attractive for service companies, trading businesses, technology centres and Global Capability Centres. Manufacturing and capital-intensive businesses should first compare the value of available deductions and incentives before opting in.

Standard Corporate Tax Regime

Companies outside the concessional framework may generally face a base rate of:

- **25%** for eligible domestic companies; or
- **30%** for other domestic companies,

plus applicable surcharge and cess.

This regime may remain useful where deductions or incentives produce a better overall result.

Minimum Alternate Tax

Relevant companies remaining in the standard regime may also be subject to Minimum Alternate Tax (MAT).

From Tax Year 2026–27:

- MAT applies at 14% of book profit
- it operates as a final tax for that year
- no new MAT credit is generated

Companies using the concessional 22% regime remain outside MAT.

India's current direct-tax framework is governed by the **Income Tax Act, 2025** for tax years beginning on or after 1 April 2026.

What Is Actually Taxed?

Corporate tax is charged on taxable profit — not revenue and not automatically on accounting profit. Expenses may be restricted where they are:

- Unsupported
- Unrelated to Indian business
- Capital in nature
- Paid without required WHT
- Not at arm's length
- Subject to statutory payment conditions

Common risk areas include:

- management and technical service fees
- royalties
- group interest
- reimbursements
- employee provisions
- parent-company cost allocations

The Key Test

For a group charge to be defensible, the Indian entity should be able to show:

1. what was supplied
2. why it benefited
3. how the amount was calculated
4. why the price is commercially reasonable
5. whether the correct taxes were applied

Early-Year Losses

New businesses often incur losses during setup. These losses may generally be carried forward, subject to prescribed conditions. But they are useful only if the same entity later earns taxable profits.

Do not separate setup costs, revenue and future profitability across entities without modelling the tax effect.

03 | GST AND WORKING CAPITAL

Goods and Services Tax is India's principal indirect tax. For a new entrant, it directly affects pricing, invoicing, imports, supply chains, interstate activity, input tax credit and working capital.

Registration

GST registration is generally required once turnover crosses the prescribed threshold, which varies depending on the nature of supply (goods or services) and the state of operations. The thresholds differ for goods suppliers and service providers, and are lower in specified states.

However, turnover is not the only test. Registration may also depend on:

- interstate activity
- e-commerce
- non-resident status
- reverse-charge obligations
- business presence in a particular state

Many B2B businesses register early because Indian customers expect a GST invoice to claim input tax credit.

GST Is State-Specific

A business may require separate registrations in different states. A new office, warehouse, branch or inventory location can create additional GST obligations.
This should be assessed before choosing operating locations — not after the business expands.

Current Rate Environment

India substantially rationalised GST rates from 22 September 2025. Most supplies now fall principally within:

5%	standard rate (essential goods, selected services)	**18%**	standard rate (most goods and services)

A small number of items remain in the 0% and 12–40% slabs. The exact rate depends on the nature of supply, classification and place of supply.

Input Tax Credit

A registered business may generally offset eligible GST paid on purchases against GST collected on sales. Credit, however, depends on valid documentation and supplier compliance.

Common risks include:

- incorrect vendor reporting
- invalid invoices
- blocked credits
- missed claim deadlines
- non-business use

Input tax credit is partly dependent on your vendors. Vendor screening and invoice reconciliation are working-capital controls — not merely tax administration.

Cash Flow Impact

GST is paid upfront at each stage, while ITC is realised only after compliance conditions are met. Poor supplier compliance or inventory held in one state and sold in another can significantly affect working capital.

Strategic Takeaway

Correct GST registration, documentation and supply-chain design can improve margins, speed up ITC realisation and prevent avoidable working-capital strain.

Imports

Imports of goods generally attract customs duty and import GST. Import GST may be creditable. Customs duty generally becomes part of the landed cost.

This can materially change the economics of importing finished goods, importing components, assembling locally, manufacturing in India or using an Indian contract manufacturer.

Overseas Services

Services received from a foreign parent or overseas supplier may attract GST under reverse charge. Typical examples include software, cloud services, management support, technical services, royalties and shared technology platforms.

Each payment should be reviewed for GST, withholding tax, deductibility and transfer pricing.

Exports

Eligible exports are generally zero-rated. Businesses may export under a Letter of Undertaking without paying integrated tax, or pay the tax and claim a refund, subject to the applicable rules. The commercial risk is refund delay.

Poor export documentation can turn a tax-neutral model into a working-capital problem.

04 WITHHOLDING TAX AND OVERSEAS PAYMENTS

India has an extensive Tax Deducted at Source (TDS) system.
The payer must deduct tax from specified payments and deposit it with the government.

Common payments that attract withholding tax

- salaries
- rent
- professional and contractor fees
- interest
- royalties
- technical service fees
- dividends
- payments to non-residents
- and other specified payments

Failure to comply can result in

- interest and penalties
- disallowance of expense in your tax computation
- delayed overseas payments
- tax demands and exposure for the payer

The Gross-Up Risk

An overseas supplier may expect to receive the full invoiced amount.
Indian law may require tax to be withheld before payment. Where the contract requires the Indian company to bear that tax, the payment may need to be grossed up — materially increasing the real cost.

Cross-Border Contracts Should State

- whether the price is gross or net of Indian tax
- who bears withholding
- whether treaty relief will be claimed
- who provides tax-residency documents
- whether GST applies

Resolve withholding before agreeing the price — not when the invoice becomes payable.

Treaty Relief

Payments to foreign companies may be taxable in India where they represent royalties, technical or consultancy fees, interest, dividends, Indian-source income or income connected with an Indian taxable presence.

A tax treaty may reduce or eliminate Indian tax. But treaty relief is not automatic.
The foreign recipient may need to provide:

- a Tax Residency Certificate
- beneficial-ownership support
- a permanent-establishment declaration
- the agreement and invoice
- evidence of the service or right supplied

When Withholding Tax Is Not Deducted

Where the Indian payer fails to deduct or short-deducts tax on a payment to a foreign company, the foreign company is not absolved of its Indian tax liability. Under the Income Tax Act, 2025, a foreign company that receives income from India on which tax has not been deducted or has been short-deducted may be required to file an Indian income tax return and pay the applicable tax directly.

This means a foreign parent or group company receiving royalties, technical service fees, interest, or other India-sourced payments cannot simply assume the Indian payer has handled the tax. If the payer has not deducted correctly, the foreign company itself may have an obligation to file a return in India and discharge the tax liability. The foreign company should independently verify that correct withholding has been applied — particularly where treaty rates are being claimed — and retain documentation to support the position taken.

Practical Implication

European parent companies should not treat Indian withholding tax as solely the Indian subsidiary's responsibility. If withholding is missed or applied incorrectly, the foreign **company may** face a direct Indian tax filing and payment obligation — along with potential interest and penalties.

Withholding Tax Rates: Domestic and Treaty Positions

The following table summarises the key withholding tax rates on common cross-border payments under the Income Tax Act, 2025 and the indicative treaty position under most India–EU DTAAs.

Payment Type	Domestic Rate	Typical DTAA Rate	Notes
Dividend	20%	10%	DTAA rate typically 10%, subject to beneficial ownership, TRC, and minimum shareholding conditions where applicable.
Fees for Technical Services (FTS)	20%	10–15%	Varies by treaty. Some treaties do not have a separate FTS article — in such cases, FTS may fall under Business Profits (taxable only if PE exists).
Royalty	20%	10–15%	Varies by treaty. Definition of royalty under the Act and under the treaty may differ — verify scope before applying the rate.
Interest	20%	10–15%	DTAA rate typically 10–15%. ECB interect may attract a lower rate under specific treaty provisions. FEMA conditions also apply to the underlying loan.

All domestic rates are base rates exclusive of applicable surcharge and cess. Effective rates will be marginally higher. Treaty rates apply only where valid documentation (Tax Residency Certificate, beneficial ownership declaration, Form 10F) is provided before the payment date.

DTAA Relief Is Available — But Not Automatic

Where a Double Taxation Avoidance Agreement exists between India and the European country of residence, the foreign recipient is entitled to the lower of the domestic rate or the treaty rate. However, claiming treaty relief requires the foreign company to provide a valid **Tax Residency Certificate (TRC)** issued by the tax authority of its home country, a completed **Form 10F** (self-declaration of treaty eligibility), and supporting documentation establishing **beneficial ownership** and the **nature of the payment**. Without this documentation, the Indian payer is required to withhold at the **full domestic rate.**

Foreign Tax Credit (FTC)

Tax withheld in India on payments to the European parent is generally available as a credit against the parent's home-country tax liability, subject to the FTC provisions of the relevant DTAA and the domestic tax law of the European country. This means that Indian withholding tax need not always represent a final cost — it may be creditable in the parent's jurisdiction, reducing the overall group tax burden.

However, FTC is subject to conditions: the credit is typically limited to the **lower of the Indian tax paid and the home-country tax attributable** to the Indian income, and **specific documentation and filing requirements** must be met in the home country.

European companies should confirm FTC eligibility and mechanics with their home-country tax advisors at the **structuring stage** — not after tax has already been withheld.

Remittance Documentation

Current foreign-remittance compliance uses:

- Form 145 for prescribed payment information; and
- Form 146 for accountant certification in applicable cases.

For management, the key point is simple: complete the tax review before treasury schedules the payment — not after the bank blocks it.

05 FUNDING, DIVIDENDS AND PROFIT REPATRIATION

Making profit in India and transferring value to the foreign parent are separate steps.

Common routes include:

- dividends
- service fees
- royalties
- interest
- capital reduction
- share buyback

Common routes include:

- share sale
- liquidation

Each route has different tax, GST, transfer pricing and foreign-exchange consequences.

Equity Funding

Equity is often the simplest long-term funding route. The former angel-tax provision no longer applies from 1 April 2025. An Indian company is therefore no longer taxed merely because shares are issued at a premium above the former prescribed tax valuation.

However, foreign investment must still comply with:

- FEMA pricing rules
- Companies Act requirements
- valuation norms
- beneficial-ownership disclosures
- source-of-funds documentation

Dividends

An Indian subsidiary may distribute post-tax profits as dividends, subject to corporate-law requirements. There is no separate dividend distribution tax on the Indian company.

The foreign shareholder is taxed on the dividend, with withholding at the applicable domestic rate, subject to a more beneficial treaty rate. The **lowest treaty rate** is not automatic. Eligibility may depend on residence, beneficial ownership, **commercial substance** and supporting documents.

Service Fees and Royalties

Service fees and royalties may provide legitimate routes for paying the foreign parent. They must, however, reflect actual services or rights.

The Indian entity should be able to show:

- what was provided
- the business benefit
- the calculation basis
- the arm's-length price
- withholding treatment
- GST treatment

Generic descriptions such as "global support fee" are rarely sufficient.

Debt Funding

Debt may provide an interest deduction, but it also creates wihholding tax, transfer pricing, FEMA conditions, interest-deduction limits, repayment obligations and currency risk.

Choose debt because it suits the business — not only because interest may be deductible.

Exit

Share sales, buybacks, capital reductions and liquidation may create capital-gains and withholding consequences.

Long-term gains are generally taxed at 12.5% without indexation, subject to the asset, transaction and applicable treaty.

The holding period is broadly:

- **12 months** for specified listed securities; and
- **24 months** for most other capital assets.

Repatriation and exit should be considered at entry — not after profits accumulate.

06 TAX TREATMENT BY BUSINESS STRUCTURE

The following table summarises the indicative tax position and strategic considerations for each business structure.

Structure	Indicative Tax Position	Main Route for Returning Value	Key Concern	Strategic View
Indian Subsidiary	Domestic-company regime; 22% concessional rate may apply (requires formal opt-in)	• **Dividends** (WHT 20% / DTAA ~10%) • **Fees** (WHT 20% / DTAA 10–15%) • **Royalties** (WHT 20% / DTAA 10–15%) • **Interest** (WHT 20% / DTAA 10–15%)	Withholding and transfer pricing	Usually the most predictable long-term model
Joint Venture	Same broad corporate-tax framework as a subsidiary	Dividends and permitted shareholder payments	Related-party terms and exit design	Suitable where a local partner adds strategic value
LLP	30% base rate plus surcharge and cess	Partner profit share	Higher entity-level tax	Selectively useful for professional or closely held businesses
Branch Office	Foreign-company rate, generally 35% plus surcharge and cess	Post-tax branch-profit remittance	Direct parent exposure	Often less tax-efficient than a subsidiary
Liaison Office	No operating profit expected	Parent-funded	Taxable-presence risk if activities become commercial	Only for genuinely representative activity
Project Office	Foreign-company rate on attributable project profit	Project-profit remittance	Contract and profit attribution	Relevant for defined projects
No-entity model	Depends on Indian nexus	Offshore revenue model	PE or SEP exposure	Works only where Indian activity remains limited

LLP Rate Note

An LLP's effective rate is approximately **31.20%** where no surcharge applies, and **34.94%** where the 12% surcharge applies on income above **INR 1 crore (approximately USD 120,000)**, subject to marginal relief.

Strategic Takeaway:

Select the structure based on the combined effect on operations, control, funding, tax, repatriation and exit. A structure that is quick to establish is not necessarily efficient to c

The Arm's Length Principle

The core requirement is that the price charged in a transaction between associated enterprises must be the same as the price that would have been charged between independent parties in comparable circumstances.

India's transfer pricing law prescribes specific methods for determining the arm's length price:

- **Comparable Uncontrolled Price (CUP) Method** — compares the price in the controlled transaction with the price in a comparable uncontrolled transaction.
- **Resale Price Method (RPM)** — starts with the resale price to an independent buyer and deducts an appropriate gross margin.
- **Cost Plus Method (CPM)** — starts with the costs incurred by the supplier and adds an appropriate markup.
- **Profit Split Method (PSM)** — splits the combined profit from a transaction between the associated enterprises based on their relative contributions.
- **Transactional Net Margin Method (TNMM)** — compares the net profit margin of the tested party with that of comparable independent enterprises. This is the most commonly used method in practice.
- **Other Method** — any method that produces a result consistent with the arm's length principle, including the use of valuation techniques for intangible property transactions.

The "most appropriate method" must be selected based on the nature of the transaction, the availability of reliable comparables, and the **functions performed, assets used, and risks assumed** by each party (the **FAR analysis**).

07 DOCUMENTATION REQUIREMENTS

India's transfer pricing documentation requirements are extensive and must be maintained contemporaneously — meaning the documentation should be prepared during the year, not assembled retrospectively at year-end.

KEY DOCUMENTATION INCLUDES:

- **Transfer Pricing Study / Report** — a detailed analysis of each international transaction, the method selected, the comparability analysis, and the arm's length price determination. This is the primary document that the tax authority will review.
- **Form 3CEB** — a statutory report certified by a Chartered Accountant, filed with the income tax return. It reports all international transactions and the methods used. Due by **30 November** for companies subject to transfer pricing.
- **Master File and Country-by-Country Report (CbCR)** — required for groups with consolidated revenue exceeding the prescribed threshold. The Master File provides a global overview of the group's transfer pricing policies; the CbCR provides country-level financial data.

The main risk is not usually the absence of an agreement between the parties. It is the absence of evidence supporting the price.

Common weaknesses include:

- vague service descriptions that do not demonstrate what was actually provided
- unsupported markups with no benchmarking analysis
- no evidence that the Indian entity actually benefited from the service
- pricing that is inconsistent with the actual functions performed by each party
- large year-end adjustments that suggest prices were set retrospectively
- mismatches between tax filings, GST records, and accounting entries

Transfer pricing should operate throughout the year — not exist only as a year-end report. Prices should be set before transactions occur, documented as they happen, and reviewed periodically. A year-end report that does not reflect real-time pricing is a **red flag** for the tax authority.

Transfer Pricing Assessments and Disputes

India has a dedicated Transfer Pricing Officer (TPO) who may review the transfer pricing documentation during an assessment. If the TPO determines that a transaction is not at arm's length, **the adjustment is made to the Indian entity's taxable income** — increasing the tax liability, plus interest and potentially penalties.

Transfer pricing disputes are common and can involve significant amounts. The assessment process can take several years, and appeals may extend the timeline further. For this reason, robust contemporaneous documentation is the **single most important defence.**

TPO REVIEW FOCUS AREAS

- Documentation Review
- Comparability Analysis
- Arm's Length Test
- Adjustment

Advance Pricing Agreements

For European companies with significant and recurring intercompany transactions, India offers the option of Advance Pricing Agreements (APAs) with the Central Board of Direct Taxes. An APA provides certainty on transfer pricing methodology for a defined period (**up to 5 years, with a possible 4-year rollback**).

Unilateral, **bilateral** (between India and the treaty partner country), and **multilateral** APAs are available.

An APA **eliminates** the risk of transfer pricing disputes and assessments for the covered transactions during the agreement period.

The process involves detailed documentation, economic analysis, and negotiation with the tax authority, but for companies with large intercompany volumes, the certainty it provides can materially outweigh the preparation cost.

PRACTICAL TAKEAWAY: Transfer pricing is not a year-end compliance exercise. It is an operational discipline that must be embedded in the way the Indian entity transacts with its group from day one. **Set prices before the transaction, document as you go, benchmark annually, and file Form 3CEB on time.**

08 Taxable Presence

A foreign company can become taxable in India without incorporating a local entity. This concept — broadly referred to as Permanent Establishment (PE) under tax treaties, or business connection under the Income Tax Act — is one of the most significant and frequently underestimated tax risks for European companies operating in or with India.

How Taxable Presence Arises

Risk may arise where Indian employees, agents, or representatives of the foreign company:

- **negotiate or conclude contracts** on behalf of the foreign company
- habitually **secure orders** for the foreign company
- maintain **inventory or stock** of goods in India
- provide **core services** that generate revenue for the foreign company
- perform **revenue-generating functions** on a sustained basis
- operate without **genuine independence** from the foreign company

"**Actual conduct matters more than job titles or contract wording.**

The tax authority will examine **what people actually do** in India — not what the contract says they should do."

Why It Matters

If a PE or business connection is established, the foreign company becomes liable to Indian tax on profits attributable to its Indian activities. This can result in:

- corporate **tax liability** on attribubable profits
- **retrospective assessments** covering multiple years
- **interest** and **penalties**
- **transfer pricing implications** on the attribution of profits
- **double taxation** where the foreign company's home country also taxes the same income

Digital and Remote Business

Foreign digital businesses should also assess **Significant Economic Presence (SEP).**

Prescribed transactions or sustained interaction with Indian users may create an Indian business connection even without a physical office.

India has abolished the former Equalisation Levy, but **digital businesses must still consider:**

- **GST** on services to Indian customers
- withholding tax on payments received from India
- Significant Economic Presence thresholds
- permanent establishment under the applicable treaty
- treaty exposure and relief availability

Taxable presence is assessed based on facts on the ground — **not on the structure shown in the organisation chart.** European companies with employees travelling to India, agents operating in India, or significant Indian customer activity should assess PE and SEP risk as part of their India strategy — not as an afterthought.

09 | FIRST-YEAR TAX READINESS

BEFORE ENTRY

- Compare **tax outcomes** across structures
- Review **treaty** implications
- Decide the **funding mix**
- Map **repatriation routes**
- Assess **taxable-presence** risk
- Evaluate whether the **22% concessional regime** should be elected

Start prepared.

The first year sets the tone for compliance, tax efficiency, and long-term certainty. Early planning reduces risk, cost, and disruption.

BEFORE THE FIRST INVOICE

- Confirm **GST registration** at the place of business
- Verify **classification and rate**
- Determine **place of supply**
- Configure **invoicing**
- Set up **customer and vendor tax data**

BEFORE THE FIRST PAYMENT

- Determine **withholding tax**
- Review **gross-up clauses**
- Collect **vendor documents**
- Establish **payment and filing controls**

BEFORE THE FIRST OVERSEAS REMITTANCE

- Classify the **payment**
- Review **treaty eligibility**
- Collect **residency documents**
- Determine **withholding and GST**
- Prepare **Forms 145 and 146** where applicable
- Allow time for **bank review**

DURING THE FIRST YEAR

- Reconcile **GST** regularly
- Monitor **vendor compliance**
- Retain **evidence for group charges**
- Review **transfer pricing** during the year
- Monitor **advance tax** and **electronic notices**
- Maintain one **compliance calendar**
- Appoint **statutory auditor** within 30 days of incorporation (if not already done)

A strong first year sets the foundation for **lower tax risk, smoother compliance**, and **better cash flows.**

10 Final Perspective

A new business entering India should expect tax to influence more than annual profit. **It affects:**

pricing	contracts	imports
working capital	funding	overseas payments
group charges	profit repatriation	exit planning

The objective is not simply to obtain the lowest headline rate. **It is to create a structure** in which:

- the tax cost is understood
- cash-flow leakage is controlled
- payments are not delayed
- intercompany charges are supportable
- profits can be repatriated efficiently

> In India, **tax efficiency** is not created when the return is filed.
> **It is created when the business model is designed.**

Disclaimer: This document provides strategic orientation, not technical tax advice. Actual outcomes depend on the business model, legal structure, transaction terms, location and applicable tax treaty. All tax rates reflect the framework under the **Income Tax Act, 2025** as understood in July 2026. GST rates reflect the rationalised structure effective from **22 September 2025**. Readers should consult qualified Indian tax and regulatory advisors before making decisions.
Tax laws and rates are subject to change.

INDIA MARKET ADVISORY

Entering India successfully requires more than market interest - it requires the *right structure.*

Whether you are evaluating India for the first time or ready to move, the right tax strategy, compliance readiness, and operational structure can shape long-term success. GSRA & Associates works with international businesses to build that foundation.

HOW WE SUPPORT BUSINESSES ENTERING INDIA

Trusted advisors for India market entry, structure, compliance, and operations. GSRA & Associates supports international businesses with India entry, structuring, regulatory compliance, and day-to-day operational readiness.

- Entry structure & incorporation advisory
- Tax planning & transfer pricing strategy
- GST, withholding tax & remittance planning
- Regulatory compliance & FEMA / RBI advisory
- Accounting, payroll & compliance support
- India market entry coordination & ongoing advisory

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