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Aircraft leasing in India: Ready to take off



pwc

Table of contents

Preface	04
Overview of global aircraft leasing market	06
India: Journey so far and success factors for lessors	10
Aircraft regulations in the IFSC	16
Tax framework of aircraft leasing companies in the IFSC	18
Way forward	26
Glossary	27



Preface

The aviation industry has shown robust growth in a dynamic environment, demonstrating its underlying strength and the value of air travel. Passenger traffic has recorded above-trend growth for the ninth straight year, with historically high aircraft utilisation rates.[1] As global economies return to normalcy after the COVID-19 pandemic, the aviation industry too is slowly resuming its upward trajectory.

In recent years, India has emerged as a major player in the global aviation industry, supported by relaxed regulatory frameworks, and the Indian aviation industry has seen unprecedented double-digit growth in the past few years.[2]

In order to make India an aviation hub and develop the aircraft leasing and financing business in India, a Working Group on Developing Avenues for Aircraft Financing and Leasing Activities in India was constituted by the Ministry of Civil Aviation in May 2018. The Working Group had identified the International Financial Services Centre (IFSC) in Gujarat International Finance Tec-City (GIFT City) as the location to onshore the offshore aviation leasing business in India.

The Union Finance Minister, in her Budget speech in 2019, had also recognised the potential of aircraft financing and leasing activities from Indian shores to develop a self-reliant aviation industry and create aspirational jobs in aviation finance.

To develop and promote the aviation leasing business in the IFSC, several changes have been proposed to the tax framework in Union Budget 2021–22. The International Financial Services Centres Authority (IFSCA) has also issued a framework for aircraft leasing in the IFSC.

Given the above favourable measures, we believe that the stage has now been set for the aircraft leasing business to take off in the country.



1 Current Aircraft Finance Market Outlook 2019 report

2 48 months of transforming aviation in India (2014-2018)





Overview of global aircraft leasing market

Market situation

The airline industry has witnessed positive growth in the past decade supported by growing economies, the rising middle class and increasing aspirations of the young generation. The growth in passenger air travel has averaged 6.5% annually in the past decade compared to the long-term average of 5%.[3] It led to global airline companies growing their fleet through new deliveries and pushing replacements to accommodate demand. This resulted in an annual growth of 3.2% in the global commercial fleet over the past decade.[4]

However, in 2020, aviation was one of the most impacted sectors by the COVID-19 outbreak. The industry-wide revenue passenger kilometres (RPKs) plunged 66% compared to 2019 – the most severe decline in aviation history. However, easing of restrictions led to recovery of domestic travel and RPK contraction reduced to half by December 2020. The emergence of effective vaccines and better treatment methods would assist the recovery going ahead; nevertheless, it is estimated that the industry will take 3–4 years to get back to 2019 figures.[5] In the long term, however, the future of aviation remains healthy.

3 Boeing Commercial Market Outlook 2020-2039

4 Oliver Wyman Global Fleet and MRO Forecast 2020-2030

5 IATA Air Passenger Market Analysis, June 2020

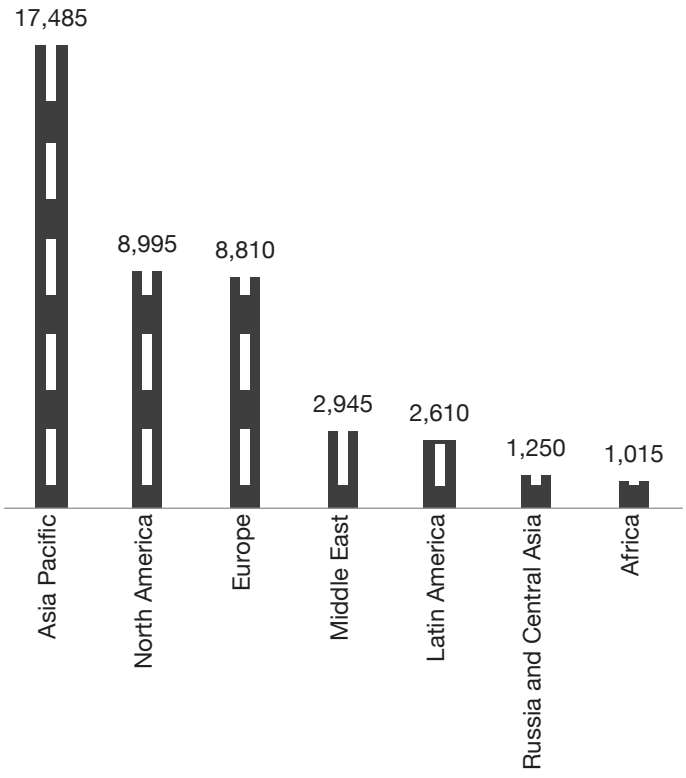
Historically, airlines have used downturns to retire aged fleet. Retirement rates average around 2–3% for normal years, while they went up to 4–5% during the global financial crisis and post 9/11.[6] Airline companies may again use this downturn to replace their current fleets with fuel-efficient aircraft to aid their profitability and sustainability.

Future growth estimates

Delivery of 43,110 new airplanes is expected to airlines globally in the period 2020–2039, leading to expansion of the global fleet of 25,900 aircrafts in 2019 to 48,400. The highest share of deliveries would be to the Asia Pacific, with China accounting for 50% of the regional total.[4]

The air cargo market is forecasted to grow at 4% annually, with the freighter fleet expanding by nearly 60% from the current level of 2,010 aircrafts to 3,260 by 2039. This growth will drive the need for 2,430 new and converted freighters.[4]

Figure 1: Commercial aircraft delivery by region, 2020–39



Gradually returning to 2019 levels following a COVID-induced blip, the aviation industry is on the brink of a new growth period, with economic recovery, increased confidence in travel due to availability of vaccines and continuing low interest rates.

Global aircraft leasing industry

The size of the global aircraft leasing industry was estimated to be USD 290.07 billion in 2019.[7] From owning just 25% of the total commercial fleet in 2000, aircraft lessors have grown to owning about 48.9% of the total fleet in 2020.[8] More than 60% of these aircraft are owned or managed out of Ireland. The benefits of leasing in terms of freed-up capital, operational flexibility and improved cashflow are the reasons for its popularity among airlines. Sustained low interest rates and government interventions have also helped in making aircraft operating leases an attractive investment class and led to the entry of new players in the market in the last decade, notably from Hong Kong and China.

Top 10 aircraft leasing companies, June 2020[9]

Rank	Company	Portfolio size	Portfolio value (USD million)
1	GE Capital Aviation Services (GECAS)	1,203	20,215
2	AerCap	1,046	28,587
3	Avolon	542	17,343
4	BBAM	524	19,447
5	Nordic Aviation Capital	486	4,821
6	SMBC Aviation Capital	437	16,201
7	Air Lease Corporation	383	16,214
8	ICBC Leasing	350	12,247
8	DAE Capital	350	9,082
10	BOC Aviation	334	13,183

6 Boeing Commercial Market Outlook 2020-2039

7 Aircraft Leasing Market Share, Size, Trends, & Industry Analysis Report by Polaris Market Research

8 Ascend by Cirium

9 Lessors and Airfinance Journal's Fleet Tracker as of 30 June, 2020

Ireland's pre-eminence in aircraft leasing

Ireland has been the leader in global aircraft leasing. A favourable tax regime, double tax avoidance treaties and a stable business environment have led to global majors like GECAS, AerCap, Avolon and BBAM setting up headquarters in Ireland. The reasons for Ireland's success are elaborated on below:

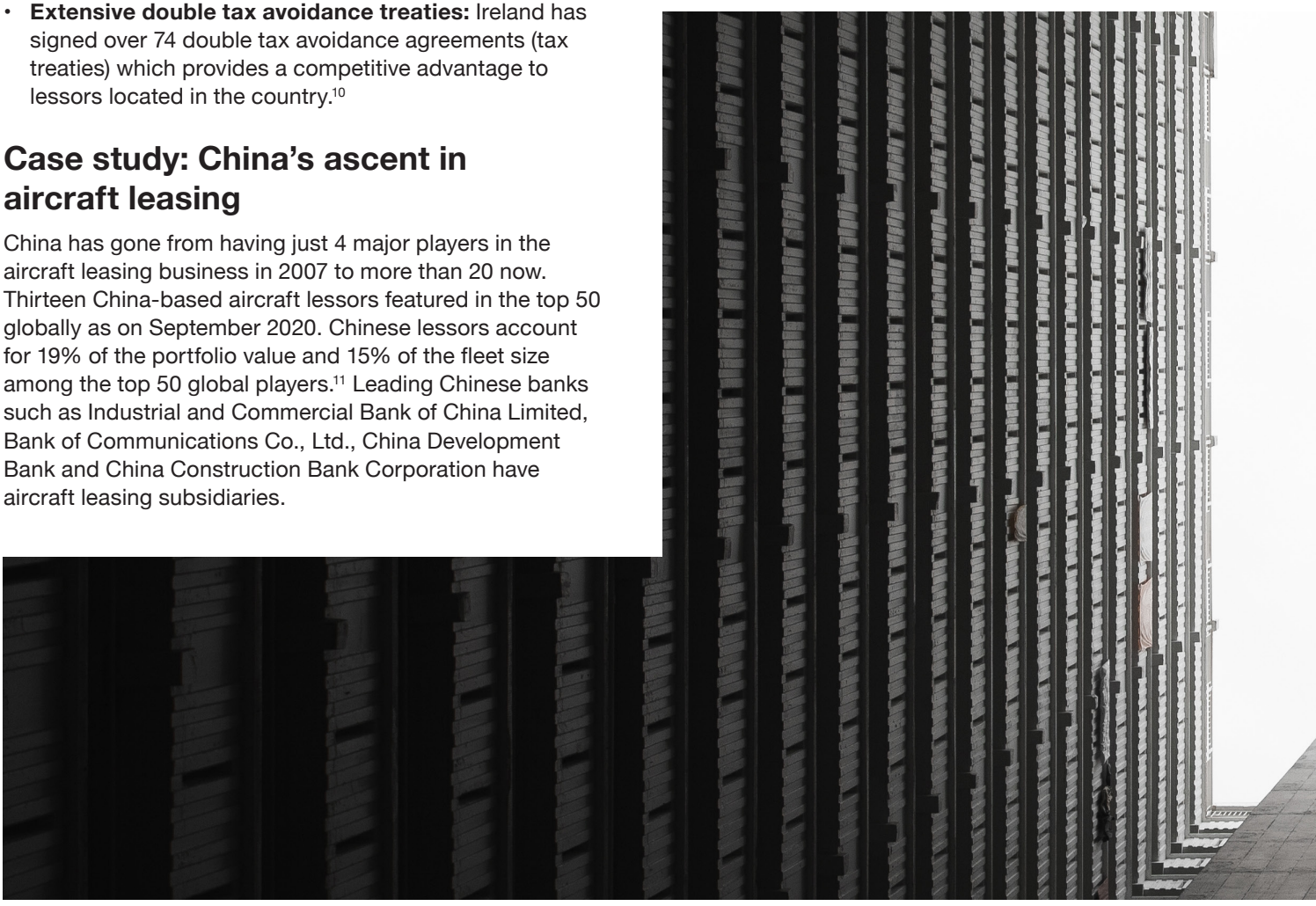
- **Low taxation:** Ireland has an extremely low tax rate of 12.5% on trading profits, which is one of the lowest in Europe. This tax rate has stayed the same for the past 20 years without political opposition, providing a stable business environment. It also provides stamp duty exemption on transfer of aircraft.
- **Favourable accounting rules:** Ireland allows companies to carry forward unused tax losses indefinitely. It also allows straight line depreciation over eight years for aircraft purchased by lessors. These factors allow for a sizeable tax deferral for companies located in Ireland.
- **Extensive double tax avoidance treaties:** Ireland has signed over 74 double tax avoidance agreements (tax treaties) which provides a competitive advantage to lessors located in the country.[10]

Case study: China's ascent in aircraft leasing

China has gone from having just 4 major players in the aircraft leasing business in 2007 to more than 20 now. Thirteen China-based aircraft lessors featured in the top 50 globally as on September 2020. Chinese lessors account for 19% of the portfolio value and 15% of the fleet size among the top 50 global players.[11] Leading Chinese banks such as Industrial and Commercial Bank of China Limited, Bank of Communications Co., Ltd., China Development Bank and China Construction Bank Corporation have aircraft leasing subsidiaries.

The factors behind the growth of the leasing business in China are listed below:

- **Policy changes:** For the first time in 2007, China allowed banks to enter the leasing business, and later, reduced the entry threshold of financial leasing companies.
- **Leveraging Hong Kong:** China leveraged Hong Kong's position as an international financial, trading and transformational centre.
- **Low cost of capital:** China has a very low cost of capital, thus providing a strong financial background for the leasing business to prosper.
- **Low corporate taxes:** Hong Kong has a tax rate of only 8.25% for aircraft lessors, whereas China has a corporate tax rate of 25%.
- **Local needs:** China is expected to receive 8,600 aircraft in the next 20 years,[12] supporting the future growth of the industry.



10 Ascend by Cirium (data supplied end December 2019)

11 Cirium, Bloomberg

12 Boeing Commercial Market Outlook 2020-2039





India: Journey so far and success factors for lessors

Aviation in India

Market snapshot

The Indian aviation market has grown at an annual rate of 10.2% from 2008–09 to 2018–19. Domestic travel has outpaced international travel, with the two growing at 13.5% and 8.2% respectively in the same period.[13] For Indian airliners, the number of weekly flights has increased by 400% from 2008 to 2018.

Low-cost carriers (LCCs) dominate the Indian market, accounting for 65% of all domestic seats and 52% of total capacity (including international travel) in 2018. Indian LCCs have grown at an annual rate of 21% in terms of number of flights flown between 2008 and 2018. The number of airports served by LCCs during the period increased from 28 to 46.[14] Increased service levels and improved efficiencies have resulted in a 70% fall in domestic airfares between 2005 and 2018 (after adjusting for inflation).[15]

13 DGCA

14 Boeing Commercial Market Outlook 2019-2038

15 India's air transport sector, IATA, DGCA

Figure 2: Total air passenger traffic in India – annual passenger journeys (millions)[13]

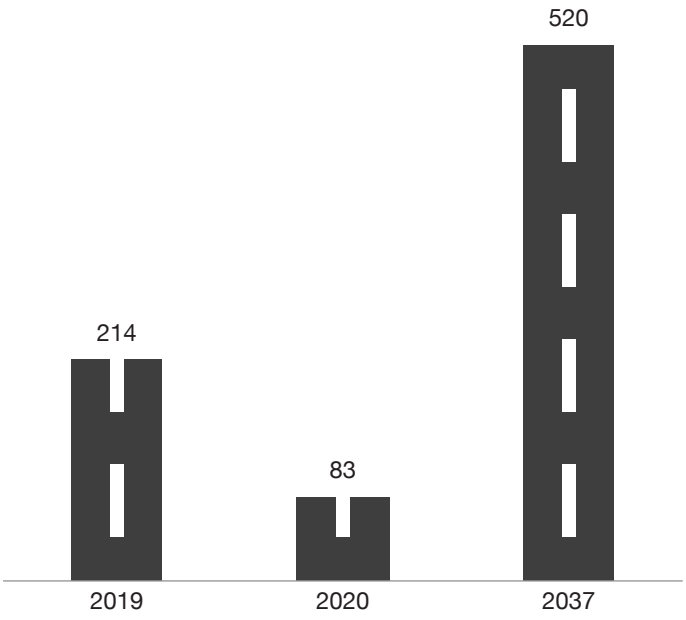
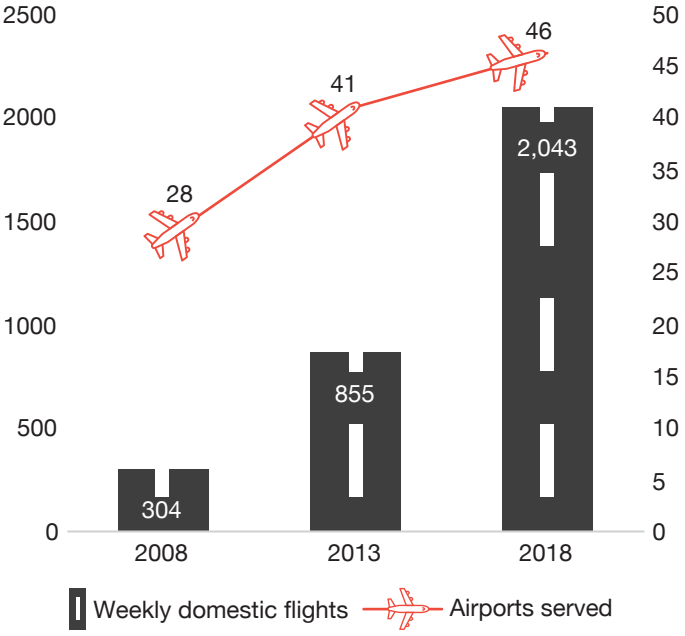


Figure 3: Flights and airports served by Indian LCCs



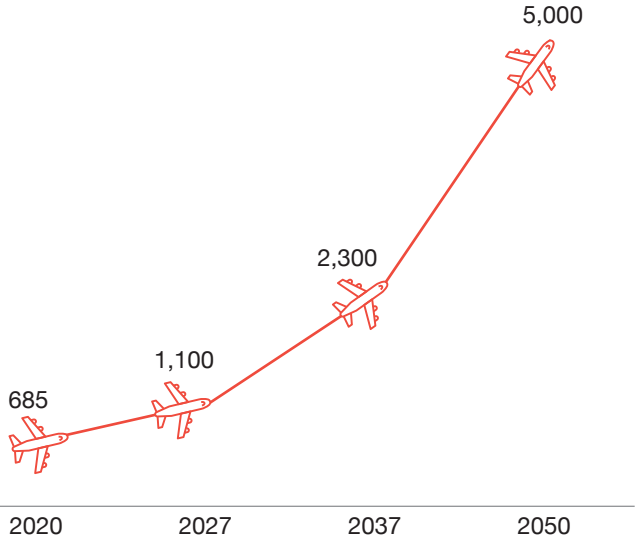
COVID-induced lockdowns affected the Indian aviation sector badly in 2020, with total passenger traffic plummeting to less than 40% of 2019 levels. However, by December 2020, domestic traffic had improved to 56% of 2019 levels.[16] However, international travel was still at 20% level of the previous year in December 2020 and is expected to improve gradually with widespread vaccination coverage. Cargo services were quick to recover and stood at 90% of the last year in December 2020 in terms of volume[17]. Airlines in India have been allowed to run at 80% of the pre-COVID capacity from December 2020 onwards, which will further aid the recovery of the sector. The effect of the pandemic, though significant, is expected to ease in the short term.

Growth projections

By 2038, domestic air traffic in India is expected to grow to 4.8 times that of 2018 levels – the fastest for any sector in the world, with India set to become the third largest aviation market by the mid-2020s.[18]

India's commercial fleet is forecasted to expand to 1,100 by 2027, almost doubling from present levels on the back of rising demand from LCCs.[19] The fleet size in 2037 is likely to stand at 2,300 aircraft, with single-aisle airplanes leading the demand and accounting for almost 85% of new deliveries.[20] By 2050, India's commercial fleet size is likely to exceed 5,000 aircraft.[21]

Figure 4: Indian commercial fleet size forecast



16 *https://dgca.gov.in/digigov-portal/?page=259/4184/servicename*

17 *https://www.aai.aero/en/business-opportunities/aai-traffic-news*

18 *Airbus Global Market Forecast 2019-2038, IATA*

19 *Avolon – An in-depth analysis of the Indian air travel market, July 2018*

20 *Boeing. It is assumed that current aircraft would be retired, and new deliveries would make up the fleet by 2037.*

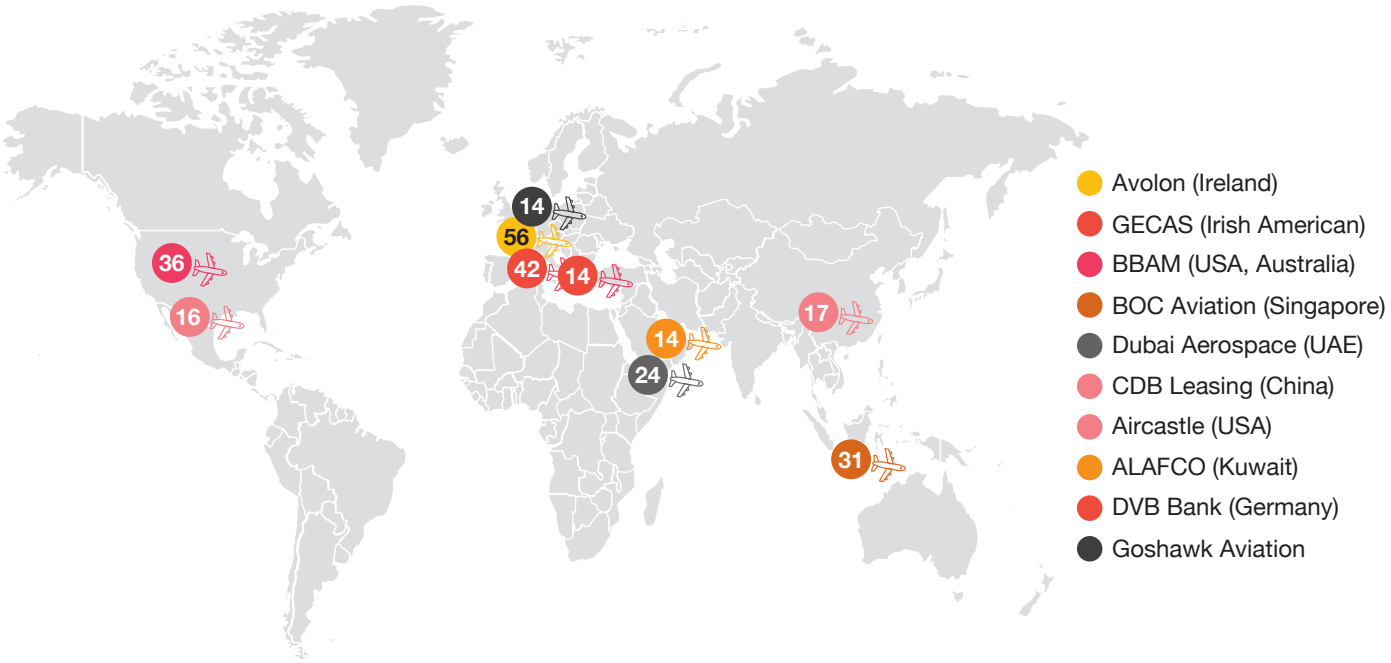
21 *Prospects for an Indian aircraft leasing sector, CAPA, September 2018*

Aircraft leasing in India

Leasing – an attractive choice

Around 80% of the total commercial fleet in India is leased compared with 53% globally. As of 2018, Avolon was the largest lessor to Indian airlines, with GE Capital Aviation Services and BBAM at the second and third position respectively.[18]

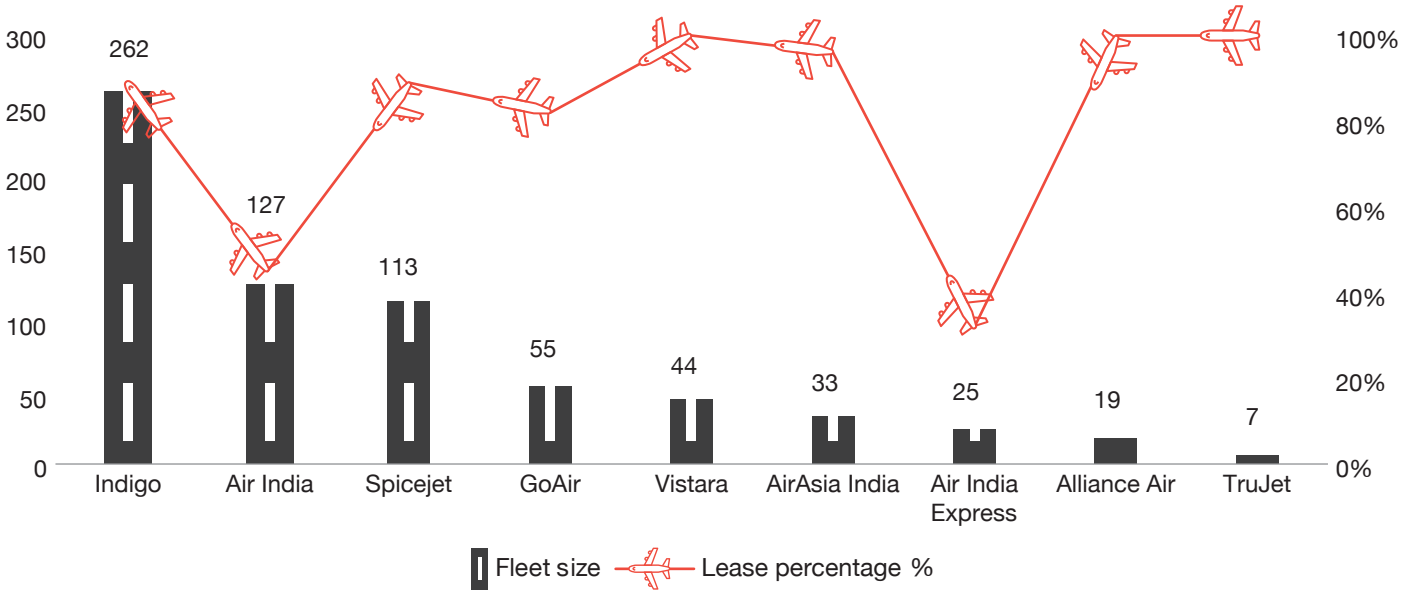
Figure 5: Top 10 aircraft lessors to India, 2018[18]



India sees a high number of leased aircrafts compared to the rest of the world due to the following factors:

- **Financial fragility:** Indian airlines are relatively new and a majority of them have not reported consistent profits in the last five fiscals. Moreover, given the liquidity constraints in Indian markets on raising vast sums of money for aircraft purchases, airlines prefer aircraft leasing for improved cashflow.
- **Operational advantage:** Leasing aircraft provides airlines the option to quickly increase and decrease capacity. As airlines keep inducting new aircraft, owing to the shorter fleet replacement cycles, they benefit from lower maintenance costs, better fuel efficiencies and access to other new technologies.
- **Price sensitivity of customers:** With most of the market being served by LCCs, price is a major differentiator in India. Airlines, therefore, prefer to use available capital to give a price advantage to customers.
- **Easy financing environment with leasing:** Leasing is driven by liquid credit markets, low interest rates, high competition and high demand. All of these together make for an attractive financing situation where banks, lessors and manufacturers compete together, and airlines get good financing offers.

Figure 6: Total fleet and lease percentage for airlines in India[22]



Aircraft leasing companies: Potential benefits to the economy

Currently, there are no aircraft leasing companies in India, which forces domestic airlines to look for lessors abroad. The presence of local lessors would not only help airlines in terms of creating greater opportunities for better leasing terms and conditions, but also help them navigate currency depreciation risks better, thus removing uncertainties from their operational framework. In addition, the airline leasing industry would benefit the country in six ways (Figure 7).

Figure 7: Benefits of aircraft leasing companies to the business ecosystem

Airport and aviation development

The forex risk exposure of Indian airlines whose revenues are in rupees will decrease – potentially boosting the airline industry in India and, consequently, the airport and supporting industries.

Increased GDP

A domestic leasing industry will also boost GDP – aircraft leasing contributes around USD 660 million to the Irish economy.

Boost to MRO industry

Lessors typically have conditions in the contract mandating MRO checks in their preferred locations, mostly outside India. Indian lessors will lead to a level playing field.

Retain international financing services

Financial leasing will retain international financial services and general business for banks/NBFCs/credit guarantors, insurance firms, etc.

Employment generation

The establishment of a leasing market in India will generate high-end employment opportunities, both at leasing companies and supporting industries like accounting, legal, tax, and consulting.

Additional tax revenues

Finally, it will result in additional tax revenues for India, through both the aircraft leasing industry and ancillary industries.

22 *Company websites, annual reports, analyst reports, CAPA, Planespotters, Flightglobal, news articles (https://www.flightglobal.com/airlines/grounded-spicejets-monthly-lease-bill-may-exceed-20m/137723.article?adredir=1). Lease percentages for GoAir, Vistara, AirAsia India and TruJet are as per a CAPA report released in 2018.*



Key success factors for aircraft lessors

Aircraft leasing is a highly complex business and cross-functional expertise is needed to navigate the business environment. Predicting the market demand and supply scenario, understanding the preferences of airlines around the globe, having a low cost of capital and maintaining efficient operations through optimal portfolio management remain key to the success of lessors. Lessors need to adopt an eight-pronged approach for winning in the market (Figure 8).

Figure 8: Aircraft leasing companies – key success factors





Securing low aircraft prices:

The aircraft leasing market is intensely competitive. Low cost of funds and entry of new players from China and Korea have only increased the competitive intensity in the market. Additionally, lessors have to compete with manufacturers in providing better terms to airlines. Thus, it becomes critical to acquire aircraft at competitive prices.



Maximising returns on aircraft trading and disposal:

Aircraft lease periods are shorter than aircraft lifespan, and thus, aircrafts change hands during their useful life. Additionally, aircraft can be sold to lessees or converted to freighters during their life. Maximising returns on each of these events remains key to success in the industry.



Asset selection and portfolio fleet management:

Lessors have to identify the needs of their customers over a long-term horizon and have suitable aircraft (e.g. narrow body vs wide body) as part of their portfolio. Failing to recognise the preferred aircraft of airliners poses a risk to the sustainability of lessors.



Asset management:

Maintaining aircraft across their useful life is expensive and it necessitates orderly and efficient management of the fleet to keep it airworthy. Effective management has the potential to upgrade aircraft performance, extend service life, lower ownership costs, yield better safety outcomes and ensure better end of life value.



Ability to redeploy aircraft quickly:

Leasing companies need to have a diversified footprint so that they can deploy their portfolio efficiently and continue the lease income inflow once aircraft are returned by lessees.



Understanding of aviation market and risk and credit analysis:

Leasing companies need to have a grasp of the global aviation market dynamics in terms of customer needs, supply and demand scenario, and financing norms. They also need to assess the creditworthiness and soundness of the business of their customers to get desired returns on their capital.



Experienced management and specialist professional skills:

Aircraft leasing is a highly specialised business requiring deep expertise in diverse business areas, e.g. portfolio management, modes of financing, asset valuation as well as detailed market understanding. Having an experienced team of professionals thus becomes critical to the success of an aircraft lessor.



Diversification on multiple levels to manage risks:

A specialist business like aircraft leasing faces risks originating from the business environment in active geographies, shifting customer requirements in terms of types of aircraft and lease duration, exposure to foreign currency, and business sustainability of lessees, among others. Therefore, leasing companies need to have a diversified portfolio at all levels of business operations to succeed in the industry.



Aircraft regulations in the IFSC

The International Financial Services Centre (IFSC) in India was set up under the SEZ route to help India unlock its potential in the international financial services space. The International Financial Services Centres Authority Act (IFSCA Act), 2019, authorised the IFSCA as a unified regulator, with representation from India's main regulators – the Reserve Bank of India (RBI), Securities and Exchange Board of India (SEBI), Insurance and Regulatory Development Authority (IRDA), Pension Fund and Regulatory and Development Authority (PFRDA) – and the Government on its critical decision-making bodies.

In order to tap the unleashed opportunity in aircraft leasing and financing and to make the vision of 'Project Rupee Raftaar' report a reality, in October 2020, the Central Government notified aircraft leases, including operating and financial leases and any hybrid of operating and financial leases of aircraft or helicopters and engines of aircraft or helicopters, or any other part thereof, as financial products under the IFSCA Act, 2019. This step will go a long way towards consolidating India-focused financial services activities in the IFSC.

Subsequently, the IFSCA, in order to facilitate the set-up of aircraft leasing businesses in the IFSC, has provided a framework for enabling aircraft operating leases on 19 February 2021.

This framework covers an entity engaged in the business of providing aircraft or helicopters and engines of aircraft or helicopters, or any other part thereof, under an operating lease. The framework, amongst other things, includes the following:

Permissible activities

A lessor in IFSCs shall be permitted to undertake the following activities:

i. operating lease for an aircraft lease arrangement, including sale and lease back, purchase, novation, transfer, assignment, and such other similar transactions in relation to aircraft lease

ii. any other related activity with the prior approval of the IFSCA.

Eligibility criteria

An entity desirous of setting up operations in IFSCs as a lessor and undertaking permissible activities shall meet the following eligibility criteria:

- The entity shall set up operations in an IFSC in India by way of a company, limited liability partnership, a trust or in any other form as may be specified by the IFSCA.
- The person(s) in control of the aforesaid entity shall be located in a Financial Action Task Force (FATF) compliant jurisdiction.
- The entity shall deploy resources in the IFSC commensurate with the business operations under the framework.
- The entity shall comply with capital requirements as required under the framework.

Capital requirements

The IFSC entity shall have maintained the following capital requirements:

- A minimum capital of USD 2,00,000 or its equivalent in freely convertible foreign currency is to be maintained at all times by the entity.
- If required, as a risk management measure, the IFSCA may prescribe maintenance of additional capital, based on the nature and scale of business of the entity.

Further, the IFSCA (Banking) Regulations, 2020, have also permitted IFSC banking units to undertake equipment leasing, including aircraft leasing.

Also, the IFSCA proposes to introduce the IFSCA (Finance Company) Regulations, 2021, for enabling finance leasing from the IFSC.[23] Final regulations are awaited.

23 Draft IFSCA (Finance Company) Regulations, 2021, were published in January 2021 and shall be notified after public consultation.



Tax framework of aircraft leasing companies in the IFSC

Direct tax benefits/implications for units in the IFSC

Corporate tax rate

A new tax regime[24] was introduced effective 1 April 2020 which lowered the corporate tax rate to 22% (plus applicable surcharge and cess)[25] for domestic companies that opted to forego certain deductions (with an exception of deductions available to IFSCs discussed below). This new regime is only applicable to domestic companies and the rate of tax applicable to a foreign company, including a branch of foreign company in India[26], continues to be 40% (plus applicable surcharge and cess).[27]

The units in the IFSC are allowed a 100% profit-linked deduction[28] for any 10 consecutive years out of the first 15 years of operation, at the option of the taxpayer.

Under the Income-tax Act (ITA), 1961, depreciation on aircraft and aircraft engines is allowed at 40% on a written down value (WDV) basis. Any unabsorbed depreciation can be carried forward to the subsequent years to be set off against future profits, without any time limit.

Based on the above, a nil corporate tax state can potentially be achieved for the first 15 years by availing the claim of tax holiday after the first five years of operation.

Post the tax holiday, companies in the IFSC can avail the concessional tax rate of 22% (plus applicable surcharge and cess).[29]

Minimum alternate tax (MAT)

Under the ITA, companies are liable to pay MAT on their adjusted book profits where the tax liability under the normal provisions of the ITA for the tax year is not more than a specified percentage of such book profits. Where tax is paid under MAT, the tax paid over and above the normal tax liability can be carried forward and utilised for 15 years (MAT credit). The rate of MAT is 15% (plus applicable surcharge and cess)[30] and for units in the IFSC is 9% (plus applicable surcharge and cess) where the unit derives its income solely in convertible foreign exchange.

The new tax regime[31] that was introduced with effect from 1 April 2020 also made MAT inapplicable to domestic companies opting for this regime.

Thus, MAT provisions would not apply to units in the IFSC under the new tax regime. However, this benefit would not be available for the branches of foreign companies setting up units in the IFSC. MAT for such units shall continue to be 9% (plus applicable surcharge and cess) of the book profits.

24 Section 115BAA of the ITA

25 The effective rate with surcharge and cess is 25.17%.

26 Note – currently, branch model not enabled for operating leases in the IFSC.

27 The effective rate with surcharge and cess is 41.6%/42.43%/43.68%.

28 Section 80LA of the ITA

29 The effective rate with surcharge and cess is 25.17%.

30 The effective rate varies from 15.6% to 17.472% for domestic companies and 15.6% to 16.380% for foreign companies.

31 Section 115BAA of the ITA

Direct tax benefits/implications for units in the IFSC

Withholding tax (WHT) on interest payment

Presently, no WHT is required on interest paid to non-residents by units in the IFSC. This makes debt funding for aircraft leasing activity lucrative, subject to thin capitalisation norms that may be applicable on the IFSC units.

A taxpayer in India is allowed to claim an expense for any interest paid in respect of capital borrowed for the purpose of its business. Where this interest is payable to a related company, the interest expense is subject to thin capitalisation norms.

WHT on lease payments

As per the Finance Bill, 2021, it is proposed that no WHT would be required on aircraft lease payments in the nature of royalty paid to non-residents by units in the IFSC that commence operations on or before 31 March 2024. These units are also eligible for a profit-linked deduction from their income.

Capital gains on disposal of aircraft

Aircraft would be a depreciable asset for a unit in the IFSC that owns it. The ITA follows a 'block of assets' concept for depreciable assets.[32] Any gain on the sale of the aircraft may be taxable in the hands of the unit at 22% (plus applicable surcharge and cess).[33]

As per the Finance Bill, 2021, it is proposed that capital gains arising from transfer of asset being aircraft or aircraft engine would be eligible for a 100% profit-linked deduction[34] for any 10 consecutive years out of the first 15 years of operations being claimed by the unit in the IFSC on its business income. provided that the unit shall commence operations on or before 31 March 2024.

Dividend received by parent from subsidiary in the IFSC

Till 1 April 2020, any dividend declared by an Indian company attracted dividend distribution tax (DDT). This tax was payable by the company distributing dividends. The dividends were not taxable in the hands of the recipient shareholder where DDT was paid on such dividends. However, in the case of a unit in the IFSC, DDT was not applicable.

With effect from 1 April 2020, DDT has been abolished, and a company paying dividends to its shareholders is required to withhold tax. Currently, there is no exemption with respect to WHT on dividends paid by IFSC units, unlike the exemption from DDT. However, withholding tax on dividend income shall be available as credit in the hands of the shareholders.

32 *Under the 'block of assets' concept, depreciation is computed with reference to the full value of the block and not with respect to individual assets included in the block. In case of a disposal of any depreciable asset, the sale value is reduced from the carrying value (WDV) of the relevant block, and depreciation is allowed on the balance amount. In cases where the sale value exceeds the carrying value of the block or the block ceases to exist, any gain/loss arising therefrom is taxed as short-term capital gain (or loss).*

33 *The effective rate with surcharge and cess is 25.17%.*

34 *Proposed inclusion in Section 80LA of the ITA*

Tax and regulatory benefits/implications for foreign companies setting up units in the IFSC

Interest income from IFSC units (in the hands of the recipient)

As mentioned above, no WHT is required on interest paid to non-residents by units in the IFSC.

This interest income arising to a non-resident lender in respect of monies borrowed from it by an IFSC unit is also exempt[35] from tax in India. Thus, any interest from an IFSC unit received by a non-resident lender would not be taxable in India.

Lease income from IFSC units (in the hands of the recipient)

As mentioned above, no WHT is required on aircraft lease payments in the nature of royalty made to non-residents by units in the IFSC.

This leasing income which is otherwise taxable as royalty arising to a non-resident lender in respect of aircraft leased from it by an IFSC unit is also exempt[36] from tax in India. Thus, aircraft leasing income in the nature of royalty from an IFSC unit received by a non-resident lessor would not be taxable in India.



35 Section 10(15)(ix) of the ITA

36 Proposed section 10(4F) of the ITA

Indirect tax benefits/implications for units in the IFSC

Import of goods/services into the IFSC/SEZ

- **Procurement on operating lease basis**
- **Procurement on outright purchase basis**

- Import of goods (aircraft/ aircraft engine) into the IFSC/SEZ is not subject to basic custom duty (BCD).
- Leasing of aircraft/aircraft engine into the IFSC is not subject to Integrated Goods and Services Tax (IGST). However, this is subject to the condition that the services are procured for authorised operations in an SEZ.

Leasing (operating lease) of aircraft/aircraft engine to an Indian airline company by an Indian lessor in the IFSC/SEZ

- Import of goods (aircraft/ aircraft engine) by an Indian airline company (operator) from an Indian lessor in the IFSC/SEZ is not subject to BCD. However, this is subject to the condition that the aircraft is imported by the operator (or on behalf of the operator) for scheduled air operations.
- Leasing of aircraft/aircraft engine by the Indian lessor in the IFSC/SEZ to an Indian airline company is subject to IGST at the rate of 5% under forward charge. The airline company should be eligible to claim ITC subject to satisfaction of conditions.



Other tax benefits and state-level subsidies for units in the IFSC

Stamp duty

A unit in the IFSC, engaged in the aircraft leasing business, has been granted a waiver from payment of stamp duty on all activities related to setting up of units in the IFSC and acquisition of any movable property (including aircraft) or immovable property for a period of 10 years commencing from 4 August 2020. However, this waiver may not be available on the stamp duty arising on the sale of an aircraft.

Gujarat state-level subsidies

Nature of subsidy	Eligibility	Subsidy	
Electricity duty and subsidy on tariff	Developers and units	Reimbursement of electricity duty and INR 1 subsidy on tariff	
Reimbursement of PF contribution by employer	Units	• 100% of EPF amount paid in case of female employees • 75% of EPF amount paid in case of male employees	
Lease rental subsidy for every 50 sq. ft. per employee	Units	Up to 20 employees	INR 8 per sq. ft.
		20–100 employees	INR 5 per sq. ft.
		Above 100 employees	INR 3 per sq. ft.
Capital subsidy for hardware, networking and related hardware	Units	Up to INR 10 Million	
Stamp duty and registration/ conversion fee exemption	Developers and units	Wherever cost is incurred	
Patent assistance	Units	At the rate of 50%, subject to a ceiling of INR 2 lakh per patent for domestic patents and INR 5 lakh per patent for international patents	

The above subsidies have been brought in by the Government of Gujarat under its IT/ITeS Policy (2016–21). A new IT/ITeS policy is envisaged soon that combines existing benefits and various other new benefits for IFSC units.

Comparative tax analysis of the IFSC vis-à-vis major aircraft leasing centres

as on 21 Feb 2021[37]

Particulars	India (in the IFSC)*	Ireland	Hong Kong	China	Singapore
Corporate tax rate	100% tax exemption for 10 consecutive years out of 15 years. (however, no group loss relief transfers available)	12.5% (group loss relief transfers available)	16.5% (reduced to 8.25% for qualifying aircraft leasing and leasing management companies)	25%	17% (reduced to 8% for income derived from aircraft leasing activities [group loss relief transfers available])
MAT for lessor company	Nil – if opting for the new tax regime, else 9%	Not applicable	Not applicable	Not applicable	Not applicable
Dividend to shareholders of company	Taxable in the hands of the non-resident shareholders – 20% (lower tax treaty rate can be applied) Taxable in the hands of resident shareholders – ~25–40%	Nil (certain cases taxable at 25%)	Nil	10%	Nil
Tax depreciation allowance	Allowed to depreciate the aircraft cost (at 40% WDV) Almost the entire value depreciated over 8 years	Allowed to depreciate the aircraft cost over 8 years	Not applicable	Allowed to depreciate the aircraft cost less residual value over 10 years	Can depreciate the aircraft over any number of years from 5–20 years
Interest expense on aircraft loan/ intercompany funding	Deductible on arm's length payments	Deductible on arm's length payments	Deductible subject to fulfilment of certain conditions	Deductible on arm's length payments	Deductible on arm's length payments
WHT on interest payment by lessor	Nil	20% (exemption available to payments to 'qualifying lender'); typically would be 'zero' WHT	Nil	10% (maybe reduced by applicable tax treaty)	Nil

37 Extracted from Project Rupee Raftaar and updated as on date

Particulars	India (in the IFSC)*	Ireland	Hong Kong	China	Singapore
WHT on lease rental paid to lessor	Indian entity to IFSC lessor – 2% IFSC lessee to foreign entity (paid as royalty) – nil**	Nil	10%	10%	10%
Taxable base	Gross rentals less deductible expenses, including depreciation allowance Generally, no cash tax liability in early years since significant tax depreciation allowance is available	Gross lease rentals less deductible expenses, including depreciation allowance Generally, no cash tax liability in early years (prolonged for leasing platforms with particular levels of growth) since significant tax depreciation allowance available	20% (gross lease rentals less allowable expenses, excluding depreciation) Effective tax rate – ~3%–7%	Gross lease rentals less deductible expenses, including depreciation allowance	Gross lease rentals less deductible expenses, including depreciation allowance Generally, no cash tax liability in early years (prolonged for leasing platforms with particular levels of growth) since significant tax depreciation allowance available
Disposal of aircraft	Capital gains on disposal of aircraft leased to an Indian company eligible for 100% deduction provided that the IFSC unit has commenced operations on or before 31 March 2024**	Taxable as business income to the extent of the original cost claimed as tax depreciation. Any gain in excess of this amount may be taxed as trading profits at 12.5% depending on the facts (33% capital gains tax applicable in certain circumstances)	Not subject to tax on aircraft disposal after 3 years	Capital gains is taxed as part of operating income at 25%	Taxable as business income to the extent of the original cost claimed as tax depreciation Any gain in excess of this amount may not be subject to tax on disposal if the gain is regarded as capital in nature (17% tax applies if any gain is regarded as revenue in nature)
GST on lease rental payments by Indian airlines	5%	5%	5%	5%	5%
Stamp duty	Nil	Nil	Nil	0.1–0.005% depending on the nature of lease arrangement	Nil

* The above tax rates are exclusive of applicable surcharge and cess.
**The above tax proposals shall be subject to the tax holiday period available to the IFSC unit. Further, these proposals have been introduced in the Finance Bill, 2021.



Way forward

The aircraft leasing business has huge potential to contribute to the growth of the economy through higher tax revenue collection, employment opportunities and affordable air travel. At this junction, it is vital to develop this business line in the IFSC in India, given the immense demand for aircraft from airlines, high growth in passenger traffic and aircraft leasing's position as the most profitable leg in the aviation supply chain. Development of the aviation leasing sector in the IFSC will create a complete ecosystem for the aviation sector in India. This would generate employment opportunities in aircraft leasing companies as well as ancillary activities such as lease management, legal and accounting.

In order to promote aircraft leasing in the IFSC, it was imperative to benchmark the ecosystem with leading regimes. The recent tax and regulatory changes seek to bring India on par with those regimes.

With tremendous focus and support from the Central Government, India's aircraft leasing market is only set to become stronger and more attractive.

Glossary

Abbreviation	Definition
BBAM	Babcock & Brown Aircraft Management
BCD	Basic custom duty
BOC	Bank of China
CAPA	Centre for Aviation
Cos	Companies
COVID-19	Coronavirus Disease 2019
DAE	Dubai Aerospace Enterprise
DDT	Dividend distribution tax
DGCA	Directorate General of Civil Aviation
DTA	Domestic Tariff Area
EPF	Employee Provident Fund
FATF	Financial Action Task Force
GDP	Gross domestic product
GE	General Electric
GECAS	GE Capital Aviation Services
GIFT City	Gujarat International Finance Tec-City
IATA	International Air Transport Association
IFSC	International Financial Services Centre
IFSCA	International Financial Services Centres Authority
IFSCA Act	International Financial Services Centres Authority Act, 2019
IGST	Integrated Goods and Services Tax

Glossary

Abbreviation	Definition
IRDA	Insurance and Regulatory Development Authority
IT	Information technology
ITA	Income-tax Act, 1961
ITC	Input tax credit
ITeS	Information technology enabled services
LCCs	Low-cost carriers
MAT	Minimum alternate tax
Mn	Million
MRO	Maintenance, repair and operations
NBFC	Non-banking financial company
PF	Provident Fund
PFRDA	Pension Fund and Regulatory and Development Authority
RBI	Reserve Bank of India
RPKs	Revenue passenger kilometres
SEBI	Securities and Exchange Board of India
SEZ	Special Economic Zone
SMBC	Sumitomo Mitsui Banking Corporation
sq. ft.	Square feet
WDV	Written down value
WHT	Withholding tax

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