4 August 2026

EY Tax Alert

on Taxation and Other Laws (Amendment) Bill, 2026

Tax Alerts cover significant tax news, developments and changes in legislation that affect Indian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor.

Background

On 5 June 2026, the Government of India (GOI) announced a series of reforms aimed at deepening the Government Securities (G-Secs) market and enhancing Foreign Portfolio Investor (FPI) participation. These reforms were announced in reaction to evolving geopolitical developments and related disruptions in international trade and supply chains.

As Parliament was not in session and circumstances existed which rendered it necessary to take immediate action, the President, in exercise of the powers conferred by clause (1) of article 123 of the Constitution, promulgated the Income-tax (Amendment) Ordinance, 2026 (Ordinance) on the 5 June 2026.

Accordingly, the Government has introduced the Taxation and Other Laws (Amendment) Bill, 2026 (Amendment Bill) in the Lok Sabha on 4 August 2026 to ratify the Ordinance.

In addition to ratification of Ordinance, the Amendment Bill introduces further amendments to the Income Tax Act, 2025 (ITA 2025) and the Finance Act, 2026 in the light of representations received from stakeholders after the enactment of Finance Act 2026 to comprehensively achieve the object of mitigating impact of external economic shocks, ensuring stability in the domestic economy and supporting key sectors affected by the prevailing global conditions.

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This Alert covers key direct tax proposals contained in the Amendment Bill. The executive summary of the proposals is as below:

- Streamlining taxation of dividend distributions by business trusts by granting a uniform exemption to unitholders regardless of the tax regime adopted by the underlying Special Purpose Vehicle (SPV), but with higher surcharge (SC) of 25% for SPVs opting for concessional regime.
- Exemption for foreign companies providing capital goods, equipment or tooling for specified electronics contract manufacturing extended till tax year 2040-41.
- Tax exemption proposed till tax year 2040-41 for foreign company storing components in bonded warehouse in India for supply to contract manufacturer manufacturing specified electronic goods.
- Relaxation of conditions for exemption available to foreign companies procuring data center services from India.
- Tax exemption proposed for foreign companies engaged in sale of rough diamonds in notified special zones.
- Significant rationalization of the safe harbor framework promoting management of offshore funds from India by deletion of eight conditions to be satisfied by the offshore fund
- Tax exemption for interest income and capital gains earned by Foreign Institutional Investors (FIIs) and the Bank for International Settlements (BIS) from investments in Government Securities introduced by the Ordinance now ratified.

Detailed discussion on the direct tax proposals of the Amendment Bill

- ► **Proposed amendment relating to dividend distribution by business trusts**

  Existing tax framework:

  - Under the existing provisions of the ITA 2025, dividend income received by a business trust (i.e., an Infrastructure Investment Trust (InvIT) or a Real Estate Investment Trust (REIT)) from its investment in a SPV is exempt from tax at the level of the business trust.

  - Further, the ITA 2025 provides for a pass-through mechanism whereby the character of income distributed by the business trust to its unitholders generally retains its original nature. Accordingly, where dividend income received by a business trust from an SPV is distributed to its unitholders, such income continues to be regarded as dividend income in the hands of the unitholders.

  - The tax treatment of such dividend income in the hands of unitholders is presently dependent upon the tax regime opted for by the underlying SPV, as summarized below:

    - **SPV not opting for the concessional corporate tax regime (CTR):** Dividend income distributed by the business trust to its unitholders is exempt from tax.

    - **New manufacturing SPV opting for special CTR:** Dividend income distributed by the business trust to its unitholders remains exempt from tax where SPV has opted special CTR of 17.16%.

    - **Other SPV opting for CTR:** Dividend income distributed by the business trust to its unitholders is fully taxable where SPV has opted CTR of 25.17%.

Proposed amendments:

The Amendment Bill proposes rationalization of the tax framework applicable to dividend distributions through business trusts and corresponding changes to the surcharge provisions applicable to SPVs opting for CTR in the following manner:

- **Exemption for dividend income distributed by business trusts:**

  The Amendment Bill proposes that dividend income distributed by a business trust to its unitholders shall be exempt from tax, irrespective of whether the underlying SPV has or has not opted for CTR.

- **Applicability of higher surcharge rate in the hands of SPVs opted for CTR:**

  The Amendment Bill further proposes enhancement in the surcharge rate for SPVs that have opted for CTR. Under the proposed amendments:

  - SPVs availing CTR of 25.17% will be subject to a surcharge at a flat rate of **25%** instead of currently applicable 10%, which will result in enhancement of effective tax rate to 28.6%.

  - New manufacturing SPVs availing special CTR of 17.16% will likewise be subject to a surcharge at a flat rate of 25% instead of currently applicable 10%, which will result in enhancement of effective tax rate to 19.5%.

- SPVs not opting for CTR will continue to be governed by the existing surcharge framework of 7% or 12% depending upon level of taxable income. Accordingly, their effective tax rate will continue to be 33.38%/34.94%.

- The tabular summary of the amendment is as under:

Sr. no.	SPV of business trust	Taxability	Pre-amendment	Post-amendment
1.	Opted for CTR regime under section 200 of ITA 2025[1]	Tax rate (in hands of SPV)	25.17% (incl. SC of 10%)	28.6% (incl. SC of 25%)
		Dividend (in hands of unitholders)	Not exempt	Exempt
2.	Opted for CTR regime under section 201 of ITA 2025[2]	Tax rate (in hands of SPV)	17.16% (incl. SC of 10%)	19.5% (incl. SC of 25%)
		Dividend (in hands of unitholders)	Exempt	Exempt
3.	Not opted for CTR regime	Tax rate (in hands of SPV)[3]	34.94% (incl. SC of 12%)	34.94% (No change)
		Dividend (in hands of unitholders)	Exempt	Exempt

- Furthermore, in view of dividend exemption under domestic law, treaty relief will become academic precluding any controversy on treaty eligibility and treaty characterization of such dividend income.

- FAQs released by CBDT[4] explaining the above amendments clarify that the rationalization of dividend taxation from business trust is introduced in the light of amendments by Finance Act 2026, making Minimum Alternative Tax (MAT) payable for tax year 2026-27 onwards a final non-creditable tax and allowing unutilized MAT credit till 31 March 2026 to be set off against regular tax only if the domestic company opts for CTR from tax year 2026-27 onwards. Therefore, SPV of business trust may also have to move to CTR, leading to unitholders losing exemption on dividend income.

Extension and rationalization of exemption for foreign companies supporting electronics manufacturing in India

- Presently, foreign companies are exempt from tax on income arising from providing capital goods, equipment or tooling (capital goods) to Indian contract manufacturer. The exemption applies when the contract manufacturer is an Indian resident company located in a customs bonded area producing electronic goods for the foreign company. The ownership of capital goods should remain with the foreign company. The exemption is available up to tax year 2030-31.

- The Amendment Bill proposes to restrict exemption only to specified electronics goods but the exemption is extended by ten years up to tax year 2040-41.

- The specified electronic products eligible for the exemption are as below:
  (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, hearables and wearables, including accessories related to the finished goods mentioned in clauses (a) to (c)

- The above amendments will be effective from 1 April 2026 (tax year 2026-27 onwards).

- Further, the Amendment Bill also proposes to insert a separate clause for exempting income of a foreign company up to tax year ending on 31 March 2041 on storage of components in a customs bonded area in India, if the components are sold to an Indian contract manufacturer of above specified electronic products, who manufactures on behalf of any foreign company in a custom bonded area. Further, the foreign company will also be required to submit the requisite information in prescribed form and manner to claim such exemption. This amendment is effective from 1 October 2026.

Relaxation of conditions for tax exemption relating to data center services

- Presently, exemption is available to foreign companies upto tax year 2046-47 on income arising from procuring data center services from a specified data center in India. To qualify for the exemption, all sales by such foreign company to users located in India must be made through a reseller Indian company and the foreign company should not own or operate any of the physical infrastructure or any resources of the specified data center. Further, the foreign company is required to be notified by the Central Government and the specified data center must be set up under an approved scheme notified

[1] S.115BAA of erstwhile Income tax Act 1961 (ITA 1961)
[2] S.115BAB of erstwhile ITA 1961
[3] Excluding small companies having turnover of less than INR 4000 million.
[4] Central Board of Direct Taxes – Apex Direct Tax Administrative Body in India

by MeitY[5] and must be owned and operated by an Indian company.

- In order to promote ease of doing business, the Amendment Bill proposes to relax some of the above conditions by removing the requirement for notification of the foreign company and of the Indian specified data center. Further, the Indian data center can either be owned or leased by the Indian entity thus permitting a lease model of operating data center. Such data center will also have to satisfy such other conditions as may be prescribed.

- This amendment will be effective from 1 April 2026 (tax year 2026-27 onwards).

Tax exemption proposed for foreign companies engaged in sale of rough diamonds in notified special zones

- The Amendment Bill proposes to provide exemption on sale of rough diamonds upto tax year ending 31 March 2041 to a foreign company which is either engaged in the business of diamond mining or is functioning as a sightholder of such company. Further, any income of foreign company being a broker, aggregator or a tender and auction entity connected with sale of rough diamonds will also be exempt.

- The exemption will apply to sales undertaken in notified special zones, subject to prescribed reporting requirements.

- This amendment will be effective from 1 October 2026.

Rationalization of offshore fund management safe harbors

- Currently, an eligible investment fund seeking to be managed from India is required to satisfy 13 conditions in order to avail a safe harbor so as to not constitute a business connection for the offshore fund in India.

- The Amendment Bill proposes to rationalize the framework by retaining only 5 conditions required to be satisfied by the eligible investment fund as under:

Conditions retained	Conditions deleted
Residency: The fund is not a person resident in India.	**Investor protection regulations:** The fund and its activities should be subject to investor protection regulations in its home jurisdiction.
Access to information exchange: The fund should be resident in a treaty jurisdiction or such other jurisdiction as may be notified (almost all countries are included)	**Investor diversification requirements:** • Minimum requirement of 25 investors who are not connected persons. • No investor, together with connected persons, may hold more than 10% participation interest in the fund • Aggregate participation of 10 or fewer investors (along with connected persons) remain below 50% of the fund
Participation of Indian residents: Aggregate direct participation by Indian residents should not exceed 5% of the corpus of the fund.	**Concentration limits:** Restriction on investing more than 25% of the corpus in a single entity.
Control and management of portfolio companies: The fund should not carry on or control and manage, directly or indirectly, any business in India (holding more than 26% of the total share capital or voting power would be considered to be controlling from the business in India)	**Investment in associates:** Restriction on investments in entities where a director or fund manager of the investment fund or a director or member of the fund manager of the fund owns more than 15% of share capital or interest.
Business connection: No person acting on behalf of the fund should undertake activities constituting a business connection in India, other than activities undertaken through an eligible fund manager.	**Minimum corpus:** Requirement to maintain a corpus of INR 100 crore.

[5] Ministry of Electronics and Information Technology

	Remuneration threshold: Meeting with the prescribed minimum level of remuneration.

- **Power of CBDT to issue notifications in case of fund managers based in IFSC taken away**
  - Currently, the CBDT is empowered to relax any condition in relation to the grant of safe harbor to an offshore fund, where it is proposed to be managed by an eligible fund manager located in an International Financial Services center (IFSC) and has commenced such activity before 31 March 2030, by way of a notification.
  - The Amendment Bill proposes to withdraw this power granted to the CBDT.

- **Tax exemption for FIIs and BIS in respect of Government Securities**
  - Currently, as per the Ordinance[6], with effect from 1 April 2026, any interest income from G-Secs and any capital gains arising from transfer thereof earned by FPIs and Banks for International Settlements (BIS) shall be exempt from tax, subject to furnishing of prescribed information (the same are pending to be notified).
  - The Amendment Bill proposes to legislatively ratify the amendments of the Ordinance.

Comments

The proposed amendments significantly simplify the tax regime governing dividend distributions through business trusts by providing a uniform exemption to unitholders in respect of dividend income distributed by a business trust, irrespective of the tax regime adopted by the underlying SPV but with higher surcharge for SPVs opting for CTR as a revenue balancing exercise.

Various relaxations and exemptions proposed for foreign companies for procuring data center services from India or contract manufacture of specified electronic goods in India or sale of rough diamonds in India are a welcome move providing better tax certainty, enhancing ease of doing business in India and attracting more investment in sunrise sectors of the economy.

While the amendments related to the ratification of the exemption on interest and capital gains earned on G-secs by FPIs were expected, the proposed amendments in relation to safe harbor regime for onshore management significantly enhance its commercial viability and align India's framework more closely with internationally prevalent practices.

The removal of investor diversification requirements, concentration limits, corpus thresholds and investment restrictions is expected to make the regime accessible to a much wider universe of offshore funds, including hedge funds, sovereign wealth funds, pension funds, family offices and separately managed account (SMA) structures providing new opportunities for asset managers based in India to move up the value chain as well as boost ancillary services. Furthermore, the revamped safe harbors apply neutrally regardless of offshore fund being managed from IFSC or mainland providing better flexibility for funds and their managers (including managing offshore funds not investing in India).

The rationale for removing the minimum remuneration threshold while retaining the cap of 20% of profits to be paid to the fund manager, though, is a bit surprising. A notification issued under the erstwhile ITA 1961 in relation to offshore funds managed from IFSC clarified that the monitoring mechanism to protect the investment in portfolio company, including the right to appoint directors would not be considered as participation in day-to-day operations of such person in India. Consequent to the removal of CBDT's powers to relax conditions for offshore fund managed from IFSC, it would be desirable that such clarification is reiterated in the context of revamped safe harbor conditions under the ITA 2025.

[6] Refer EY Alert 8 June 2026 for details of the Ordinance 2026

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