

TAX FLASH NEWS

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CBDT prescribes conditions for exemption of income earned by a non-resident on transfer of non-deliverable forward contracts entered into with an offshore banking unit located in IFSC

Background

The non-residents typically hedge their exposure to Indian Rupee (emanating from investments / income receivable from India) by entering into non-deliverable forward (NDF) contracts with banks outside India. With a view to incentivize execution of such NDF contracts in India, the Finance Act, 2021 introduced Section 10(4E) that provides an exemption for the income earned by a non-resident from transfer of non-deliverable forward contracts entered into with an offshore banking unit located in IFSC subject to prescribed conditions.

Recently, the Central Board of Direct Taxes (CBDT) has issued a Notification¹ introducing a new Rule 21AK under the Income-tax Rules, 1962 (the Rules). The new rule prescribes the conditions for availing the exemption under Section 10(4E) of the Income-tax Act, 1961.

CBDT Notification

The income accrued or arisen to, or received by, a non-resident as a result of transfer of non-deliverable forward contracts under Section 10(4E) shall be exempted subject to fulfillment of the following conditions:

- The non-deliverable forward contract is entered into by the non-resident with an offshore banking unit of an IFSC which holds a valid certificate of registration granted under International Financial Services Centres Authority (Banking) Regulations, 2020 by the International Financial Services Centres Authority²; and

- Such contract is not entered into by the non-resident through or on behalf of its Permanent Establishment (PE) in India.

The Rules defined certain terms as follows:

- PE shall have the meaning assigned under Section 92F(iiiia) which provides that PE includes a fixed place of business through which the business of the enterprise is wholly or partly carried on.
- 'A non-deliverable forward contract' shall mean a contract for the difference between an exchange rate agreed before and the actual spot rate at maturity, with the spot rate being taken as the domestic rate or a market determined rate and such contract being settled with a single payment in a foreign currency.
- 'Offshore banking unit' means a banking branch Unit located in an IFSC, as referred to in Section 80LA(1A).

Our comments

The specification of the aforesaid conditions should make the provisions of section 10(4E) workable and should provide a fillip to development of a NDF market in IFSC.

¹ CBDT Notification No. 136/2021, dated 10 December 2021

² The offshore banking unit shall ensure that this condition is complied with.

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