Taxation and Other Laws (Amendment) Bill, 2026: Analysing Key International Tax Amendments

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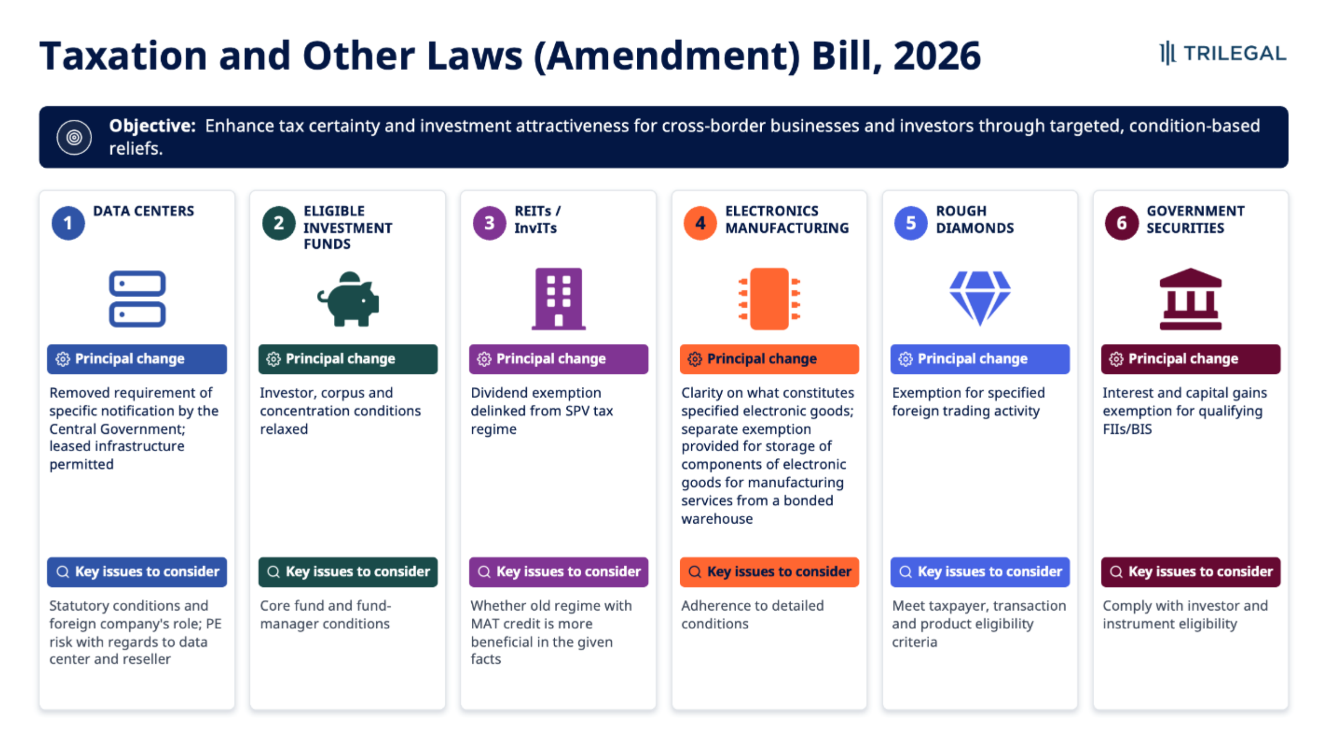
Execution summary

India's ***Taxation and Other Laws (Amendment) Bill, 2026*** proposes amendments for specific cross-border structures for ease of doing business in India. For data centers, the bill seeks to simplify the eligibility to claim the tax exemption by removing the condition for notification of 'specified data centers' and 'foreign company' and to allow the lease model of ownership of specified data centre to be operated by Indian company.

For eligible investment funds, the Bill substantially relaxes the fund level conditions, widening the scope of exemption for the smaller and more concentrated offshore investment vehicles. The Bill also seeks to restore the exemption for qualifying dividend distributions by REITs and InvITs, irrespective of the corporate tax regime adopted by the underlying SPV.

The Bill further introduces a targeted exemption for qualifying rough-diamond trading undertaken through a notified zone, subject to taxpayer-, transaction- and product-level conditions. Separately, qualifying FIIs and the BIS would receive full exemption from tax on specified interest and capital gains arising from Government securities, subject to the relevant eligibility and compliance requirements.

Overall, the amendments are aimed at improving tax certainty and investment attractiveness, but the reliefs remain condition-based and do not displace the need for separate analysis under section 9, applicable DTAAs and transfer pricing rules.



1. Introduction

The Taxation and Other Laws (Amendment) Bill, 2026 (**Bill**) proposes amendments to the income-tax framework aimed at providing greater certainty to cross-border businesses and investors and facilitating investment and business activity in India.

From an international tax perspective, the key amendments address foreign companies procuring data centre services, eligible investment funds and Indian fund managers, Real Estate Investment Trusts (**REITs**) and Infrastructure Investment Trusts (**InvITs**), electronics manufacturing, rough-diamond trading and specified income from Government securities. This update considers the relevant statutory changes, their policy context and the principal implications for taxpayers.

References below are to the Income-tax Act, 2025 (**ITA 2025**), unless otherwise stated.

2. Exemption for Income from Procuring Data Centre Services

Under the existing framework, an exemption is available to a foreign company is provided in respect of income accruing or arising in India, or deemed to accrue or arise in India, from procuring data centre services from a specified data centre under SL No. 13C of Schedule IV of the ITA 2025.

The provision is intended to address potential Indian tax nexus concerns where a foreign company uses data centre infrastructure located in India without owning or operating that infrastructure.

The exemption is subject to conditions intended to maintain a separation between the foreign company and the Indian data centre infrastructure. In particular, the foreign company must not own or operate the physical infrastructure or resources of the data centre; and sales to users in India must be made through an Indian company acting as a 'reseller'.

The existing framework also requires the foreign company to be specifically notified by the Central Government. The definition of a *'specified data centre'* also contains conditions concerning its ownership and operation.

Proposed Amendment

The Bill proposes to remove the requirement of a specific notification in respect of the foreign company and the data centre. It also proposes to permit a specified data centre to be operated by an Indian company where the underlying infrastructure can be owned or leased by that company, subject to prescribed conditions.

What does this mean for taxpayers?

The proposed amendment will benefit foreign cloud, technology and digital businesses procuring capacity from Indian data centre operators. The removal of the notification requirement could reduce the administrative uncertainty associated with accessing the exemption, while permitting leased infrastructure should accommodate a wider range of commercial arrangements.

That said, the contractual allocation of ownership, operation and control should nevertheless be reviewed carefully. The exemption is not a general PE exemption, and the foreign company's activities should continue to be examined separately under section 9 of the ITA 2025 read with the applicable Double Taxation Avoidance Treaty (**DTAA**). Where the foreign enterprise exercises significant control or supervision over the servers or other infrastructure in India or has such infrastructure at its disposal for carrying out core income-generating functions, a fixed place PE could arise under the applicable DTAA. In such circumstances, the exemption itself may cease to be available, resulting in the foreign enterprise being exposed to Indian tax on the relevant income.

Similarly, PE exposure may arise where the Indian reseller by whom services are provided in India acts beyond the scope of a routine seller and habitually concludes contracts, plays the principal role leading to the conclusion of contracts, or otherwise acts as a dependent agent of the foreign enterprise. While such circumstances would not result in the data centre constituting PE, they could result in the Indian reseller constituting a dependent agent PE of the foreign enterprise under the applicable DTAA. This aspect would therefore need to be carefully structured and implemented to ensure that the Indian reseller remains limited-risk reseller.

Further, if the employees of the foreign company are seconded to the Indian reseller, it could create a Service PE of the foreign company in India. Any such secondment arrangement would accordingly need to be carefully designed from both a contractual and functional perspective.

3. Eligible Investment Fund and Indian Fund Manager

The eligible investment fund regime, originally introduced as section 9A of the Income Tax Act 1961, with effect from 1 April 2016, with the intention to make India an attractive jurisdiction to manage global funds without constituting PE. However, owing to the onerous conditions attached to the regime, this objective has not been fully realised.

Under the ITA 2025, the corresponding framework is contained principally in section 9(12) read with Schedule I. The legislative objective was therefore to ensure that an offshore fund would not be regarded as having a business connection in India or becoming resident in India merely because its fund manager is situated in India.

The existing regime imposed extensive conditions intended to demonstrate that the offshore vehicle is a genuine pooled investment fund including requirements concerning minimum number of investors, investor concentration, investment concentration; investment in associates, minimum corpus, investor-protection regulation, and fund-manager remuneration.

Amendment

The Bill without changing the core protection against creation of business connection in India, substantially removes certain fund-level conditions:

Condition	Existing framework	Proposed framework
Minimum investors	25	No minimum
Individual investor concentration	10% restriction	Removed
Concentration among 10 or fewer members	50% restriction	Removed
Investment concentration	25% of corpus	Removed
Investment in associates	Restricted	Removed
Minimum corpus	₹100 crore	Removed
Investor-protection regulation	Required	Removed
Minimum fund-manager remuneration	Prescribed	Removed

<u>What does this mean for taxpayers?</u>

The proposed amendment materially widens the potential pool of funds that can access the safe harbour. In particular, smaller funds, concentrated funds and funds with fewer investors should now also be able to access the benefit. This is particularly relevant for private funds and specialised investment vehicles that would not naturally satisfy the diversification and corpus requirements of the earlier regime.

The relaxation is also significant from a compliance perspective, as the earlier regime required satisfaction of approximately 13 eligibility conditions, whereas the proposed framework retains only a limited number of core conditions (5 to be precise), including those relating to the fund's non-resident status, jurisdiction, Indian participation thresholds and appointment of an eligible fund manager.

The fund must, however, continue to satisfy the core conditions concerning its non-resident status, jurisdiction, Indian participation, eligible fund manager and other prescribed requirements.

4. REITs and InvITs: dividend exemption delinked from SPV tax regime

The REIT and InvIT regime provides a tax framework for investment in real estate and infrastructure through business trust structures. Under the existing framework, however, the tax treatment of certain dividend distributions in the hands of investors were dependent on the corporate tax regime adopted by the underlying Special Purpose Vehicle (**SPV**).

The Bill restores the exemption for eligible dividend distributions by REITs and InvITs irrespective of whether the underlying SPV has opted for the concessional corporate tax regime. At the same time, the surcharge applicable to an SPV opting for the concessional regime is increased from 10% to 25%.

The amendment is limited to the relevant dividend component and does not change the treatment of other distribution components, including interest, rental income, repayment of debt/capital and capital gains.

<u>What does this mean for taxpayers?</u>

The proposed amendment would provide greater certainty to investors as dividend income distributed by a REIT or InvIT will remain tax exempt in the hands of investors, regardless of whether the underlying SPV follows the old tax regime or the new concessional tax regime.

The key structuring consequence is therefore a shift in the location of the tax burden: investors obtain the dividend exemption, while the increased SPV-level surcharge needs to be factored into the economics of the REIT/InvIT structure.

Further, harmonization of the tax treatment of REIT/InvIT distributions also places the new regime on a more favourable footing, particularly when viewed alongside the reduced availability of MAT credit under the old regime, thereby providing an additional incentive for taxpayers to consider transitioning to the new regime.

The character of each distribution should continue to be determined separately; the amendment should not be applied to the entire distribution without identifying its underlying components.

5. Electronics Manufacturing and Bonded Warehouses

The existing regime provides an exemption for income of a foreign company from the manufacture of specified electronic goods through an eligible contract manufacturer in India. The regime is intended to promote India as a manufacturing base while permitting the foreign enterprise to retain its broader commercial relationship and ownership of inputs.

A measure for certainty on taxable income already existed under section 61 to a non-resident providing services or technology in India to set up an electronics manufacturing facility, or in connection with manufacturing or producing electronic goods, articles or things in India to an eligible resident company. In such a scenario, 25% of the relevant gross receipts is deemed to be taxable business profit in India. The foreign company pays tax on that deemed profit at the applicable rate; deductions or losses cannot be set claimed against it. This provision, however, did not provide an exemption for such income.

The Bill extends the exemption from tax year 2030–31 to tax year 2040–41 boosting long term manufacturing arrangements in India. The scope of ‘specified electronic goods’ is also proposed to be expanded to include:

(a) mobile phones; or

(b) laptops, all-in-one personal computers and tablets; or

(c) servers and ultra small form factor (**USFF**); or

(d) sub-assemblies to the finished goods mentioned in clauses (a) to (c); or

(e) hearables and wearables and accessories related to the finished goods mentioned in clauses (a) to (c).

From manufacturing to the supply chain: bonded warehousing exemption. The Bill introduces an exemption for specified income from the storage of components in a customs bonded area for subsequent sale to said eligible contract manufacturer. A *'customs bonded area',* for this purpose, is linked to a warehouse referred to in section 65 of the Customs Act, 1962.

<u>What does this mean for taxpayers?</u>

The amendments facilitate a structure in which a foreign electronics manufacturer:

retains ownership of components → stores them in a qualifying bonded warehouse → supplies them to an Indian contract manufacturer → obtains finished goods manufactured on its behalf.

The principal benefits are:

- greater certainty for long-term manufacturing arrangements through the extension to 2040–41;
- availability of relief for the component storage and supply leg, in addition to the existing manufacturing exemption; and
- expansion of the range of electronic products capable of qualifying.

Contracts should clearly establish the foreign company's ownership of the relevant components and the Indian entity's role as a contract manufacturer acting on behalf of the foreign company for consideration.

The foreign company's broader activities in India should nevertheless be reviewed separately under section 9, the PE provisions of the applicable DTAA and transfer-pricing rules.

Further, it is pertinent to note that the applicable DTAA generally provide a specific PE exemption where goods belonging to an enterprise are maintained in India solely for the purpose of storage, display or delivery, or where goods are maintained solely for the purpose of processing by another enterprise, subject to the conditions of the relevant treaty. The introduction of a corresponding exemption under domestic law provides an additional layer of certainty and reduces the need for taxpayers to rely on and establish treaty eligibility for such activities. This may also reduce the associated treaty compliance and documentation requirements, including the need to furnish and substantiate treaty entitlement, particularly where the income falls squarely within the scope of the domestic statutory exemption.

Separately, the interaction with section 61 would also need to be examined carefully by the taxpayer. Activities that fall within the Schedule IV exemption may be removed from the presumptive taxation framework to the extent specifically covered by the exemption. Conversely, activities falling outside the exemption may continue to be relevant for section 61, where its conditions are satisfied.

6. Rough-Diamond Trading

India is one of the largest centres for diamond polishing and, according to IBEF reports, processes over 90% of the world's cut and polished diamonds. With a view to facilitate international trading in rough diamonds through India, the Bill introduces a new provision proposing a targeted exemption for specified income arising from the sale of rough diamonds, with effect from 1 October 2026.

The exemption applies to a foreign company that is engaged in diamond mining a sightholder of a diamond mining company, ora broker, aggregator or a tender and auction entity connected with the sale of rough diamonds.

Further, the exemption is subject to, among other things,

- the sale being carried out in the notified special zone referred to in section 9(9)(c)(ii)(C) of the ITA 2025;
- prescribed information must be maintained and furnished, and
- the exemption is available up to the tax year ending 31 March 2041.

A *'rough diamond'* for this purpose is limited to a diamond which is unworked or simply sawn, cleaved or bruted, covered by the specified Customs Tariff Headings, including 7102 10, 7102 21 and 7102 31, and accompanied by a Kimberley Process Certificate.

What does this mean for taxpayers?

The exemption would benefit foreign mining companies, sightholders and qualifying international diamond-trading intermediaries undertaking rough-diamond transactions through the notified zone. Eligibility should be verified at the taxpayer, transaction and product level, particularly with respect to the taxpayer's status, location of the sale, tariff classification and Kimberley Process certification and should not be treated as a general exemption for all diamond trading activities in India.

7. Government Securities: broadening the tax exemption for foreign investors

The Bill makes the India's sovereign debt market more attractive to foreign investors by providing specific exemption for certain income earned by Foreign Institutional Investor (**FII**) and Bank for International Settlements **(BIS)**. The Government securities exemption was introduced through the Income-tax (Amendment) Ordinance, 2026, promulgated on 5 June 2026, and is proposed to be incorporated into the Bill.

Under the framework, Sl. No. 13D of Schedule IV provides an exemption toa qualifying FII from tax on interest on a government security and capital gains arising from the sale, exchange or transfer of such Government security.

The exemption, however, is not available to every foreign investor. The term *'Foreign Institutional Investor'* is linked to section 210(6)(a) of the ITA 2025 and is therefore a notification-based category. The exemption is subject to the prescribed information-furnishing requirement.

A corresponding exemption is proposed under Sl. No. 13E to the BIS. thereby extending tax exemption to interest and capital gains arising from its investment in Government securities.

An important point in determining the scope of the exemption is the nature of the underlying instrument. *'Government security'* takes its meaning from section 2(f) of the Government Securities Act, 2006. Accordingly, eligibility depends on the instrument satisfying the statutory definition and not merely on its commercial description.

What does this mean for taxpayers?

For qualifying FIIs and the BIS, the amendment provides a full exemption for the specified interest and capital gains rather than merely a reduced withholding rate.

The principal diligence points are therefore:

- whether the investor falls within the notified FII category or is the BIS;
- whether the relevant instrument qualifies as a government security;
- whether the income falls within Sl. No. 13D or 13E; and
- whether the prescribed information has been furnished.

8. Conclusion

The amendments are largely targeted at high-growth and globally mobile sectors, including electronics manufacturing, data centres, investment fund management, REITs/InvITs, diamond trading, and foreign portfolio investment, reflecting the Government's focus on attracting capital, technology, and international business activity to India.

Collectively, these measures reinforce India's commitment to creating a more predictable and investor-friendly tax environment for cross-border investment and business activities. Although the benefits are condition-based, taxpayers who appropriately structure and document their arrangements can meaningfully benefit from the available exemptions and safe harbour provisions.

The above amendments are positive and will be welcome by industry participants whether it be manufacturing, data/technology or the funds ecosystem.