Tit-Bits for Doing Business in India

Introduction

Business activities in India can be carried out either singly or collectively through different legal entities. An entrepreneur has to take a decision about the form of business organization depending upon the availability and requirement of resources, magnitude of risk, need of administration and legal requirements.

The following are the principal forms of business organizations in India :

Sole Proprietorship Concern
Partnership Firm
Corporations, both Public and Private
Limited Liability Partnership (LLP)

India has a federal system of Government with clear demarcation of powers between the Central Government and the State Governments.

The Liberalisation process that began about 18 years ago in 1991 has come along way. The Indian economy is increasingly integrating with the global economy. This integration has created a climate conducive to increase in inward investment, free flow of capital skill and technology between India and the other country. This has also resulted in an increased flow of capital from India, as can be seen form various acquisitions by Indian business overseas.

Resident / Non-Resident:

If an individual stays in India for more than 182 days during the course of the preceding financial year, he weill be treated as a person resident in India. There are a few exceptions as under:

-If a person goes/stays outside India for (a) taking up employment, or (b) carrying on business or vocation, or © for any other purpose for an a uncertain period; he will be treated as a person resident outside India(non- resident).

-If a person comes to /stays in India for (a) taking up employment, or (b) carrying on business or vocation, or © for any other purpose for an a uncertain period; he will be treated as a person resident in India.

Following persons (other than individuals) will be treated as person resident in India:

Person or body corporate which is registered or incorporated in India
An office, branch or agency in India, even if it is owned or contorled by a person resident outside India.
An office, branch or agency outside India, if it is owned or controlled by a person resident in India.

Financial System:

India has a financial system that is regulated by independent regulators in the sectors of banking, insurance, capital markets, competition and various services sectors. In a number of sectors Government plays the role of regulator.

Ministry of Finance, Government of India looks after financial sector in India. Finance Ministry every year presents annual budget during February in the Parliament. The annual budget proposes changes in taxes, changes in government policy in almost all the sectors and budgetary and other allocations for all the Ministries of Government of India. The annual budget is passed by the Parliament after debate and takes the shape of law.

Reserve bank of India (RBI) established in 1935 is the Central bank. RBI is regulator for financial and banking system, formulates monetary policy and prescribes exchange control norms. The Banking Regulation Act, 1949 and the Reserve Bank of India Act, 1934 authorize the RBI to regulate the banking sector in India.

India has commercial banks, co-operative banks and regional rural banks. The commercial banking sector comprises of public sector banks, private banks and foreign banks. The public sector banks comprise the 'State Bank of India' and its seven associate banks and nineteen other banks owned by the government and account for almost three fourth of the banking sector. The Government of India has majority shares in these public sector banks.

India has a two-tier structure of financial institutions with thirteen all India financial institutions and forty-six institutions at the state level. All India financial institutions comprise term-lending institutions, specialized institutions and investment institutions, including in insurance. State level institutions comprise of State Financial Institutions and State Industrial Development Corporations providing project finance, equipment leasing, corporate loans, short-term loans and bill discounting facilities to corporate. Government holds majority shares in these financial institutions.

Non-banking Financial Institutions provide loans and hire-purchase finance, mostly for retail assets and are regulated by RBI.

Insurance sector in India has been traditionally dominated by state owned Life Insurance Corporation and General Insurance Corporation and its four subsidiaries. Government of India has now allowed FDI in insurance sector up to 26%. Since then, a number of new joint venture private companies have entered into life and general insurance sectors and their share in the insurance market in rising. Insurance Development and Regulatory Authority (IRDA) is the regulatory authority in the insurance sector under the Insurance Development and Regulatory Authority Act, 1999.

RBI also regulates foreign exchange under the Foreign Exchange Management Act (FEMA). India has liberalized its foreign exchange controls. Rupee is freely convertible on current account. Rupee is also almost fully convertible on capital account for non-residents. Profits earned, dividends and proceeds out of the sale of investments are fully repatriable for FDI. There are restrictions on capital account for resident Indians for incomes earned in India.

Securities and Exchange Board of India (SEBI) established under the Securities and Exchange aboard of India Act, 1992 is the regulatory authority for capital markets in India. India has 23 recognized stock exchanges that operate under government approved rules, bylaws and regulations. These exchanges constitute an organized market for securities issued by the central and state governments, public sector companies and public limited companies. The Stock Exchange, Mumbai and National Stock Exchange are the premier stock exchanges. Under the process of de-mutualization, these stock exchanges have been converted into companies now, in which brokers only hold minority share holding. In addition to the SEBI Act, the Securities Contracts (Regulation) Act, 1956 and the Companies Act, 1956 regulates the stock markets.

Repatriation of investment capital and profits earned in India

(i) All foreign investments are freely repatriable, subject to sectoral policies and except for cases where Non Resident Indians choose to invest specifically under non-repatriable schemes. Dividends declared on foreign investments can be remitted freely through an Authorized Dealer.
(ii) Non-residents can sell shares on stock exchange without prior approval of RBI and repatriate through a bank the sale proceeds if they hold the shares on repatriation basis and if they have necessary NOC/ tax clearance certificate issued by Income Tax authorities.
(iii) For sale of shares through private arrangements, Regional offices of RBI grant permission for recognized units of foreign equity in Indian company in terms of guidelines indicated in Regulation 10.B of Notification No. FEMA.20/2000 RB dated May '2000. The sale price of shares on recognized units is to be determined in accordance with the guidelines prescribed under Regulation 10B(2) of the above Notification.
(iv) Profits, dividends, etc. (which are remittances classified as current account transactions) can be freely repatriated.

Acquisition of Immovable Property by Non-resident

A person resident outside India, who has been permitted by Reserve Bank of India to establish a branch, or office, or place of business in India (excluding a Liaison Office), has general permission of Reserve Bank of India to acquire immovable property in India, which is necessary for, or incidental to, the activity. However, in such cases a declaration, in prescribed form (IPI), is required to be filed with the Reserve Bank, within 90 days of the acquisition of immovable property.

Foreign nationals of non-Indian origin who have acquired immovable property in India with the specific approval of the Reserve Bank of India cannot transfer such property without prior permission from the Reserve Bank of India.

Acquisition of Immovable Property by NRI

An Indian citizen resident outside India (NRI) can acquire by way of purchase any immovable property in India other than agricultural/ plantation /farm house. He may transfer any immovable property other than agricultural or plantation property or farm house to a person resident outside India who is a citizen of India or to a Person of Indian Origin resident outside India or a person resident in India.

Foreign Institutional Investors (FIIs) are allowed to invest in India in the securities traded in both primary and secondary capital markets. These securities include shares, debentures, warrants, and units of mutual funds, government securities and derivative instruments.

The term FII is defined as an institution established or incorporated outside India for making investment in Indian securities and also includes a sub-account of an FII. FIIs include Asset Management Companies, Pension Funds, Mutual Funds, Investment Trust as nominee companies, Incorporated/Institutional Portfolio managers or their power attorney holders, University Funds, Endowment Foundations, Charitable Trusts and Charitable Societies.

FIIs, must register with Securities and Exchange Board of India (SEBI) and shall comply with the Exchange Control Regulations of RBI.

Taxation System in India

India has a well-developed tax structure with clearly demarcated authority between Central and State Governments and local bodies. Central Government levies taxes on income (except tax on agricultural income, which the State Governments can levy), customs duties, central excise and service tax.

Value Added Tax (VAT), stamp duty, State Excise, land revenue and tax on professions are levied by the State Governments. Local bodies are empowered to levy tax on properties, octroi and for utilities like water supply, drainage etc.

In last 10-15 years, Indian taxation system has undergone tremendous reforms. The tax rates have been rationalized and tax laws have been simplified resulting in better compliance, ease of tax payment and better enforcement. The process of rationalization of tax administration is ongoing in India.

Since April 01, 2005, most of the State Governments in India have replaced sales tax with VAT.
Taxes Levied by Central Government

Direct Taxes
- Tax on Corporate Income
- Capital Gains Tax
- Personal Income Tax
- Wealth Tax
- Gift Tax

Indirect Taxes
- Excise Duty
- Customs Duty
- Service Tax
- Securities Transaction Tax

Taxes Levied by State Governments and Local Bodies
- Sales Tax/VAT
- Other Taxes

Direct Taxes

Taxes on Corporate Income

Companies residents in India are taxed on their worldwide income arising from all sources in accordance with the provisions of the Income Tax Act. Non-resident corporations are essentially taxed on the income earned from a business connection in India or from other Indian sources. A corporation is deemed to be resident in India if it is incorporated in India or if it's control and management is situated entirely in India.

Domestic corporations are subject to tax at a basic rate of 30% and Surcharge of 10% is leviable if net taxable income exceeds Rs. 1 Crore. Foreign corporations have a basic tax rate of 40% and Surcharge of 10% is leviable if net taxable income exceeds Rs. 1 Crore.. In addition, education cess+Secondary & Higher education cess at the rate of 3% on the tax payable is also charged. Corporates are subject to wealth tax at the rate of 1%, if the net wealth exceeds Rs.1.5 mn.

Domestic corporations have to pay dividend distribution tax at the rate of 15%, however, such dividends received are exempt in the hands of recipients.

Corporations also have to pay for Minimum Alternative Tax at 15% (plus surcharge and education cess) of book profit as tax, if the tax payable as per regular tax provisions is less than 15% of its book profits.

Capital Gains Tax

Tax is payable on capital gains on sale of assets.

Long-term Capital Gains Tax is charged if
• Capital assets are held for more than three years and
• In case of shares, securities listed on a recognized stock exchange in India, units of specified mutual funds, the period for holding is one year.

Long-term capital gains are taxed at a basic rate of 20%. However, long-term capital gain from sale of equity shares or units of mutual funds are exempt from tax.

Short-term capital gains are taxed at the normal corporate income tax rates. Short-term capital gains arising on the transfer of equity shares or units of mutual funds are taxed at a rate of 10%.

Long-term and short-term capital losses are allowed to be carried forward for eight consecutive years. Long-term capital losses may be offset against taxable long-term capital gains and short-term capital losses may be offset against both long term and short-term taxable capital gains.

Personal Income tax

Personal income tax is levied by Central Government and is administered by Central Board of Direct taxes under Ministry of Finance in accordance with the provisions of the Income Tax Act. The rates for personal income tax are as follows:-

Income range (Rupee) Tax Rate (%)

Tax %	Income (INR)
0%	1 - 160,000
10%	160,001 - 300,000
20%	300,001-500,000
30%	500,001 and above

Rates of Withholding Tax

Current rates for withholding tax for payment to non-residents are:-

(i) Interest 20%
(ii) Dividends paid by domestic companies: Nil
(iii) Royalties 10%
(iv) Technical Services 10%
(v) Any other services Individuals: 30% of the income
Companies: 40% of the net income

The above rates are general and are applicable in respect of countries with which India does not have a Double Taxation Avoidance Agreement (DTAA).

Tax Incentives

Government of India provides tax incentives for:-
• Corporate profit
• Accelerated depreciation allowance
• Deductibility of certain expenses subject to certain conditions.

These tax incentives are, subject to specified conditions, available for new investment in
• Infrastructure,
• Power distribution,
• Certain telecom services,
• Undertakings developing or operating industrial parks or special economic zones,
• Production or refining of mineral oil,
• Companies carrying on R&D,
• Developing housing projects,
• Undertakings in certain hill states,
• Handling of food grains,
• Food processing,
• Rural hospitals etc.

Double Tax Avoidance Treaty

India has entered into DTAA with 65 countries including the US. In case of countries with which India has Double tax Avoidance Agreement, the tax rates are determined by such agreements. Domestic corporations are granted credit on foreign tax paid by them, while calculating tax liability in India.

In the case of the US, dividends are taxed at 20%, interest income at 15% and royalties at 15%.

Indirect Taxes

Excise Duty

Manufacture of goods in India attracts Excise Duty under the Central Excise act 1944 and the Central Excise Tariff Act 1985. Herein, the term Manufacture means bringing into existence a new article having a distinct name, character, use and marketability and includes packing, labeling etc. Though the tax levy is on the manufacture of goods, the tax is required to be paid on removal of goods from the factory premises where the manufacture takes place. The duty is levied at the rates specified in the Excise Tariff.

The rate at which excise duty is leviable on the goods depends on the classification of the goods under the Excise Tariff. The Excise Tariff is primarily based on the Harmonized System of Nomenclature (HSN). The Government has adopted an eight digit classification under the Excise Tariff so as to bring it in conformity with the Customs Tariff.

Most of the products attract excise duties at the rate of 8%. Some products also attract special excise duty/and an additional duty of excise above the 8% excise duty. 2% education cess+1% secondary education cess are also applicable on the aggregate of the duties of excise. Excise duty is levied on ad valorem basis or based on the maximum retail price in some cases.

The central excise duty is a modified VAT wherein a manufacturer is allowed the credit of the excise duty paid on locally sourced goods and the Additional Duty of Customs on imported goods. The CENVAT credit can be utilized for the payment of excise duty on the clearance fo dutiable final products manufactured in India. The Finance Act 2004 had introduced the integration of goods and services tax. Therefore, manufacturers of dutiable final products would also be eligible to avail

CENVAT credit of the service taxes paid on input services used both in the or in relation to the manufacture of final products and clearances of final products from the place of removal. In addition, CENVAT credit would be admissible on the following input services:

- Services used in relation to setting up of factory or an office relating to such factory.
- Advertisement or sales promotion services
- Services in relation to the procurement of inputs.
- Activities relating to management of business such as accounting , auditing, financing, Recruitment and quality control.

Exemption limit for small scale industry (SSI) is Rs.1.5 crore;
Specific rates of duty are applicable on cigarettes and biris.
Central Excise duty is administered by the Central Board of Excise and Customs.

Customs Duty

The levy and the rate of customs duty in India are governed by the Customs Act 1962 and the Customs Tariff Act 1975. Imported goods in India attract basic customs duty, additional customs duty and education cess. The rates of basic customs duty are specified under the Tariff Act. The peak rate of basic customs duty has been reduced to 10% for industrial goods. Additional customs duty(CVD) is equivalent to the excise duty payable on similar goods manufactured in India.
In addition, all imports w.e.f. 01.03.2006 are chargeable to an additional duty of customs @4% in lieu of Sales tax /VAT with few exceptions. Education cess at 2% + 1% secondary education cess is also leviable on the aggregate of duties of customs. Customs duty is calculated on the transaction value of the goods.
Customs duties in India are administrated by Central Board of Excise and Customs under Ministry of Finance.

Service Tax

Service tax is levied at the rate of 10% (plus 2% education cess+1% secondary and higher education cess) on certain identified taxable services provided in India by specified service providers. Service tax on taxable services rendered in India are exempt, if payment for such services is received in convertible foreign exchange in India and the same is not repatriated outside India. The Cenvat Credit Rules allow a service provider to avail and utilize the credit of additional duty of customs/excise duty for payment of service tax. Credit is also provided on payment of service tax on input services for the discharge of output service tax liability.

Service provider is not required to pay service tax if the aggregate value of services rendered does not exceed Rs. 10 lacs in any financial year subject to the fulfillment of the certain conditions. In terms of the provisions, as amended from time to time, service provider is required to be registered with the jurisdictional service tax authorities. However, he need not register if the value of the service provide does not exceed Rs. 9 Lacs.

Generally, the liability to deposit service tax lies with the service provider. In case the service provider is a non-resident, not having an office in India, the person liable to pay the serive tax is the service recipient in India. The services so received shall be treated as input services and shall not to be treated as output services for the purpose of availing of CENVAT Credits on inputs/ input services.

Securities Transaction Tax

Transactions in equity shares, derivatives and units of equity-oriented funds entered in a recognized stock exchange attract Securities Transaction Tax at the following rate:-

• Delivery base transactions in equity shares or buyer and seller
each units of an equity-oriented fund - 0.075%
• Sale of units of an equity-oriented fund to the seller mutual fund - 0.15%
• Non delivery base transactions in the above - 0.015%
• Derivatives (futures and options) seller - 0.01%

Sales Tax/VAT

Sales tax is levied on the sale of movable goods. Most of the Indian States have replaced Sales tax with a new Value Added Tax (VAT) from April 01, 2005. VAT is imposed on goods only and not services and it has replaced sales tax. Other indirect taxes such as excise duty, service tax etc., are not replaced by VAT. VAT is implemented at the State level by State Governments. VAT is applied on each stage of sale with a mechanism of credit for the input VAT paid. There are four slabs of VAT:-

• 0% for essential commodities
• 1% on bullion and precious stones
• 4% on industrial inputs and capital goods and items of mass consumption
• All other items 12.5%

In general, all the goods, will be covered under VAT and will get the benefit of input tax credit. Liquor, lottery tickets, petrol , diesel, aviation turbine fuel and other motor spirit are outside VAT, but continue to be taxed under the Sales Tax Act or any of the State Act.

For interstate sale, the provisions under the Central Sales Tax Act would be applicable. The rate of Central Sales Tax (CST) vary between 2%, 10% or the State Sales tax rate, whichever is higher. Where goods are bought and sold by registered dealers for use as inputs in the manufacture of other goods or activities (such as mining or telecommunication networks), the rate of sales tax is 2%, provided Form C is issued by the purchasing dealer. In the absence of Form C the rate would be 10% or the State sales tax rate, whichever is higher.

Works Contract Tax

The works contact tax is levied on the transfer of property in goods involved in the course of the execution of a works contract. Contracts for the construction of bridges, power plants, etc. or for repairs, erection, etc. could attract the works contract tax.

Basically, the tax is levied only on the value of the material supplied under the contract and thus the value of labour and services are allowed as deductions. In addition, various other deductions are also available and these vary from one state to another. Most states also provide for a composition whereby, the works contract tax is levied at a fixed rate on the entire value of the contract without any deductions. The rate of tax is either equivalent to the rate of the sales tax on similar goods or in some cases a specific rate of tax is prescribed, regardless of the nature of gods supplied.

Municipal/Local Taxes

• Octori/entry tax: -

Octroi/entry tax is levy on the entry of goods into a particular municipal/state jurisdiction for use, consumption or sale within such jurisdiction. The rate of Octroi/Entry tax on different products may vary from state to state.

Other State Taxes

• Stamp duty on transfer of assets
• Property/building tax levied by local bodies
• Agriculture income tax levied by State Governments on income from plantations
• Luxury tax levied by certain State Government on specified goods

Stamp Duty

Almost all documents, such as bills of exchange, promissory notes, insurance policies, contracts effecting transfer of shares, debenture, and conveyances for transfer of immovable property, executed in India are chargeable to Stamp Duty at various rates. The rate structure is decided by the States. The legal enforceability of any document requiring to bear stamp duty is considered by any authority only when it bears stamp at the prescribed rate applicable in the place of its execution.

Important Economic Laws in India

Reserve Bank of India Act 1934

Insurance Act , 1938
Industries (Development and Regulation) Act, 1951

Industrial Disputes Act, 1947

Environment (Protection) Act, 1986

Foreign Trade (Development and Regulation) Act, 1992

Income-tax Act , 1961

Foreign Exchange Management Act , 1999

Customs Act, 1962

Customs Tariff Act 1975

Central Excise Act, 1944

Central Excise Tariff Act, 1985, 1986

Companies Act , 1956

Patents Act , 1970

Copyright Act 1957

Trade Marks Act , 1999

Securities and Exchange Board of India Act 1992

Indian Penal Code 1860

Indian Evidence Act 1872

Central Electricity Act 2003

Information Technology Act 2000

Constitution of India

India provides protection to Intellectual Property Rights in accordance with its obligations under the TRIPS Agreement of the WTO. The importance of intellectual property in India is well established at all levels- statutory, administrative and judicial.

India has well-established administrative mechanism for enforcement of Intellectual Property Rights. Police officers are empowered to take action against the infringement of IPRs in case of pirated and counterfeit products.

Cases of infringement of IPRs are tried in the judicial courts. Indian Intellectual Property Rights Laws also provide for appeals in the judicial courts of the administrative decisions relating to Intellectual Property Rights.

State Governments

India has a federal system of government with clear demarcation of powers. The states deal with subjects of law & order, agriculture, sales tax, minor minerals, electricity, health, education, irrigation, water supply, minor ports, roads, etc.

With liberalization of Indian economy, both domestic and foreign investors now mainly require to interact with state governments and local bodies for seeking various regulatory approvals and for getting land and necessary infrastructure.

Most of the state governments have set up a number of industrial parks with necessary infrastructure for power, water, roads, etc. Investors could take land on lease or purchase land from the state level corporations for setting up their units. These industrial parks have been developed either by State Industrial Development Corporations, State Infrastructure Development Corporations or by private sector or in joint sector. Many states provide single window clearance for many regulatory approvals and for getting infrastructure for units being setup in these industrial parks. Some of these parks are also for specific sector such as information technology, biotechnology, food processing, garments, etc.

Industrial Licensing

With progressive liberalization and deregulation of the economy, industrial license is required in very few cases. Industrial licenses are regulated under the Industries (Development and Regulation) Act 1951. At present, industrial license is required only for the following: -

1. Industries retained under compulsory licensing
2. Manufacture of items reserved for small scale sector by larger units
3. When the proposed location attracts locational restriction

The following industries require compulsory license: -

I Alcoholics drinks
II Cigarettes and tobacco products
III Electronic aerospace and defense equipment
IV Explosives
V Hazardous chemicals such as hydrocyanic acid, phosgene, isocynates and di-isocynates of hydro carbon and derivatives

Procedure for obtaining an industrial license

Industrial license is granted by the Secretariat for Industrial Assistance in Department of Industrial Policy and Promotion, Government of India. Application for industrial license is required to be submitted in Form FC-IL to Department of Industrial Policy and Promotion.

Small Scale Sector

Ministry of Agro and Rural Industries and Ministry of Small Scale industries have been merged into a single Ministry, namely, Ministry of Micro, Small and Medium Enterprises(MSME).

In accordance with the provision of Micro, Small & Medium Enterprises Development (MSMED) Act, 2006 the Micro, Small and Medium Enterprises (MSME) are classified in two Classes:

Manufacturing Sector	
Enterprises	**Investment in plant & machinery**
Micro Enterprises	Does not exceed twenty five lakh rupees
Small Enterprises	More than twenty five lakh rupees but does not exceed five crore rupees
Medium Enterprises	More than five crore rupees but does not exceed ten crore rupees
Service Sector	
Enterprises	**Investment in equipments**
Micro Enterprises	Does not exceed ten lakh rupees:
Small Enterprises	More than ten lakh rupees but does not exceed two crore rupees
Medium Enterprises	More than two crore rupees but does not exceed five core rupees

Locational restrictions

Industrial undertakings to be located within 25 kms of the standard urban area limit of 23 cities having a population of 1 million as per 1991 census require an industrial license. Industrial license even in these cases is not required if a unit is located in an area designated as an industrial area before 1991 or non-polluting industries such as electronics, computer software, printing and other specified industries.

Environmental Clearances

Entrepreneurs are required to obtain Statutory clearances, relating to Pollution Control and Environment as may be necessary, for setting up an industrial project for 31 categories of industries in terms of Notification S.O. 60(E) dated 27.1.94 as amended from time to time, issued by the Ministry of Environment and Forests under The Environment (Protection) Act 1986. This list includes petrochemicals complexes, petroleum refineries, cement, thermal power plants, bulk drugs, fertilizers, dyes, papers etc.,

However, if investment in the project is less than Rs.1 billion, such Environmental clearance is not necessary, except in cases of pesticides, bulk drugs and pharmaceuticals, asbestos and asbestos products, integrated paint complexes, mining projects, tourism projects of certain parameters, tarred roads in Himalayan areas, distilleries, dyes, foundries and electroplating industries.

Setting up industries in certain locations considered ecologically fragile (e.g. Aravalli Range, coastal areas, Doon Valley, Dahanu etc.) are guided by separate guidelines issues by the Ministry of Environment and Forests.

Other approvals/clearances at State level

Land, Water, Electricity, Registrations etc.

Setting up Liaison / Representative / Branch / Project Office

Liaison Office / Representative Office

A Liaison Office could be established with the approval of Reserve Bank of India. The role of Liaison Office is limited to collection of information, promotion of exports/imports and facilitate technical/financial collaborations.

Liaison office cannot undertake any commercial activity directly or indirectly.

Project Office

Foreign companies planning to execute specific projects in India can set up a temporary project/site offices in India for carrying out activities only relating to that project. RBI has now granted general permission to foreign entities to establish project offices subject to specified conditions.

Branch Office

Foreign companies engaged in manufacturing and trading activities abroad are allowed to set up branch offices in India for the purposes of export/import of goods, rendering professional or consultancies services, R&D, promoting technical or financial collaborations, representing the parent company, acting as buying/selling agents, rendering services in IT and development of software, rendering technical support to the products supplied by the parent/group companies, foreign airline/shipping companies. Branch offices could be established with the approval of RBI and may remit outside India profit of the branch, subject to RBI guidelines after payment of applicable Indian taxes.

Special Privileges for Non-Resident Indians (NRIs)

Government of India has provided some special privileges to Non-resident Indians (NRIs) in areas of foreign exchange, investments including in financial sector, investment in real estate etc. These privileges are over and above the rules applicable to non-residents foreigners.

Persons of Indian Origin (PIO) and Overseas Citizens of India (OCI) have been given same privileges in economic field as NRIs except for investment in agricultural lands.

NRIs / OCI / PIO are granted the following facilities:

• Maintenance of bank accounts in India
• Investment in securities/shares of, and deposits with Indian firms/companies
• Investments in immovable properties in India

The following regulatory approvals may be required for setting a unit:

• Building plan approval by local body
• Permission under Factories and Boilers Act from the Inspectorate of Factories and Boilers
• Permission from Inspectorate of Electricity for safety of power system
• Permission from State Pollution Control Board for certain type of industries
• Approval from Labour Department
• Approval from Drugs Inspectorate for manufacturing pharmaceutical products
• Infrastructure required for setting up a unit may be obtained from the following agencies:
• Power Connection from the State Electricity Board
• Water supply connection from the local body/Water Authority or the other relevant agency
• Land could be taken on lease or bought from agency running an industrial park or could be bought from private individuals

Special Economic Zones (SEZ)

The Foreign Trade Policy of Government of India provides for setting up of Special Economic Zones (SEZ) in the country with a view to provide an internationally competitive hassle free environment for exports. Units may be set up in SEZ for manufacture of goods and rendering of services. The units in SEZs have to be a net foreign exchange earner but they are not subjected to any pre-determined value addition or minimum export performance requirements. Sales in the domestic tariff area by SEZ units shall be subject to payment of full custom duty and import policy inflows.

SEZs could be set up in public, private, joint sector or by State governments. 100% FDI is allowed in setting up of SEZs. The government of India has also converted existing Export Processing Zones into SEZs.

The minimum size of the SEZs shall be 1000 hectares except in product specific and port/airport based SEZs. Approval for setting up of new SEZs is given by Department of Commerce, Government of India.

For setting up units in SEZs, all approvals are given by a Committee headed by Development Commissioner of the concerned SEZ. For setting up a unit in SEZ, application in prescribed format should be submitted to the development Commissioner.

Facilities to SEZ Units

Detailed policy applicable to SEZ units is given in Appendix 14-II of Handbook of Procedures Vol-I of Director General of Foreign Trade (DGFT).

- SEZ units may import or procure from the domestic sources, duty free, all their requirements of capital goods, raw materials, consumables, office equipment etc., for setting up of units or further operations without any license or specific approval
- Goods imported/procured locally duty free could be utilized over the approval period of five years
- 100% income tax exemption (Section 10 A) for first five years and 50% for two years thereafter
- 100% FDI is allowed in manufacturing sector in SEZ units under automatic route except sectors requiring industrial license. 100% FDI allowed in items reserved for small scale units
- Setting up of offshore banking units allowed in SEZs. They would be entitled for 100% income tax exemption for three years and 50% for next two years
- More flexible exchange control regulations for units in SEZs and for external commercial borrowing upto $ 500 million in a year
- Exemption from service tax to SEZ units

Human Resources :

India provides for core labour standards of ILO for welfare of workers and to protect their interests. India has a number of labour laws addressing various issues such as resolution of industrial disputes, working conditions, labour compensation, insurance, child labour, equal remuneration etc. Labour is a subject in the concurrent list of the Indian Constitution and is therefore in the jurisdiction of both central and state governments. Both central and state governments have enacted laws on labour issues. Central laws grant powers to officers under central government in some cases and to the officers of the state governments in some cases.

The main central laws dealing with labor issues are given below: -

- Workmen's Compensation Act 1923
- Minimum Wages Act 1948
- Payment of Wages Act 1936
- Industrial Disputes Act 1947
- Employees Provident Fund and Miscellaneous Provisions Act 1952
- Payment of Bonus Act 1965 Payment of Gratuity Act 1972
- Maternity Benefit Act 1961
- Industrial Employment (Standing orders) Act 1946

Workmen's Compensation Act 1923

The Workmen's Compensation Act provides that compensation shall be provided to a workman for any injury suffered during the course of his employment or to his dependents in the case of his death. The Act provides for the rate at which compensation shall be paid to an employee.

Minimum Wages Act 1948

The Minimum Wages Act prescribes minimum wages for all employees in all establishments or working at home in certain employments specified in the schedule of the Act. Central and State Governments revise minimum wages specified in the schedule.

Payment of Wages Act 1936

The Payment of Wages Act regulates issues relating to time limits within which wages shall be distributed to employees and that no deductions other than those authorized by the law are made by the employers.

Industrial Disputes Act 1947

The Industrial Disputes act 1947 provides for the investigation and settlement of industrial disputes in an industrial establishment relating to lockouts, layoffs, retrenchment etc. It provides the machinery for the reconciliation and adjudication of disputes or differences between the employees and the employers. Industrial undertaking includes an undertaking carrying any business, trade, manufacture etc.

The Act lays down the conditions that shall be complied before the termination/retrenchment or layoff of a workman who has been in continuous service for not less than one year under an employer. The workman shall be given one month’s notice in writing, indicating the reasons for retrenchment and the period of the notice that has expired or the workman has been paid, in lieu of such notice, wages for the period of the notice. The workman shall also be paid compensation equivalent to 15 days’ average pay for each completed year of continuous service. A notice shall also be served on the appropriate government.

Employees Provident Fund and Miscellaneous Provisions Act 1952

This Act seeks to ensure the financial security of the employees in an establishment by providing for a system of compulsory savings. The Act provides for establishments of a contributory Provident Fund in which employees’ contribution shall be at least equal to the contribution payable by the employer. Minimum contribution by the employees shall be 10-12% of the wages. This amount is payable to the employee after retirement and could also be withdrawn partly for certain specified purposes.

Payment of Bonus Act 1965

The payment of Bonus Act provides for the payment of bonus to persons employed in certain establishments on the basis of profits or on the basis of production or productivity. The Act is applicable to establishments employing 20 or more persons. The minimum bonus, which an employer is required to pay even if he suffers losses during the accounting year is 8.33% of the salary.

Payment of Gratuity Act 1972

The Payment of Gratuity Act provides for a scheme for the payment of gratuity to all employees in all establishments employing ten or more employees to all types of workers. Gratuity is payable to an employee on his retirement/resignation at the rate of 15 days salary of the employee for each completed year of service subject to a maximum of Rs. 350,000.

Maternity Benefit Act 1961

The Maternity Benefit Act regulates the employment of the women in certain establishments for a prescribed period before and after child birth and provides certain other benefits. The Act does not apply to any factory or other establishment to which the Employees State Insurance Act 1948 is applicable. Every women employee who has actually worked in an establishment for a period of at least 80 days during the 12 months immediately proceeding the date of her expected delivery, is entitled to receive maternity benefits under the Act. The employer is thus required to pay maternity benefits and/or medical bonus and allow maternity leave and nursing breaks.

Industrial Employment (Standing orders) Act 1946

The Industrial Employment Act requires employers in industrial establishments to clearly define the conditions of employment by issuing standing orders duly certified. Model standing orders issued under the Act deal with classification of workmen, holidays, shifts, payment of wages, leaves, termination etc.

Policy on Foreign Direct Investment

India has among the most liberal and transparent policies on FDI among the emerging economies. FDI up to 100% is allowed under the automatic route in all activities/sectors except the following, which require prior approval of the Government:-

1. Sectors prohibited for FDI
2. Activities/items that require an industrial license
3. Proposals in which the foreign collaborator has an existing financial/technical collaboration in India in the same field
4. Proposals for acquisitions of shares in an existing Indian company in financial service sector and where Securities and Exchange Board of India (substantial acquisition of shares and takeovers) regulations, 1997 is attracted
5. All proposals falling outside notified sectoral policy/CAPS under sectors in which FDI is not permitted

Most of the sectors fall under the automatic route for FDI. In these sectors, investment could be made without approval of the central government. The sectors that are not in the automatic route, investment requires prior approval of the Central Government. The approval in granted by Foreign Investment Promotion Board (FIPB). In few sectors, FDI is not allowed.

After the grant of approval for FDI by FIPB or for the sectors falling under automatic route, FDI could take place after taking necessary regulatory approvals form the state governments and local authorities for construction of building, water, environmental clearance, etc.

Procedure under automatic route

FDI in sectors/activities to the extent permitted under automatic route does not require any prior approval either by the Government or RBI. The investors are only required to notify the Regional Office concerned of RBI within 30 days of receipt of inward remittances and file the required documents with that office within 30 days of issue of shares of foreign investors.

Procedure under Government Approval

FDI in activities not covered under the automatic route require prior government approval. Approvals of all such proposals including composite proposals involving foreign investment/foreign technical collaboration is granted on the recommendations of Foreign Investment Promotion Board (FIPB).

Application for all FDI cases, except Non-Resident Indian (NRI) investments and 100% Export Oriented Units (EOUs), should be submitted to the FIPB Unit, Department of Economic Affairs (DEA), Ministry of Finance.

Application for NRI and 100% EOU cases should be presented to SIA in Department of Industrial Policy and Promotion.

Application can be made in Form FC-IL. Plain paper applications carrying all relevant details are also accepted. No fee is payable. The guidelines for consideration of FDI proposals by the FIPB are at Annexure-III of the Manual for FDI.

Prohibited Sectors

The extant policy does not permit FDI in the following cases:

i. Gambling and betting
ii. Lottery Business
iii. Atomic Energy
iv. Retail Trading
v. Agricultural or plantation activities of Agriculture (excluding Floriculture, Horticulture, Development of Seeds, Animal Husbandry, Pisiculture and Cultivation of Vegetables, Mushrooms etc., under controlled conditions and services related to agro and allied sectors) and Plantations (other than Tea Plantations)

General permission of RBI under FEMA

Indian companies having foreign investment approval through FIPB route do no require any further clearance from RBI for receiving inward remittance and issue of shares to the foreign investors.

The companies are required to notify the concerned Regional Office of the RBI of receipt of inward remittances within 30 days of such receipt and within 30 days of issue of shares to the foreign investors or NRIs.

Incorporation of a Company

Incorporation of a company in India is governed by the Companies Act 1956. A company could be a private limited company or a public limited company.

A private limited company is one that through its Articles restricts the rights to transfer its shares, limits the number of its members to 50, prohibits any invitation to the public to subscribe for any shares in the company and prohibits any invitation or acceptance of deposits from other than its members.

A public company is a company, which is not a private company.

For registration and incorporation of a company, an application has been filed with Registrar of companies. Application for registration of a company accompanied by the selected names, memorandum of association and articles of association and other necessary documents is to be filed with the Registrar of companies of the State in which the company is proposed to incorporated. The documents required to be filed along with applications are as follows: -

A. Memorandum of Association
B. Articles of Association
C. The agreement, if any, which the company proposes to enter into with any individual for appointments as its managing or whole time director or manager
D. A copy of the letter of the Registrar of Companies intimating the availability of the proper time
E. Documents evidencing payment of prescribed registration and filling fee
F. Documents evidencing the directorship and situation of Registered Office inform 32 and Form 18 respectively and declaration of compliance with the requirements of Companies Act for giving consent to act as a director.

Upon compliance with all requirements, the Registrar will register the company and issue a certificate of incorporation of company that would bring the company into existence as a legal entity. Once the company has been duly registered and incorporated as an Indian company, it is subject to Indian laws and regulations as applicable to other domestic Indian companies.

Judiciary

India has a well-established and independent judiciary system. The Supreme Court of India in New Delhi is the highest Court of Appeal. Each State has a High Court along with subsidiary District Courts, which enforce the rule of law and ensure fundamental rights of citizens, guaranteed by the Constitution of India.

India has a three-tier court system with a typical Indian litigation starting from a District Courts and reaching its logical conclusion in the Supreme Court of India. The High Courts along with the various State level forums, situated mostly in the State capitals, constitute the middle rung of this three-tier system. District level courts are the courts of first instance in dispute resolution except in cases where they are prevented from being so by virtue of lack of pecuniary jurisdiction. Cases involving violation of fundamental rights are filed in respective High Court or Supreme Court.

A civil, criminal or commercial dispute may be filed in the court having territorial jurisdiction and depending upon level of crime or pecuniary jurisdiction. The place of cause of action and the place of residence of the defendant are the necessary determinants of territorial jurisdiction.

A number of special courts and tribunals have been constituted in India to deal with specific disputes: -

1. Various Tax Tribunals
2. Consumer Dispute Rederssal Forums
3. Insurance Regulatory Authority of India
4. Industrial Tribunals
5. Debts Recovery Tribunals
6. Company Law Board
7. Motor Accidents Claims Tribunals

An appeal can be filed against an order of the civil or criminal judge before the Court of District and Sessions Judge. Next appeal can be preferred before the High Court and after that to the Supreme Court.

Under Article 141 of the Constitution of India, every judgment delivered by the Supreme Court becomes the Law of the Land to be followed by all the other lower courts.

Dispute Resolution

The awards and decrees of the Indian courts are sacrosanct. However, Section 13 of the Code of Civil Procedure 1908 (CPC) lays down that a foreign judgment shall be conclusive as to any matter directly adjudicated upon between the same parties or between parties under whom they or any of them claim litigating under the same title except in few cases.

Section 44A of the CPC provides for execution of decrees passed by courts in a reciprocating territory. It lays down that where a certified copy of decree of any of the superior courts of any reciprocating territory has been filed in a District Court, the decree may be executed in India as it has been passed by the District Court. Government of India has notified Singapore, Malaysia, UK, New Zealand, Hong Kong and Fiji as reciprocating territories. For other countries, a foreign decree may be executed in India by filing a suit in the District Court on the basis of the said decree praying inter-alia, for the execution of the decree passed by the foreign court. In addition, the CPC provides for a summary procedure for faster recovery of a debt or liquidated money in demand under Order 37 of the CPC. In summary suit, defendant is not, as in an ordinary suit, entitled as of right to defend the suit.

Arbitration and Conciliation

Arbitration and Conciliation Act 1996 based on the UNCITRAL model law provides for resolution of a commercial dispute expeditiously for:

- International commercial arbitration, where the seat of arbitration is India and

- Enforcement of international commercial arbitration agreements and awards under the New York Convention and Geneva Convention where the seat of arbitration is outside India.

The Arbitration Act also provides for international commercial arbitration whether contractual or not, considered as commercial under Indian law and where at least one of the parties is a foreign national or incorporated in a foreign country.

New Dispute Resolution Opportunities offered by Investment Treaties

India has entered into bilateral investment treaties with a number of countries including Australia, France, Japan, Korea, UK, Germany, Russian Federation, The Netherlands, Malaysia, Denmark, OPIC of US. Each agreement makes provision for settlement of disputes between an investor of one contracting party and an investor of the other contracting party through negotiation, conciliation and arbitration.

India is a party to the Convention establishing the Multilateral Investment Guarantee Agency (MIGA), which provides for settlement of disputes between State parties to the Convention and MIGA through negotiation, conciliation and arbitration.

Under Indian Law, the following types of differences cannot be settled by arbitration, and therefore, must be settled only through civil suits: -

- Matters of public rights
- Proceedings under the Foreign Exchange Management Act (FEMA) which are quasi-criminal in nature
- Validity of intellectual property rights granted by statutory authorities
- Taxation matters beyond the will of the parties
- Winding up under the Companies Act, 1956
- Disputes involving insolvency proceedings

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