

**DOING  
BUSINESS  
IN**

**INDIA**



**Khimji Kunverji & Co.**

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## *Foreword*

"This booklet has been prepared for the use of clients, partners and staff of HLB International member firms. It is designed to give some general information to those contemplating doing business in India and is not intended to be a comprehensive document. You should consult us, therefore, before taking further action. The Indian Federation Firms and HLB International cannot be held liable for any action or business decision taken on the basis of information in this booklet.

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## *Preface*

This guide is designed to provide to an investor, particularly a foreign investor, only basic information on the present business and economic environment in India. The information covers areas like economic trends, taxation, accounting, finance, capital markets, employment and labour, besides other commercial and legal implications influencing business decisions in the country's changing economic scenario.

The information given is not exhaustive and is only meant to be a guide. This guide does not purport to be an offer, invitation or solicitation of any kind.

This book reflects information current at September 2007. We shall be happy to provide additional information.

## *General - An Introduction To India*

Welcome to an insight of an enigma that is India. In the world, India is the seventh largest country, with the second largest population having the third largest English speaking population and will shortly be the fourth largest economy. It is a land of immense opportunities.

India will never cease to amaze, whether in its people, its culture or in economic activity.

India is a land of diversity with a congruence of many disparate cultures that continue to coexist in balanced harmony. It enjoys the advantage of a civilization of more than 5000 years. It is a vibrant country that symbolizes continuity in change and change in continuity.

The country is a land of contrasts where tradition can coexist with development and where hope manages to flourish in despair.

The present economic and tourism scenario is aptly described in the words "INCREDIBLE INDIA".

# A Brief Overview of India

## GEOGRAPHY OF INDIA

Longitude	68°7' to 97°25'
Latitude	8°4' to 37°6' North
Land Mass details	Total land area 3,287,590 sq. kms. Coastline 7516 kms. Land frontier 15,200 kms.
Boundaries	North - China, Nepal, Bhutan and the mountain range of the Himalayas. East - Myanmar (Burma), Bangladesh and the Bay of Bengal. South - The Indian Ocean and Sri Lanka. North West - Pakistan, Afghanistan and the Arabian Sea
Climate	Winter Season from October to February, Summer Season from March to May, Monsoon from June to September.
Natural Resources	Coal (fourth-largest reserves in the world), iron ore, manganese, mica, bauxite, titanium ore, chromite, natural gas, diamonds, petroleum, limestone, arable land
Environment - international agreements	India is part of Antarctic-Environmental Protocol, Antarctic-Marine Living Resources, Antarctic Treaty, Biodiversity, Climate Change, Desertification, Endangered Species, Environmental Modification, Hazardous Wastes, Law of the Sea, Nuclear Test Ban, Ozone Layer Protection, Ship Pollution, Tropical Timber 83, Tropical Timber 94, Wetlands, Whaling

## CONSTITUTION AND GOVERNMENT

India is a sovereign, socialist, secular, democratic republic with a parliamentary system of Government. The Indian federation is the world's largest democracy with strong foundations having a single citizenship, an extremely active judiciary and a parliamentary form of democracy. India is a Union of States. There are 31 States and 7 Union Territories.

**Three main arms of the Indian Governance Structure are:**

### 1. *The Executive:*

The President of India is the Constitutional head of the Executive of the Union. The cabinet of ministers headed by the Prime Minister of the country is responsible for the day-to-day running of the country. Though the President does not interfere with the working of the Prime Minister and his cabinet he is an important guiding force

for the country. The Prime Minister and his cabinet are answerable to the bicameral Parliament of India, which is formed of the democratically elected representatives.

## **2. *The Legislature:***

The bicameral legislature is known as the parliament comprised of the Lok Sabha and the Rajya Sabha. The Lok Sabha members are elected by universal adult suffrage (right to vote) from all parts of India. The Rajya Sabha members are elected by the representatives of state legislatures and some nominated by the President of India on the basis of their contribution to society.

An independent body known as Election Commission oversees the election process to ensure free and fair elections at central and state levels. It is highly respected for its independence, efficiency and integrity.

## **3. *Local Governments:***

Many of the state legislatures are bicameral and have a similar structure as the main Parliament. The state governments have a similar authority structure to the national government and enjoy similar powers.

4. The constitution has demarcated the subject jurisdiction of the Central Parliament and the state legislatures; some subjects are concurrent.

## **LEGAL SYSTEM**

The legal system in India is well established. The Supreme Court of India is the apex court of the Nation headed by the Chief Justice of India. All States have a High Court as an apex court at State level. In addition, there are district courts, metropolitan courts, city civil courts, tribunals and criminal courts functioning in the States. Judgments of lower level courts can be petitioned in the higher level courts. The entire judiciary system is independent of the India Governance Structure and operates as per provisions laid down in the Constitution of India. The legal system of India is based on English Law.

For efficiency in disposal special Tribunals have been set up especially for economy matters such as direct and indirect tax, company law, competition act, modern arbitration and conciliation law is in place.

## **POPULATION**

India has a population of approximately 1.11 billion people (2007), comprising approximately one sixth of the world's

population. Although India occupies only 2.4% of the world's land area, it supports over 16% of the world's population. Currently, it is the second most populous nation on earth, though if current trends persist, India will replace the People's Republic of China, as the most populous nation in less than 40 Years.

It is a cultural mix of various races, religions, dialects, cultures, likes, dislikes and all the possible variations that one can expect.

India can be described as a young country with almost 64% of its population lying between the age group of 15-64 years. About 28% of the Indian population lives in urban areas.

India can boast of the largest pool of skilled and unskilled manpower, which is very versatile and adaptive. It has also got probably the largest pool of scientific qualified and technologically adapt manpower along with globally recognized innovators, managers, scientists and entrepreneurs in many fields. There also exists skilled and unskilled labour, which is not only cost effective and efficient but also capable of moulding itself to any requirements.

## **LANGUAGE SPOKEN**

The official language of the country is Hindi. However, English with various degrees of fluency is spoken and understood throughout the country.

## **TRAVEL TO INDIA**

India offers a multi-hued variety to its tourists. It's a country of holy shrines, beautiful beaches, snow-capped mountains, wildlife sanctuaries, Ayurveda massages and many interesting places to explore.

Some of the interesting tourist spots are Taj Mahal - one of the seven wonders of the world, at Agra, the famous erotic sculptures of Khajuraho, the Temples of South India, Beaches of Goa & Kerala, Kashmir - the Switzerland of India, Desert & Crafts of Rajasthan etc.

New Delhi is the capital of India. The other major cities are Mumbai, Chennai, Kolkata, Bangalore, Hyderabad and Ahmedabad.

International air connections are available from New Delhi, Mumbai, Chennai, Thiruvananthapuram, Bangalore, Hyderabad, Ahmedabad, Kochi, Kozhikode and Kolkata. Further, a number of international chartered air connections are also available from Goa. Most international airlines have regular

flights into the country, with Air India, Jet Airways & King Fisher (the national international carriers) offering flight connections to various international destinations.

For domestic air travel, there are a number of regular airlines – Indian, Jet Airways, and Kingfisher airlines as well as budget airlines for inexpensive air travel Air Deccan, Spice Jet, Paramount Airways etc. The country also has an extensive rail and road transport network.

## VISA ISSUE REGULATIONS

Foreigners desirous of visiting India can obtain a visa from the Indian Mission in the country of their residence. They should possess a valid National Passport - except in the case of nationals of Bhutan and Nepal, who may carry only suitable means of identification.

The Consular Passport and Visa Division of the Ministry of External Affairs is responsible for issuance of Indian visas to foreign nationals for visits for various purposes. This facility is granted through various Indian missions abroad.

The Indian High Commission / Embassy usually issues the visas in the applicant's country of residence with supporting documents.

India permits tourist visa, business visa, employment visa and few other visas. Please refer to “**Appendix A**” for details.

## PORTS

India is presently ranked in 17th position in the maritime nations of the world. About 95% by volume and 70% by value of the country's trade is carried on through maritime transport.

India has eleven major seaports: Kandla, Bombay, Nhava Sheva, Marmagao, New Mangalore, and Kochi (formerly known as Cochin) on the west coast, and Calcutta-Haldia, Paradip, Vishakhapatnam, Madras, and Tuticorin on the east coast. The eleven ports are the responsibility of the Ministry of State for Surface Transport but are managed by semi-independent port trusts overseen by boards appointed by the ministry from government departments, including the navy, port labour and industry, and ship owners and shipping companies.

In order of gross weight tonnage conveyed annually, Bombay, Vishakhapatnam, Madras, and Marmagao are the most important ports. In addition, there are some 185 minor and intermediate working ports.

## EMPLOYMENT REGULATIONS

There are various Acts, which regulate labour and employment in India. Some of the Acts are:

- Apprentices Act, 1961
- Bonded Labour System (Abolition) Act, 1976
- Child Labour (Prohibition & Regulation) Act, 1986
- Minimum Wages Act, 1948
- Payment of Bonus Act, 1965
- Payment of Gratuity Act, 1972
- Payment of Wages Act, 1936
- Contract Labour (Regulation & Abolition) Act, 1970
- Employees Provident Fund & Miscellaneous Provisions Act, 1952
- Employees' State Insurance Act, 1948
- Employers' Liability Act, 1938
- Factories Act, 1948
- Industrial Disputes Act, 1947
- Inter-State Migrant Workmen (Regulation of Employment and Condition of Service) Act, 1979.
- Pensions Act, 1871
- Trade Union Act, 1926
- Workmen's Compensation Act, 1923

## BANKING AND FINANCE

India provides a strong, well regulated banking, finance and capital markets. It supports new projects, expansions as well as acquisitions. The stock exchange allow companies to raise risk capital. It also has a supportive structure of venture capital and private equity funding.

The banking sector is segregated as public or private sector banks, cooperative banks, regional rural banks and foreign banks. With the advancement of technology, banking has become more easy, fast, accurate and also time saving. ATMs, Mobile Banking, SMS Banking and Net Banking is only the tip of an ice-berg.

Almost all the Indian Banks provide services to Non-Resident Indians (NRIs). There are different types of accounts for them. They are:

- Non-Resident (Ordinary) Account - NRO A/c
- Non-Resident (External) Rupee Account - NRE A/c
- Non-Resident (Foreign Currency) Account - FCNR A/c

## GENERAL LENDING POLICIES

Broadly, Banks and Financial Institutions in India grant loans for capital expenditure for setting up a new project or for expansion and diversification programmes of existing businesses. The finance is available for a fixed term ranging from one to seven years depending upon the project requirements. The rate of interest varies from seven to twelve percent depending upon the merits of each case.

The Banks also grant working capital facilities against current assets of

business entities. Non-fund based facilities in terms of letters of credit for procurement of raw materials and issuing payment and performance guarantees of business entities are also issued by the Banks.

There are industry specific lending institutions also for power generation, irrigation, railways, roads, shipping, hotels and tourism, films production, housing construction, etc. In addition, special financial institutions for the promotion of small industries, agriculture, etc provide soft finance to eligible business entities

## **CURRENCY**

The official currency of India is the "Indian rupee" commonly known as the INR. The rupee is fully convertible on the trade front under the liberalized exchange rate management system ("LERMS"). All transactions under the LERMS will take place at market-determined rates. The rupee is fully convertible on current account. On the capital account also the rupee is substantially free with residents permitted to invest abroad subject to completion of certain formalities and non-residents are permitted to invest in most sectors. In the international market the rupee is pegged to the US Dollar.

The Indian Rupee has appreciated

against the US Dollar over the past few years. The INR US\$ exchange rate, which stood at 48.80 on March, 31, 2002, is currently at around 39.50.

## **DOMESTIC MARKET**

India can boast of being the largest growing market in the world due to its fast growing middle class with increasing standards of living and growing aspirations. The middle class has a high saving and spending potential making India a large market for a variety of goods.

## *Our Vibrant Economy- Areas for Investment*

Presently, the economy of India is on the fast track of progress at all levels. Prime sectors like Agriculture, Industry, Services etc. are progressing at a rapid rate. All the engines of the economy are currently running at nearly full speed.

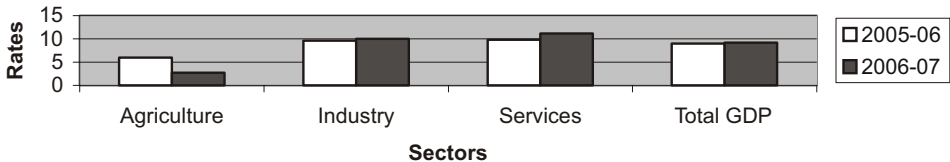
### **GROSS DOMESTIC PRODUCT**

As per the Economic Survey 2006-2007 tabled in the Parliament on 27th

February 2007, the robust & impressive performance of the Indian economy in 2006-2007 has exceeded expectations formed at the beginning of the year. As against the initial growth projection of 8%, the GDP growth in 2006-2007 is expected to be 9.2%. It is in fact exemplary that growth momentum has been maintained despite floods in five agro-major states and a two-year high level of inflation.

The economy is expected to maintain its growth tempo in the current year.

**Sectoral real growth rates in GDP (at factor cost) over  
Previous Year in %**



The average inflation in the 52 weeks ending on February 3, 2007 remained at 5 percent. Government has targeted to bring it down to 4% and is succeeding.

### **INDUSTRY**

India is one of the leading developing nations with a strong presence in all areas of business and commerce. The major growth drivers in the future where immense growth is possible are:

- IT Enabled Services
- Software Development

- Automobiles
- Power
- Infrastructure and Allied Industries
- Transport
- Hospitality
- Tourism Development
- Insurance
- Telecoms
- Back office operations
- Bio-technology, Fast Moving Health Goods (FMHG) and Pharmaceuticals
- Media & Entertainment
- Fast Moving Consumer Goods (FMCG) and Luxury Goods

- Manufacturing Hubs
- Retail Marketing and Sales
- Engineering and capital goods
- Textiles

The areas stated above are considered as the basis on which India can convert itself into economic superpower. The potential of these industries is unlimited due to the large Indian market and also due to India's immense influence in the South Asian economy.

The development of the three main sectors of the economy i.e. infrastructure, manufacturing and service sector, is enumerated below:

### **INFRASTRUCTURE**

The economy's growth rate has seen a surge in demand for increased capacities in roads, ports, airports, railways, power generation & transmission and in industrial infrastructure for the manufacturing and service sector. It is giving good returns to the investor.

### **MANUFACTURING**

Manufacturing recorded an impressive growth rate of 12.5 per cent during the year 2006-07. It also continued its growth rate in the new fiscal year 2007-08 by growing at a rate of 15.1 per cent during April as compared to the corresponding period in the last year. It is because of impressive growth in the industrial

sector, propelled by the robust growth in the manufacturing sector which continues the growth rate unabated. Overseas companies are investing more in India to take advantage of growing demand. Several MNCs like Sony, Samsung, Coca Cola, Nokia, Motorola, etc. which have got varied profiles are manufacturing in India.

### **SERVICE SECTOR**

It is another emerging area having a huge potential for expansion in a number of services. Some of the specific services having good scope for growth are:

#### *Information Technology (IT)*

The industry comprises software services, hardware and IT enabled services (ITES). IT and ITES services had shown an immense growth with a multi dynamic portfolio including Business Process Outsourcing (BPO) and Knowledge Process Outsourcing (KPO).

#### *Business Process Outsourcing (BPO)*

The sector in the past few years has witnessed considerable activity, including revamping up of operations by both the Indian and MNC players. BPO involves business process management and outsourcing. Business process management uses technology aimed at redesigning the process, reducing unnecessary steps, and bring efficiencies.

On the other hand, outsourcing uses the expertise and resources of dedicated outside service providers to perform many of these vital yet non-core activities

India is firmly established as the largest recipient of outsourcing contracts as well as FDI inflows into BPO activities from industry majors and MNCs as more and more countries are striving to become outsourcers and are succeeding. The BPO industry is mostly dominated by companies providing BPO services (45%), followed by software development (20%) and call centres (18%).

India is undoubtedly the most favoured BPO destination of the world for a variety of reasons, a few of which are listed below:

- Human Resource: India is home to large and skilled human resources. India has an inherent strength, which has made it a major success as an outsourcing destination.
- Language: Besides being technically sound, the work force is proficient in English
- Cost Effectiveness: Employee costs are lower in comparison to other developed countries of the world.

- Time Zone Differences: India also has a distinct advantage of being in a different time zone that gives it a flexibility in working hours.

### *Knowledge Process Outsourcing (KPO)*

KPO is one-step extension of Business Processing Outsourcing (BPO) as BPO Industry is grooming into Knowledge Process Outsourcing because of its favourable advantages and future scope. Knowledge process can be defined as a high added value process chain where the achievement of objectives is highly dependent on the skills, domain knowledge and experience of the people carrying out the activity.

Some of the general services provided by the KPOs are:

- Intellectual Property research,
- Equity financial and insurance research,
- Data search,
- Integration and management,
- Analytics (data analytics/risk analytics) and data mining services,
- Research and information services in human resources,
- Business and market research,
- Engineering and design services,
- Design, animation, and simulation services,
- Research and Development,
- Network management,
- Decision Support Systems.

India is amongst the most favoured destinations for KPO's as the benefits described in the BPO sector above hold good for the KPO sector too.

### ***Telecommunication***

India's rapidly growing telecom sector has seen much activity in last couple of years. FDI upto 49% under the automatic route and 74% subject to conditions is allowed for telecom services. In case of Internet services without gateway, and for telecom equipment-manufacturing industry, 100% is permitted.

The Department of Telecommunications (DOT), under the Ministry of Communications, is the administrative department for monitoring the telecom sector.

The total number of telecom subscribers is expected to reach 250 millions approximately by the end of year 2007.

### ***Tourism***

The Indian Tourism industry is one of the most important export industries of the country. Tourism yields substantial foreign exchanges for India. A large number of participants are contributing to the revenue of the industry. Segments such as hotels, tour operators, airlines, shipping etc., are significant contributors to this revenue.

### ***Retail and Distribution***

These are two fast emerging areas for organized large-scale activity from farms to the food table, with opportunities in the entire value chain.

## *Investment - Supportive Environment*

With globalization and the widening of the world economy, there is an immense potential for investment in India due to the following reasons:

- India is one of the largest economies in the world.
- Substantially a free market economy with government recognition of the need for further reforms.
- Availability of one of the largest pool of cost effective, skilled and qualified scientific and technical manpower.
- Large availability of educated manpower of around 360 million, which is more than the population of many countries.
- Vibrant capital markets and strong financial sectors along with a large and penetrative network of banks and financial institutions.
- Latest state of the art infrastructure facilities with governmental recognition of the need for greater improvement.
- Growing middle class with increasing aspirations.
- A vast untapped market waiting to be tapped. Approximately 1% of the Indian population would mean more than 10 million consumers, which is more than the combined population of Singapore and Hong Kong.

- Recognized educational institutions, which are the providers of many top industry professionals in the world and also a source of manpower for potential investors.
- India has a high savings rate leading to greater capital flow and therefore higher investment.
- Indian Governments' recognition about fiscal discipline and awareness of the need for prudent financial policies and curbing of subsidies over the long run.

### **FOREIGN DIRECT INVESTMENT**

Foreign Direct Investment (FDI) is permitted under the following forms of investments:

- Through financial collaborations.
- Through joint ventures and technical collaborations.
- Through capital markets via Euro issues.
- Through private placements or preferential allotments.

### *Sectors prohibited for FDI*

- i. Retail trading (except Single Brand Product retailing)
- ii. Atomic energy
- iii. Lottery business
- iv. Gambling and Betting
- v. Housing and Real Estate Business (only NRIs are allowed to invest)

vi. Coal & Lignite Mining (allowed only for captive purposes but for large size projects - no prohibition)

### *Automatic Route*

In order to further improve the investment climate, a major rationalization of the FDI policy and associated procedures was recently undertaken by Ministry of Commerce and Industry.

As per the extant policy, FDI up to 100% is allowed, under the automatic route, in most sectors/activities. FDI under the automatic route does not require prior approval either by the Government of India or the Reserve Bank of India (RBI). Investors are only required to notify the relevant Regional office of RBI within 30 days of receipt of inward remittances and file required documents with that office within 30 days of issue of shares to foreign investors.

Automatic route allowed in almost all sectors except:

- Where more than 24% foreign equity is proposed to be inducted for the manufacture of items reserved for the Small Scale Sector.
- Proposals in which a foreign collaborator has a previous venture/tie up with India, where the consent of a partner is required.

- Where shares are being issued for acquiring existing shares of another Indian company.
- Proposals falling outside notified sectoral policy/caps.

### *Approval Route-FIPB*

FDI in activities not covered under the automatic route requires prior Government approval and is considered by the Foreign Investment Promotion Board (FIPB), Ministry of Finance.

Indian companies having foreign investment approval through FIPB route do not require any further clearance from RBI for receiving inward remittance and issue of shares to the foreign investors. Again, 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.

### *Processing of non-automatic approval cases*

The Foreign Investment Promotion Board (FIPB) approves all other cases where the parameters of automatic approval are not met. Normal processing time is 4 to 6 weeks. Its approach is liberal for all sectors and all types of proposals, and rejections are few. It is not necessary for foreign investors to have a local

partner, even when the foreign investor wishes to hold less than the entire equity of the company. The portion of the equity not proposed to be held by the foreign investor can be offered to the public.

The Foreign Investment Promotion Board (FIPB) has been constituted by the Government with a view to promote and attract foreign investment in India. The FIPB is a high powered committee comprising the Principal Secretary to the Prime Minister (Chairman), Finance Secretary and Commerce Secretary, and is located at the Ministry of Industry.

The Sectorwise list for Automatic Approval and FIPB approval is appended as “**Appendix-B**”.

### *Foreign Investment through GDRs*

Indian companies are allowed to raise equity capital in the international market through the issue of Global Depository Receipts (GDRs). GDRs are designated in dollars and are not subject to any ceilings on investment. An applicant company seeking Government's approval in this regard should have a consistent track record of good performance (financial or otherwise) for a minimum period of 3 years. This condition would be relaxed for infrastructure projects such as power generation, telecommunications, petroleum exploration and refining, ports, airports and roads.

## **CAPITAL MARKETS**

India has by the virtue of its size probably one of the largest investor bases in the world. The Bombay Stock exchange is one of the oldest stock exchanges in Asia. There are 23 recognized stock exchanges in India. However predominant business is done at the Bombay Stock Exchange (BSE) and National Stock Exchange (NSE). All the stock exchanges have screened based computerized trading with satellite up-linking facilities from any part in India. The exchanges now have trading of all securities in electronic units known as dematerialized shares.

The BSE and the NSE have also introduced derivative products like Futures and Options with a view of bringing the Indian stock markets in tune with international markets and practices.

## **MUTUAL FUNDS**

In India, Mutual Funds are governed by the Securities and Exchange Board of India (SEBI) regulations. Foreign Participation in Mutual Funds and Asset Management Companies are governed by SEBI. All companies who wish to provide services of a mutual fund are also required to be members of Association of Mutual Funds of India.

## VENTURE CAPITAL FUNDS AND COMPANIES

Venture Capital funding is also considered as an option for funding business. It has gained momentum after the Information Technology boom where it gained popularity as a means of funding. In India, these funds are governed by SEBI guidelines. There are a number of funds, which are currently operational in India and involved in funding start up ventures. Many of the venture funds are involved in providing mezzanine or bridge financing and are better known as private equity players. The venture capital companies also provide entrepreneurs with incubator facilities with innovative ideas.

The Indian Venture Capital Agency (IVCA) is the nodal centre for all venture capital activities in the country. The

association was set up in 1992 and over the last few years it has developed an impressive database.

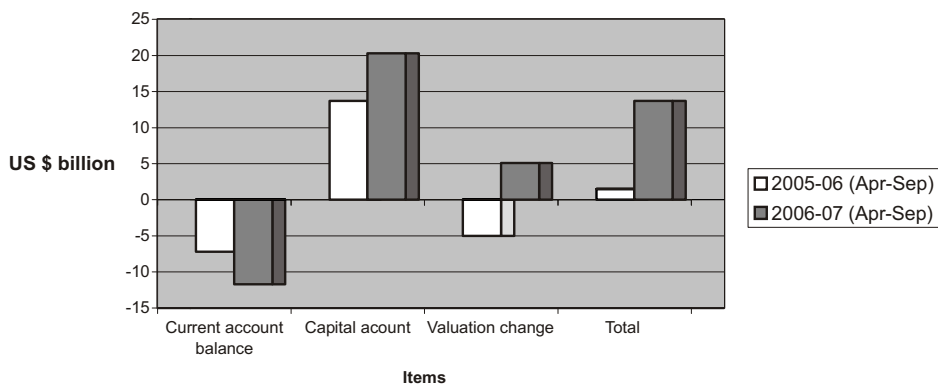
## FOREIGN EXCHANGE MARKET

The money market in India is structured and well developed. The major players in the money market are the Authorized dealers, Nationalized banks (mainly State Bank Of India) and foreign banks that work under the active and regulatory control of the Reserve Bank of India.

With the economic liberalization, the Govt. of India has opened the doors for attracting foreign exchange to the Country. The provisions of Foreign Exchange Management Act, govern foreign exchange in India.

Foreign Exchange reserves continue to show an impressive growth.

**Sources of accretion to foreign exchange reserve**



## FOREIGN EXCHANGE

The Reserve Bank of India (RBI) is the governing authority for all matters relating to foreign exchange management and control. RBI manages through stipulations in the Foreign Exchange Management Act (FEMA) to supervise, control and flourish foreign funds.

# ***Business Organisations- Law and Formats***

## **LEGAL ENTITY FOR INDIAN OPERATIONS**

A foreign company has to make a choice as to its legal entity for carrying out business activities in India. The choice of legal entity will largely depend on the type of business operations in India. It is quite possible that a foreign company may do business in India without physically carrying out any activities in India. An example of such activity could be the export of goods and services to India. However, in most of the cases, when a foreign company decides to do business in India, it is generally not possible to totally abstain from activities in India. As a general guideline, a foreign company may do business in India in any one of the following manners while retaining its legal status as a foreign company:

- (i) As a foreign company without carrying out any business activity within Indian boundaries;
- (ii) Through a liaison office in India;
- (iii) Through a project office in India; and
- (iv) Through a branch office in India.

A foreign company, depending upon its nature of business activities in India, may also operate through an Indian company in any of the following manners:

- (i) As an Indian company with 100% share holding held by the foreign company. Such a company is called 100% subsidiary of the foreign company.
- (ii) As an Indian company in joint venture with one or more Indian and foreign partners.

## **FOREIGN COMPANY**

A Foreign Company is a company, which is incorporated outside India. Such companies, for conducting business in India, have to comply with the following formalities:

- (a) Compliance with the Indian Companies Act, 1956.
- (b) Compliance with the Reserve Bank of India's rules and regulations.

### ***Compliance with the Companies Act***

Sections 591 to 602 of the Companies Act contain provisions relating to foreign companies. As per section 592, foreign companies are required to file certain documents with the Registrar of Companies. The list of the documents to be filed is given in section 591. Foreign companies which establish a place of business in India shall, within 30 days of the establishment of the place of business, file with the Registrar of Companies the following documents:-

- Certified copy of the Charter or Memorandum and Articles of Association of the company and if the instrument is not in the English language, a certified translation thereof in English.
- Full address of the registered office or principal office of the company abroad.
- List of Directors and Secretary of the company.
- The name and address of one or more persons resident in India who is or are authorized to accept, on behalf of the company, service of any notice served on the company.
- The full address of the office of the company in India which is its place of business.

The above documents are required to be delivered to the Registrar of Companies, New Delhi and also to the Registrar of the State in which the principal place of business of the foreign company is situated along with the prescribed form.

Further, such a foreign company is required to submit its Indian business accounts and world accounts to the prescribed authorities. The Balance Sheet and Profit & Loss Account for Indian operations are to be compiled separately and independently as per the

requirements of Schedule VI of the Companies Act. For the purposes of maintaining Indian accounts, a foreign company is required to keep at its principal place of business in India such books of accounts which relate to:-

- Money received or expended;
- Sales and purchases made; and
- Assets and liabilities.

However, where the foreign company has only liaison office(s) in India and is not engaged in any trading, manufacturing or other commercial activity in India, such a company should submit a certificate that the company did not carry out any trading activities.

### *Compliance with Reserve Bank of India's Formalities*

The Foreign Exchange Regulation Act, 1973 ["FERA"] governed the business carried on in India by the foreign companies and foreign nationals. However, w.e.f. 1st, June 2000 FERA has been replaced by Foreign Exchange Management Act, 1999 (FEMA). A foreign company has to comply with various rules and regulations as prescribed in FEMA.

### *Liaison Office in India or Representative in India:*

Foreign companies intending to set up a liaison office in India or to post a

representative in India for undertaking liaison activities are required to obtain approval from Reserve Bank of India. The RBI normally grants approval for liaison activities initially for a period of three years. The application is to be submitted to the Central Office of Reserve Bank (Foreign Investment Division).

It may be noted that when a foreign company undertakes liaison activities in India, whether through a liaison office or through a representative, the permission from the Reserve Bank is granted on the condition that the expenses of the liaison/representative office are to be met exclusively out of foreign exchange to be remitted from a foreign country to India. The Reserve Bank also requires submission of annual accounts.

***List of the activities which may be undertaken by the Liaison office in India:***

- Representing in India the parent company/group companies.
- Promoting export import from/to India.
- Promoting technical/financial collaborations between parent/group companies and companies in India.
- Acting as a communication channel between the parent company and Indian companies.

***Appointment as an Agent in India:***

Foreign companies and foreign nationals are required to obtain RBI's permission for their appointment as agents in India. For the purposes of RBI regulations, the term 'agent' includes any person or company (including its branch) buying goods with a view of selling them before any processing thereof. It may also be mentioned that there are altogether different regulations for foreign nationals of Indian origin permanently resident in India.

***Project Office in India:***

A foreign company may open a project office/s in India provided it has secured from an Indian company, a contract to execute a project in India. RBI has now granted general permission to foreign entities to establish Project Offices subject to specified conditions. Project Offices may remit outside India the surplus of the project on its completion, general permission for which has been granted by the RBI.

***Branch Office in India:***

Foreign companies can establish a branch office or other place of business for their activities of a trading, commercial or industrial nature. They are required to obtain permission of Reserve Bank to carry on such activities,

for which an application to Reserve Bank should be made.

There are separate regulations for foreign nationals of Indian origin permanently resident in India.

*List of the activities which may be undertaken by the branch office in India:*

- Export/Import of goods.
- Rendering professional or consultancy services.
- Carrying out research work, in which the parent company is engaged.
- Promoting technical or financial collaborations between Indian companies and parent or overseas group company.
- Representing the parent company in India and acting as buying/selling agent in India.
- Rendering services in Information Technology and development of software in India.
- Rendering technical support to the products supplied by parent/group companies.
- Foreign airline/shipping company.

A branch office is not allowed to carry out manufacturing activities on its own but is permitted to subcontract these to an Indian manufacturer. Branch Offices established with the approval of RBI, may remit outside India the profit of the branch, net of applicable Indian taxes and subject to RBI guidelines Permission

for setting up branch offices is granted by the Reserve Bank of India (RBI).

## **INDIAN COMPANY**

A foreign company, depending upon its nature of business activities in India may also operate through an Indian company in any of the following manners:-

- as a joint venture with Indian partner
- as a wholly owned subsidiary

A foreign company can operate in India through an Indian company the shares of which may be partly held by the foreign company and partly by Indian partners. The incorporation of the Indian company shall be governed by the Indian Companies Act, 1956.

Incorporation of a company in India requires filing of certain documents with the Registrar of Companies including the Articles and the Memorandum of Association of the company along with the prescribed fees. The formalities relating to incorporation are rather simple requiring in all six to ten weeks time when a company can start its commercial operations.

The Indian companies can be primarily divided into two categories:

- (i) Private Limited Company
- (ii) Public Limited Company.

A private company means a company having a minimum paid up capital of Rs. 0.1 million or such higher paid up capital as may be prescribed. The private limited company is a company which by its articles of association

- Restricts the right of its members to transfer shares;
- Limits the number of its members to fifty;
- Prohibits any invitation to the public to subscribe to its shares and debentures.
- Prohibits any invitation or acceptance of deposits from persons other than its members, directors or their relatives.

However, a public limited company does not have any such restrictions. Such a company can be quoted on stock exchanges in India and abroad. The company can also invite public to subscribe to its shares and can also raise loan by issue of debentures. The financial institutions also generally prefer to deal with a public limited company. Therefore, from foreigners' point of view, formation of a public limited company is a more appropriate form to carry out business activities in India.

These companies can be limited by share capital or guarantee

### *Capital of a Limited Liability Company*

The minimum paid-up capital of a Public Company must be at least Rs. 0.5 million and that of a Private Company must be at least Rs. 0.1 million. Of the authorized share capital not all needs be paid in immediately. Shares may be partly paid. The authorized share capital may be increased by a simple resolution passed at the company's general meeting, if the articles of association so provide.

A limited company can issue only two kinds of shares, equity shares and preference shares, provided they form part of the authorized share capital of the company. Every member holding equity shares has a right to vote in respect of the capital held on every resolution placed before the company. Every member holding a preference share has a preferential right to be paid a fixed amount or rate of dividend; a preferential right, on winding up or repayment of capital, to be repaid the amount of capital paid up on his shares; right to vote only on resolutions which directly affect the rights attached to preference shares.

Shares are now permitted to be held in an electronic form through the depository mode.

### *Procedure for formation of a Company:*

The procedure for setting up a limited liability company whether public or private, which is normally entrusted to professional advisors, can be summarized as follows:

- At least two promoter subscribers in case of a private company and at least seven in the case of a public company must apply for availability of a suitable name.
- The proposed name must be approved by the Registrar of Companies.
- Two principal constitution documents of the company must be drawn up:
  - (a) Memorandum of Association, which states the company's name, the situation of its legal address or registered office (which must be in India), the objects of the company, its limited liability status and the amount of its authorized capital.
  - (b) Articles of Association, which regulates the company's internal management and the rights of its members among themselves.
- The promoter subscribers must sign two printed copies of the memorandum and the articles of association, in presence of a witness.
- In the case of a public company, a declaration by persons agreeing to act as directors must be obtained.

- The two signed copies of the memorandum and articles of association, one of which is duly stamped, the declaration (if required) and other specified documents, along with the registration fees prescribed, are presented to the Registrar of Companies for registration. On issue of its certificate of incorporation by the Registrar of Companies, the company comes legally into existence from that date.
- A private company may commence business as soon as a certificate of incorporation is issued. A public company, however, may not start operations until the Registrar of Companies, on completion of further formalities, has issued a certificate of entitlement to commence business.
- At any point of time, a private company must have at least two shareholders and a public company at least seven.

### *Cost of forming a Company*

For the formation of a company other than the usual costs involved in research and development, documentation, stamp duty etc., costs have to be incurred for registration fees with the ROC. The amount of duty and the registration fees depends on the authorized capital of the company.

## *Management of a Limited Liability Company*

The management of a company is vested in the board of directors, appointed by the shareholders, all of whom must be individuals. Directors need not be resident and can also be foreign nationals.

The minimum number of directors in a public company is 3 and in a private company 2. As to the maximum number of directors, if a public company proposes to increase the number of its directors by more than 12, approval of the Central Government is required.

The subscribers to the memorandum are deemed to be the first directors of the company. The shareholders in a General Body Meeting normally appoint subsequent directors.

A company may appoint one or more managing or full time directors. The appointment and remuneration of a managing or full time director of a public company is required to be approved by the shareholders in their General Body Meeting. Approval of the Government is not necessary if the appointee meets specified conditions and the remuneration is within the limits prescribed under the Companies Act.

Directors' remuneration is normally determined by the articles of association or by the shareholders at a General Body Meeting. A provision is made for minimum remuneration based upon the effective capital of the company, in case there is no profit or profit is inadequate. Unless the Central Government approves otherwise, the remuneration paid to the managing and full time directors of a public company may not exceed 5% of net profits if there is one such director, and 10% if there are more than one such director.

The articles of a private limited company can give power to its board of directors to fix the remuneration of a managing or full time director.

## *Meetings and Votes in a Limited Liability Company*

An Annual General Meeting must be held in each calendar year, not more than fifteen months after the preceding meeting and within six months from close of each accounting period. The Annual General Meeting is required to be held during business hours on a working day at a place within the city in which the registered office of the company is situated. Shareholders are entitled to appoint proxies to attend meetings and vote on their behalf.

Ordinary resolutions require a simple majority of the votes that are cast by those attending the meeting (in person or by proxy). A company's articles of association can be amended only by a 'Special Resolution' which is passed by a 75% or greater majority of the votes cast at a general meeting of which due notice has been given. Usually, each shareholder has one vote by a show of hands. On a poll, voting rights are in proportion to each shareholder's share of the paid up capital.

A formal meeting of the Board of Directors is required to be held once in every three months. These meetings need not be necessarily held in a place within the city of the registered office of the company, and can be held anywhere even outside India.

### ***Publication of Information by a Limited Liability Company***

In addition to its constitution documents, every limited company must file its annual financial statements with the Registrar of Companies and an 'Annual Return' containing updated particulars of its shareholders, directors and share capital. Information filed with the Registrar of Companies is available to the public for inspection on payment of a nominal fee.

Public companies listed on the stock exchanges are required to publish their quarterly results in a local and National newspaper.

A limited company must state its name and registered office address in legible characters in its business letters, bill heads, notices and other official publications; and its name on all communications including invoices, receipts, cheques and endorsements.

### ***Corporate Governance***

The Government of India has introduced good Corporate Governance (CG) leading to more transparent, ethical and fair business practices to be adopted by corporate entities at large. Certain important features of CG are as under:

The Report of the Board of Directors shall now include a Directors' Responsibility Statement confirming (i) maintenance of adequate accounting records for safeguarding the assets of the company and for preventing and detecting frauds and other irregularities (ii) judgments and estimates made in a reasonable and prudent manner to ensure true and fair view of the accounts (iii) preparation of accounts by following the applicable accounting standards (iv) consistent application of the accounting policies selected, and (v) preparation of financial statements on a going concern basis.

It is further provided that every public company having paid up capital of Rs. Fifty million or more shall constitute a committee of the Board known as the Audit Committee. Such a committee shall have full access to the information contained in the records of the company and shall also have powers to seek external professional advice. All the recommendations of the Committee relating to financial management and audit reporting shall be binding on the Board. Recommendations not acceptable to the Board are to be communicated to the Shareholders with reasons thereof.

The Companies Act now debars a person from acting as a Director of a company if there is a default in filing Annual Return / Accounts or repayment of deposits / interest or dividends.

Apart from the above requirements, all listed companies are now required to publish their quarterly and half yearly results with a limited review by the Auditors. Such accounts shall be prepared in compliance with the applicable accounting standards and shall also disclose segmental results. With the annual report, all listed companies have to publish audited consolidated accounts also.

Listed companies are also required to include a report on CG in their annual report covering certain vital information. Some elements of the important information are listed below:

- A brief statement on company's philosophy on code of governance.
- Composition and category of directors, their attendance at the Board Meeting etc.
- Audit committee, Remuneration committee and Shareholders committee details.
- Certain important disclosure by the Board.
- Means of communication with the company.
- General shareholders information.

### *Accounting Systems and Standards and Audit Committee*

India has a well established system of accounting. All corporate entities follow the mercantile (accrual) system for recording their accounting transactions. The Institute of Chartered Accountants of India, the Accounting regulatory authority, has prescribed Accounting Standards and Auditing and Assurance Standards providing comprehensive guidelines. These are mandatory applicable mainly to listed companies. Some of the Accounting Standards are applicable to private limited companies and non-corporate entities.

India is also a member of International Accounting Standards Board and whenever the international body prescribes new accounting standards, these are adopted in India also with modifications to suit the Indian environment and laws.

### *Joint Venture Company*

A joint venture company in India is like any other Indian company for the purposes of Indian Companies Act, Indian Income-tax Act and other applicable laws, rules and regulations. The formalities relating to incorporation of an Indian company have already been discussed in preceding paragraphs. A foreign company participating in a Joint Venture may need the permission from the Reserve Bank of India (RBI) or Foreign Investment Promotion Board (FIPB) depending upon the nature of the industry vis a vis the quantum of the investment as already explained in earlier section of Foreign Direct Investment.

### *Wholly Owned Subsidiary*

A foreign company may also operate in India by incorporating a company in India whose 100% shares are held by a foreign company. Such a company is known as a wholly owned subsidiary.

## **OTHER LEGAL ENTITIES:**

Partnership: Partnership is created by an agreement between the partners, which is called the Partnership Deed. The Indian Partnership Act governs the partnerships.

Cooperatives: Government encourages cooperatives in certain sectors like retailing of goods for mass consumption and certain agro industries.

Trusts: Trusts are usually created in India for charitable or religious purposes.

# Taxation

The tax system in India aims at achieving economic growth by encouraging investments in the desired channels. Though there are attractive tax incentives for foreign investment in India, domestic industry and trade also enjoys numerous tax concessions. Likewise the service sector particularly the export of services is entitled to number of tax incentives.

Preferred categories where these tax incentives are made available can broadly be classified into 3 categories as below:

- Priority sector, which includes infrastructure, power, tourism etc.
- Set up in certain preferred locations.
- Export of goods and services.

These incentives are dealt in detail under the head of “Tax Concessions” and “Some lucrative areas for investment”

The levy of tax in India is broadly divided into Direct and Indirect Taxes and the same is divided amongst Central & the State Governments as per the Constitution.

Direct Taxes include levies such as Income Tax, Wealth Tax, and Fringe Benefit Tax etc., which come within the purview of Central Government.

The Income Tax Act, 1961 (IT Act) is the operative (main) Act in India providing the machinery and methodology for the determination, computation and payment of income tax. The IT Act is substantiated by the Income Tax Rules providing methodology, rules and forms for payment of taxes. The Central Board of Direct Taxes (CBDT) is the final Authority and governs the entire mechanism of direct taxes in India. Indirect taxes on the other hand are handled either by the Central or State Governments. Customs Duty, Excise Duty & Service tax being the prime drivers of nation's growth are under direct control of the Central Government, the final authority being Central Board of Excise and Customs (CBEC). The States enjoy the power to levy taxes like professional tax and state sales tax, now popularly known as VAT and other local taxes like octroi etc.

## General Structure

The general structure of taxes in India is comprised of two parts:

Direct Taxes	Indirect Taxes
Income Tax	Excise Duty
Wealth Tax	Value Added Tax / Sales Tax
Fringe Benefit Tax	Customs Duty
	Stamp Duty
	Service Tax
	Octroi Duty

## DIRECT TAXES - INCOME TAX

### *Terminology*

#### a) Assessment

In general context the word assessment means computation of tax and procedure for imposing tax liability. An assessment, therefore, comprises of two stages:

- Computation of total income
- Determination of tax payable thereon

#### b) Assessment year

An assessment year is the year in which the income of the previous year is to be assessed and brought to tax and means the period of twelve months commencing on the 1st day of April every year.

#### c) Previous Year

The financial year immediately preceding the assessment year, in which the income is earned and brought to tax, is the previous year.

#### d) Assessee

An assessee is a person by whom any tax or any other sum of money is payable; or in respect of whom any proceeding has been taken for the assessment of his / its' income or loss; or of the income or loss of any other person in respect of which he / it is assessable; or any amount of refund

is due to him / it or to such other person under the IT Act.

#### e) Categories of Assessee

The Income Tax Act recognizes seven categories of persons chargeable to tax:

- Individuals,
- Hindu Undivided Families (HUF),
- Companies,
- Firms,
- Association of persons (AOP) or Body of individuals (BOI),
- Local Authorities,
- Artificial juridical persons not falling within any of the preceding categories.

### *Residence*

Under the Income Tax Act, the incidence of tax on a taxpayer depends on his residential status.

Assessee's are divided into the following three categories:

- Resident in India,
- Resident but not an ordinary resident,
- Non-resident in India.

### *Residential Status and Basis of Charge*

The residential status of individual taxpayer primarily depends upon the period of stay in India and in case of others, on the location of control and management of their business in India.

## Individual

Conditions for being Resident are as under:

Category	Days for which he should be in India in the previous year	Days for which he should be in India, during 4 years preceding the previous year
Indian citizen leaving India during the previous year as member of crew of an Indian ship or for employment outside India	182 days or more	Not applicable
Indian citizen or person of Indian origin who being outside India, comes on a visit to India during the previous year.	182 days or more	Not applicable
Any other individual –		
(1) Either Case 1; or	182 days or more	Not applicable
(2) Case 2:	60 days or more	365 days or more

Conditions for being a 'Resident and Ordinarily Resident':

1. Should be 'a resident' in India in at least 2 out of 10 previous years preceding the relevant previous year; and
2. Should be in India for 730 days or more during 7 previous years preceding the relevant previous year.

### *Firm/Association of Persons*

If control and management is situated wholly outside India, it is non-resident otherwise resident.

### *Company*

If the control and management is situated wholly in India, it is resident, otherwise non-resident. An Indian Company is always a resident. Companies are further classified into two categories viz. Domestic and Foreign Company. Domestic company means an Indian company or any other company, which has made prescribed arrangements for the declaration and payment of dividend within India. Foreign company means a company, which is not a domestic company.

## *Basis of Charge*

<b>Time &amp; place of Accrual/ Receipt of income</b>	<b>Resident &amp; Ordinarily Resident</b>	<b>Resident &amp; Not Ordinarily Resident</b>	<b>Non-Resident</b>
Received in India by him or on his behalf	Y	Y	Y
Deemed to be received in India by him or on his behalf	Y	Y	Y
Accrues or arises to him in India	Y	Y	Y
Deemed to accrue or arise to him in India	Y	Y	Y
Accrues/ arises & received outside India from business controlled or profession set up in India	Y	Y	N
Accrues/ arises & received outside India from business controlled or profession set up outside India	Y	N	N

## *Heads of Income*

The income liable to tax is to be computed under the following heads:

- Income from Salaries.
- Income from House Property.
- Profits and Gains from Business and Profession.
- Capital Gains.
- Income from Other Sources.

## *Rates of Tax*

Individuals, Hindu Undivided Families and Body of Individuals:

<b>Total Income Slab</b>	<b>Rate of Tax (A.Y. 2009-10)</b>	<b>Education Cess (EC)</b>	<b>Secondary and Higher Education Cess</b>
Up to Rs 150, 000*	Nil	Nil	Nil
Rs 150, 001 - Rs 250, 000	10%	2%	1%
Rs 250, 001 - Rs 5,00,000	20%	2%	1%
Rs 5,00,000 above	30%	2%	1%

There is a surcharge of 10 % of tax on income exceeding Rs. 1,000,000 (One Million)

{\*Rs. 185,000 in case of a woman, resident in India, Rs. 225,000 in case of an individual resident in India who is 65 years of age or above.}

## Others

Category	Rate of Tax(A.Y. 2009-10)	Surcharge(SC)	Education Cess & Secondary and Higher Education cess
Partnership Firms(having income below 10 million)	30%	Nil	3%
Having income above 1 crore	30%	10%	3%
Domestic Company(having income below 10 million)	30%	Nil	3%
Having income above 10 million	30%	10%	3%
Foreign Company(having income below 10 million)	40%	Nil	3%
Having income above 10 million	40%	2.50%	3%

A.Y.- Assessment Year

Note: A surcharge is applicable in cases where the total income exceeds Rs. 10,000,000 (Ten Millions)

(Above rates are updated as per Finance Act, 2008)

### ***Dividend Income***

Dividend (other than a deemed dividend explained below) declared by a domestic company is exempt in the hands of the recipient, but is taxed in the hands of the dividend distributing company @ 16.995% (applicable from AY 2009-10).

### ***Deemed Dividend***

Under section 2(22)(e) of the Income Tax Act, any loan or advance made by a company in which the public is not substantially interested in India to a shareholder holding 10% or more of the voting powers of the company or to any person in which such a shareholder is substantially interested or any payments made by any such company on behalf of or for the individual benefit of such a

shareholder is deemed to be a dividend in the hands of the recipient, taxable in the hands of the shareholder and not liable to tax in the company.

### ***Capital Gains Tax***

Capital gains arising from the sale of capital assets are classified into two categories viz:

- Short term capital gains; and
- Long term capital gains.

Short term capital gains means any gains arising from transfer of capital assets which are held for a period of not more than 36 months (12 months in case of shares held in a company, other securities listed on a recognized stock exchange in India or a unit of a mutual

fund registered in India, units of UTI, zero coupon bonds). Such short term capital gains are taxable at the normal tax rates applicable to each category of taxable persons.

Long term capital gains are capital gains other than short term capital gains. Such long term capital gains are taxable at special rate of 20% (plus applicable SC & EC @3%). In computing the capital gains, the cost of acquisition of the capital asset is indexed as per the cost inflation index of India.

Exemptions from capital gains tax are available in certain cases if such capital gains or sales proceeds from the capital assets are reinvested in some other specified capital assets.

#### ***Capital gains on securities purchased in Indian Currency:***

In the case of equity shares and equity oriented units of mutual fund, which are sold on recognized stock exchanges in India and on which securities transaction taxes have been charged, short term capital gains are taxable at special rate of 15% (plus applicable SC & EC @3%) from A.Y. 2009-10. (Updated as per Finance Act, 2008).

If such shares and funds are held for long term i.e. for 12 months or more capital gains are entirely exempt from tax.

There are separate provisions for non-residents acquiring shares and other securities in the foreign currency. These provisions relate to mode of computation of capital gains.

#### ***Special Rates For Non-Resident Companies***

##### Royalty or Fees from Technical Services:

Non-resident corporations are taxed in the following manner:

Received from the government or from Indian corporations under agreements that are approved by the government or which are in accordance with the Industrial Policy (refer notes 1 and 2)	
In pursuance of agreements made after May 31, 1997 but before June 1, 2005	Taxable at 20% on a gross basis
In pursuance of agreements made on or after June 1, 2005	Taxable at 10% on a gross basis

**The above rates may be subject to more beneficial provisions contained in a tax treaty entered into between India and the country in which the taxpayer is resident. Hence, countries like Mauritius, Singapore, Dubai etc. become very important to inbound investment due to favourable tax treaties with India.**

## Notes:

1. Royalties and fees for technical services earned in pursuance of agreements made after March 31, 2003 which are effectively connected with the foreign corporation's Permanent Indian Establishment are taxed at the rate of 40% (plus surcharge and education cess) on a net income basis.

2. Royalties and fees for technical services (not effectively connected with the foreign corporation's Indian Permanent Establishment) that are not received from the government or where received from Indian corporations under agreements not approved by the government or which are not in accordance with the industrial policy are also taxed at the rate of 40% (exclusive of surcharge and education cess) on a net income basis.

All the tax rates mentioned above, excluding the rates prescribed under the relevant treaty, must be enhanced by a surcharge of 2.5%. Further, the tax payable by all the corporations should be enhanced by an education cess at the rate of 3% on the tax payable inclusive of surcharge.

## *Interest on Foreign-Currency Loans:*

Non-resident corporations earning interest on foreign-currency loans extended to Indian business enterprises or to the Government of India are taxed at the rate of 20% on the gross amount of interest.

## *Financial Institutional Investors:*

FIIIs are taxed at the rate of 10% on long-term capital gains and at the rate of 30% on short-term capital gains arising from the transfer of securities (other than units). However, if the transaction is liable to STT, the long-term capital gains may be exempt from tax and short-term capital gains may be liable to tax at 15% from A.Y. 2009-10. (Updated as per Finance Act, 2008).

The above rates may be subject to more beneficial provisions contained in the tax treaty between India and the country in which the taxpayer is resident. All the tax rates mentioned above, excluding the rates prescribed under the relevant treaty, must be enhanced by a surcharge of 2.5% and an education cess at the rate of 3% on the tax payable inclusive of surcharge.

## *Presumptive Taxation*

In certain specified cases, taxable income and the tax thereon is calculated on a presumptive basis.

Activity	Shipping business of Non Resident	Exploration of mineral oils	Operation of Aircrafts	Business of Civil construction
Sections applied	44B	44BB	44BBA	44BBB
Conditions	(1) Assessee is non-resident in India. (2) The assessee is engaged in the business of operation of ships	(1) Assessee is non-resident in India. (2) The assessee is engaged in the business of providing services and facilities in connection with, or supplying plant and machinery on hire, used or to be used in the exploration for , and exploration of mineral oils.	(1) Assessee is non-resident in India. (2) The assessee is engaged in the business of operation of Aircrafts	(1) Assessee is a foreign company. (2) Assessee is engaged in the business of civil construction or erection of plant or machinery or testing or commissioning thereof, in connection with a turnkey power project (3) The aforesaid project is approved by Central Government. (4) The above project is financed under any international aid programme
Tax liability	7.5% of amount received on account of carriage of goods, passengers, livestock mail or shipped at any port in India etc.  The amount received or deemed to be received in India by or on behalf of the assessee on account of carriage of goods, passengers, livestock mail or goods shipped at any port in India etc. shipped at any port outside India	10% of the aggregate of the amount on account of aforesaid services and facilities	5% of amount on account of carriage of passengers, livestock, mail or goods from any place in or from any place outside India.	10% of the amount paid or payable (whether in or out of India) on account of aforesaid services and facilities

### ***Withholding Tax/Tax Deducted at Source (TDS)***

Under Indian Income Tax laws, tax has to be withheld at source by the person responsible for making the payment if such a payment is taxable in India in the hands of the payee. Such tax has to be deducted at the time of credit to the account of the payee or actual payment, whichever is earlier. The rates for such deduction are provided in the Income tax Act.

### ***Minimum Alternate Tax (MAT)***

With a view to bring zero tax paying companies having book profits under the tax net, the domestic tax law requires companies to pay MAT in lieu of the normal corporate tax, in a case where the normal corporate tax is lower than the MAT.

MAT is levied at 10 percent (plus applicable surcharge, cess and secondary and higher education cess) of the adjusted book profits of companies where the normal corporate tax payable is less than 10 percent of their book profits.

A tax credit, being the difference between the tax liability under MAT provisions and normal provisions, can be carried forward for set off in the year in which tax is payable under the regular provisions. Such set off shall be allowed

on the difference of tax as per regular provisions and as per MAT provisions. However, no carry forward shall be allowed beyond the seventh assessment year succeeding the assessment year in which the tax credit becomes allowable.

A certificate from a Chartered Accountant certifying the amount of book profits must be filed together with the corporate tax return.

### ***Fringe Benefit Tax (FBT)***

Fringe Benefit Tax has been introduced w.e.f. F.Y. 2005-06. It provides for levy of an additional tax @ 30% (plus applicable surcharge & education cess) in the hands of an employer on the value of fringe benefits provided to the employees other than perquisites on which tax is paid/ payable by the employee.

The FBT legislation contains an exhaustive list of expenses which are deemed to be fringe benefits to the extent of 5%, 20% or 50% of the cost incurred or payment made by the employer. It is not an allowable expense from taxable income, but is allowable deduction for computing book profits for the purpose of computation of book profit under MAT. FBT is payable irrespective of whether the employer has taxable income in India or not.

In the case of foreign companies FBT liability arises only if their employees are based in India and that too in respect of operations attributable to Indian operations.

The Finance Act, 2007 has brought Employees' Stock Option Plan within the purview of FBT and this would include any specified security or sweat equity shares allotted or transferred, directly or indirectly, by the employer free of cost or at concessional rates to his employees.

The Finance Act, 2008 has inserted a new section enabling the employer to recover the fringe benefit tax from the employees in respect of specified security or sweat equity shares, if such security or shares are transferred or allotted to the employee on or after 1st April, 2007.

### *Tax Concessions*

The Government of India provides various incentives for encouraging the development of industries and exports and the promotion of programmes for the betterment of the society. It also provides various other incentives and exemptions for setting up of Industrial Undertakings in the specified areas in India. Such incentives and exemptions are given to tap the unutilized resources of India.

Some of the incentives allowed in the computation of income under the head 'Profits and Gains from Business and Profession' in this connection are as under:

<b>Nature of Business</b>	<b>Undertaking should start operating.</b>	<b>Exemption-Quantum &amp; Period</b>
Undertaking engaged in the business of developing or operating and maintaining or developing, operating and maintaining of infrastructure facility.	1st April 1995 and onwards	100% of the profits for any 10 consecutive years within a time frame of the initial 20 years (15 years in case of ports, airports, inland ports, inland waterways).
Undertaking which develops or develops and operates or maintains and operates an industrial park	1st April 1997 to 31st March 2009	100% of the profits for any 10 consecutive years within a time frame of the initial 15 years
Undertaking set up for generation or generation and distribution of power	1st April, 1993 to 31st March, 2008	100% of the profits for any 10 consecutive years within a time frame of the initial 15 years

Undertaking which undertakes substantial renovation and modernization of the existing transmission or distribution lines.	1st April, 1994 to 31st March, 2010.	100% of the profits for any 10 consecutive years within a time frame of the initial 15 years
Undertaking engaged in development of Special Economic Zone (SEZ)	1st April, 2005 onwards	100% of the profits for any 10 consecutive years within a time frame of the initial 15 years.
Undertaking located in areas other than North-Eastern regions that begins commercial production of mineral oils and refining minerals oils	1st April, 1997 onwards (for mineral oils) and 1st October, 1998 onwards (for refining of mineral oils).	100% of the profits for first 7 consecutive years.
Undertaking engaged in integrated business of handling, storing and transporting food grains or undertaking engaged in business or processing, preservation and packaging of fruits and vegetables.	1st April, 2001 and onwards	100% of profits for first five years and then 25% (30% in case of companies) of profits for next five years
Undertaking engaged in the business of hotel or in the business of building, owning and operating a convention centre, located in a "specified area"	1st April, 2008 to 31st March 2013.	100% of the profits for first 5 consecutive years.
Undertaking engaged in operating and maintaining a hospital located anywhere in India except in certain excluded areas.	1st April, 2008 to 31st March 2013.	100% of the profits for first 5 consecutive years

Undertaking engaged in collecting and processing or treating of bio-degradable waste for generating power or producing bio-fertilizers, bio-pesticides or other biological agents or for producing bio-gas or making pellets or briquettes for fuel or organic manure.		100% of the profits for first 5 consecutive years.
Scheduled bank incorporated in India or owing offshore banking unit in SEZ.		100% of the profits for first 5 consecutive years and 50% for next five years.
Undertaking manufacturing hand made articles or things which are of artistic value and which requires use of wood as a main raw material provided 90% or more of its sales should be by way of exports of such articles.		Deduction of 100% profits derived from export of such articles will be allowed up to AY 2009-10.
Undertaking manufacturing, and exporting articles or things or computer software situated in a special economic zone (SEZ)	1st April, 2006 onwards	100% of export profits for initial five years, 50% of export profit for next 5 years and thereafter for another 5 years, an amount not exceeding 50% of export profit credited to SEZ Re-investment reserve account.
New undertaking engaged in manufacture of articles or things (other than specified articles) in specified zones or areas or new undertaking engaged in manufacture of articles or things specified :  <ul style="list-style-type: none"> <li>• In state of Sikkim</li> <li>• In state of Himachal Pradesh or Uttarnchal.</li> </ul>	23rd December, 2002 to 31st March, 2012  7th January, 2003 to 31st March, 2012	100% for initial 10 years.  100% for initial 5 years and thereafter 25% (30% in case of company) of the profits for next 5 years

(Updated as per Finance Act, 2008)

## *Depreciation Allowance*

In the process of extending incentives and concessions to achieve economic growth, Indian tax law provides for accelerated depreciation allowance through higher rates, intended to encourage capital investments by reducing overall tax incidence

Allowance for depreciation is available from the year since when the asset is ready to “put to use” for the business purpose. The Indian Income Tax Act provides that for tax purposes, the depreciation is calculated on block of assets at prescribed rates as per declining balance method (written down value

method). The only exception is the undertakings engaged in power generation where the straight-line method could also be opted.

The block of assets method is easy to understand. The cost of assets acquired during the year is added to the opening balance and sale value of the assets disposed off during the year is reduced therefrom. The prescribed rates are then applied on the balance.

For assets installed in the second half of the fiscal year depreciation at 50% of the normal rate is applied.

Tax depreciation rates (written down value method):

Assets	Percent
Residential buildings	5
Buildings other than above	10
Purely temporary erections	100
Plant and machinery	15
Power generating and transmission	80
Computers (including software)	60
Furniture and fittings, including electrical fittings	10
Intangible assets (such as know-how, patents, copyrights trademarks, licenses, franchises or any other business or commercial right of similar nature)	25

The above list is only illustrative, and not exhaustive.

Any unabsorbed depreciation is allowed to be carried forward for an indefinite period for claiming set off against the taxable income of subsequent years.

Company law provides for the straight line method of depreciation which leads to a lower charge in the initial years in the published accounts thus giving rise to deferred tax.

## *Business Losses*

Business losses are allowed to be carried forward and set off in the next eight subsequent years against the taxable business income derived in those years.

## *Double Tax Relief*

Keeping in line with the international practice of avoiding double taxation of cross border income, India has entered into agreements with the Government of other countries outside India for the avoidance of double taxation of income under the Indian Act and under the corresponding law in force in that country. The double taxation agreements are in the nature of delegated legislation negotiated with the purpose of providing a rational and equitable allocation of income between two countries over which both have tax jurisdiction and to provide relief from double taxation of the same income taxed in two countries.

The purpose of a Double Taxation

Avoidance Agreement is to assist tax payers in India and abroad to know in advance, to the extent practicable, the tax implications of the various transactions arising from the implementation of an agreement for foreign collaboration between any person in India and another outside India. Also help to choose a foreign collaborator located in a particular country with which India has entered into an agreement for avoidance of double taxation. This is because the provisions of such bilateral agreements override the provisions of the domestic laws and because the burden of tax falling on the collaborators in the two countries becomes much more clearly ascertainable in the light of such bilateral agreements. Most of these agreements are comprehensive and cover all types of income whereas some of these are limited to aircraft and/ or shipping profits.

Countries with which India has entered into Double Tax Relief agreement :

Armenia	Cyprus	Ireland
Afghanistan*	Czech Republic	Iran*
Australia	Denmark	Israel
Austria	Ethiopia*	Italy
Bangladesh	Egypt	Japan
Belarus	Finland	Hashemite Kingdom of Jordan
Belgium	France	Kazakhstan
Brazil	Germany	Kenya
Bulgaria	Greece	Korea
Canada	Hungary	Kuwait*
China	Indonesia	Kyrgyz Republic

Lebanon*	Poland	Thailand
Libya	Portuguese Republic	Trinidad & Tobago
Malaysia	Qatar	Turkey
Malta	Romania	Turkmenistan
Mauritius	Russia	Ukraine
Mexico	Saudi Arabia*	U.A.E.**
Mongolia	Slovenia	Uganda
Morocco	Singapore	United Arab Republic (Egypt)
Namibia	South Africa	U.K.
Nepal	Spain	U.S.A.
Netherlands	Sri Lanka	Uzbekistan
New Zealand	Sudan	Vietnam
Norway	Sweden	Yemen Arab Republic
Oman	Switzerland*	Luxembourg
Pakistan*	Syria	Zambia
Philippines	Tanzania	

\* Limited Agreements

\*\* both Comprehensive & Limited Agreements

### *Advance Rulings*

Income-tax law in India is complicated as in most other countries. It is sometimes not easy to construe the legal provisions; doubts arise in the minds of tax gatherers and taxpayers alike as to the correct interpretation of law. This situation creates more practical difficulties to foreign enterprises doing business in India. Therefore, with a view to minimizing uncertainty in taxation of income, the Government of India has introduced a system of Advance Rulings to enable any non-resident to obtain binding rulings on its income-tax liability even before the income is earned. The system of Advance Rulings is primarily meant for non-residents so

that the complexity of the Indian tax legislation or the delay and cost of litigation in tax matters may not act as a disincentive for their investment proposals in India. Accordingly, the foreign companies and other non-residents proposing to do business in India can know the extent of their tax liability in advance. For this purpose, Chapter "XIX-B" consisting of sections 245N to 245V was inserted in the Income-tax Act by the Finance Act, 1993, with effect from 1st June, 1993.

An authority constituted under the Income-tax Act, which is known as the Authority for Advance Rulings, renders advance Rulings in India.

## *Transfer Pricing*

As per provisions of Income Tax Act, any income arising from an international transaction shall be computed having regard to the Arms Length Price.

International transaction means a transaction between two or more Associated Enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property or provision of services or lending or borrowing money or any other transaction having a bearing on the profits, income, losses or assets of such enterprises. In addition, a mutual agreement or arrangement between two or more associated enterprises for allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service, or facility provided or to be provided to any one or more of such enterprises will also be subject to the Arms Length rule.

Arms Length Price means a price, which is applied or proposed to be applied in a transaction between persons other than associated enterprises in uncontrolled conditions. As per provisions of the Act, all or anyone of the associated enterprises must be a “non-resident”.

An “enterprise” is an Associated Enterprise:

- If it participates directly or indirectly in the management or control or capital of the other Enterprise
- If any person who participates in the management or control or capital of an enterprise and also participates in the management or control or capital of the other enterprise.

## *Banking Cash Transaction Tax (BCTT)*

BCTT is a recent levy & has been introduced in India w.e.f. June 1, 2005. Tax is leviable @ 0.1% on the value of following taxable banking transactions:

Amounts of cash withdrawn from a scheduled bank on a single day from an account (for other than savings account) or amounts of cash received on encashment of term deposit(s) on a single day from a scheduled bank exceeding:

- INR 25,000 (increased to INR 50,000 from 1.06.2007) in case of Individuals & HUF.
- INR 1,00,000 in other cases.

No BCTT shall be charged in respect of any taxable banking transaction after the 31st day of March, 2009. (Updated as per Finance Act, 2008)

### **Securities Transaction Tax (STT)**

STT is payable on transactions in equity shares, derivatives and units of an equity-oriented funds entered in a recognized stock exchange or on sale of units of any equity mutual fund to the mutual fund.

The rates of STT are:

- Delivery-based transactions in equity shares or units of an equity-oriented funds–Buyer and seller each to pay 0.125%
- Sale of units of any equity mutual fund to the mutual fund–Seller to pay 0.25%
- Non-Delivery based transactions in equity shares or units of an equity-oriented units - Seller to pay 0.25%
- Derivatives–Seller to pay 0.017%.

### **Commodity Transaction Tax (CTT)**

Commodities Transaction Tax (CTT) is levied on taxable commodities transactions of purchase or sale of option in goods; or option in commodity derivative; or any other commodity derivative traded in a recognized association.

Tax Rates:

Taxable commodities transaction	Rate	Payable by
Sale of an option in goods or an option in commodity derivative	0.017%	Seller
Sale of an option in goods or an option in commodity derivative, where option is exercised	0.125%	Purchaser
Sale of any other commodity derivative	0.017%	Seller

(Updated as per Finance Act, 2008)

### **Wealth Tax**

This is a tax imposed on certain non-productive assets owned by the assessee. Some of the non-productive assets include jewellery, non-residential house property, etc. Investment in shares and other financial instruments are entirely exempt from Wealth tax. Wealth Tax is charged for every assessment year, on the net wealth of an individual / company, on the corresponding valuation date @ 1% of the amount by which net wealth exceeds Rs.1.5 million.

# INDIRECT TAXES

## *Customs Duty*

Item No. 83 of the Union list of the Constitution of India provides for the levy of Duties of Customs including export duties. Custom Duty is levied on goods imported into or exported from India. Predominantly, this duty is on import and partially on export of goods. In the present scenario of increasing globalization and entering into of free trade agreements with the members of the various regional trading blocks like SAARC & ASEAN & with WTO, the custom duty rates have been standardized by the regulatory authorities and the levy load reduced to a great extent. The peak rate has reduced from 30% in 2002-03 to 10% in 2007-08

The customs duty on imports is levied when the goods cross the custom frontiers, i.e., when they enter the territorial boundaries of India. Goods can either be cleared for home consumption, directly from the port on the payment of custom duty or else can be cleared to warehouse without payment of duty, by furnishing a bond, wherefrom such goods can be cleared at a later date for home consumption, on payment of duty and other warehousing charges. Certain goods for import fall

under the Negative List whereby specific permission is required before its import.

For the purpose of computation of custom duty, rate and value are required.

Rate: A separate act i.e. CTA (Customs Tariff Act) provides for the rates of import & export duties. There are two types of rates as specified in CTA. One is standard rate & the other one is preferential rate. The preferential rate is applicable only for the countries as notified by the Central Government.

Valuation: The valuation is done as per Custom Valuation (DPIG) Rules, 1988 & transaction value is the primary basis for valuation under the Indian Customs Law.

### Types of Duties under Customs Law:

- Basic Custom Duty i.e. BCD.
- Additional Customs Duty i.e. CVD (Countervail Excise Duty).
- Additional Duty of Customs in lieu of VAT.

In addition following duties can also be levied to protect domestic industry

- Anti-Dumping Duty.
- Countervailing duty on subsidized articles.
- Safeguard Duty.
- Protective Duty.

Due to imposition of these additional duties, the effective custom rate becomes much higher than 10%. Certain Exemptions/concessions are available for imports under specific schemes. The foreign trade policy also provides incentives for exports like Duty drawback, Export promotion Capital Goods Scheme (EPCG) etc.

### *Excise Duty*

Item No. 84 of the Union List of the Constitution of India provides for the levy of Excise Duty on goods produced or manufactured in India. The incidence of tax is normally passed on to the buyer. 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. Thus the outflow of funds can be delayed till the goods are removed from the factory.

For the purpose of computation of excise duty, rate and value are required.

Rate: A separate Act i.e. CETA (Central Excise Tariff Act) provides for the rates of excise duties and goods must be essentially mentioned in CETA to become excisable. The rates are on a declining trend & at present most of the products mentioned in CETA are either charged at 14% or are NIL rated.

Valuation: The Excise Act provides three basis for the Calculation of excise duty:

1. Specific Duty payable on the basis of weight, length etc.
2. Tariff Value i.e. values fixed by the Central Government for certain notified goods.
3. Retail Sale Price i.e. on the basis of MRP subject to certain abatements.

Duty is charged mostly on an ad-valorem basis. Value for the purpose of calculating excise duty is taken as per the Central Excise Valuation Rules, 2000. Where price is the sole consideration for sale, and buyer & seller are not related person, assessable value is taken to be 'Transactional Value'. It is the price at which goods are sold by the assessee at the time & place of removal.

### CENVAT- Avoidance of Double Taxation:

Double taxation on the goods manufactured, which consists of duty paid on raw materials can be avoided by applying the provisions of CENVAT (Central Value Added Tax).

Cess: Cess @3% is applicable on duties of Customs and Excise.

## *Central Sales Tax (CST) / Value Added Tax (VAT)*

CST & VAT are the taxes on sale of goods. CST is charged by the Central Government on inter-state sales & VAT is charged on intrastate sales by the respective state government.

For the present CST will continue, though it is proposed to be phased out in due course. The provisions in respect of Central State Tax are summarized below:

- Recently, the rate of CST has fallen from 3% to 2%.
- There will be no credit of CST paid on inter-state purchases.
- If goods are sent on stock transfer outside the state, input tax credit in excess of 4% will be allowed as credit. In other words, input tax to the extent of 4% will not be allowed as credit, if goods are sent inter-state.

The Government has now implemented a Value Added Tax (VAT) regime in most of the States from 1st April 2005. After implementation of VAT throughout India, there will be a uniform rate structure among all the states. The VAT scheme in India is quite similar to those prevailing in other Countries. It is a multi-point tax & is levied on value added at each stage. Under the VAT scheme, full input tax credit is available

in respect of locally procured goods and in respect of capital goods, input credit is available on a staggered basis over a period of two to three years. Accordingly, it removes the cascading effect of tax for intermediate businesses.

The basic slabs of rate under VAT are as follows:

- 0% for natural and unprocessed products and others essential goods;
- 1% for silver, gold ornaments, etc;
- 4% for agricultural and industrial inputs, IT products, Capital goods, items of basic necessities, etc; and
- 12.5% for other goods.

A composition scheme is also available to dealers whose gross turnover exceeds 1 million but does not exceed 5 millions. This scheme is optional and if any dealer opts for the said scheme, the same is not entitled to input tax credit.

Sales tax (i.e. CST & VAT) is levied on the value of goods sold. The value of goods will include the cost of manufacture, excise duty levied on the cost of manufacture and profit margin adjusted in the unit rate. Sales tax is recovered from the first buyer and passed on the exchequer. Second Sales do not bear the burden of Sales Tax. Rates of sales tax are different in various states.

## *Service Tax*

Item No. 92C of the Union List of the Constitution of India provides for the levy of Service tax in India. There is no separate Act for service tax and provisions relating thereto are given in the Finance Act itself. Service tax is levied only on the taxable services as are specified in law. Presently more than 106 services are covered under the Service Tax net.

Rate: Service tax is charged at a uniform rate on the value of taxable services for all services covered. The Current rate of Service Tax is fixed at 12.36% (including cess) on the value of chargeable services.

Valuation: Service tax is basically levied on the value of the services provided. The Service Tax (Determination of Value) Rules have been recently framed and now non-monetary consideration can also be subjected to service tax levy.

Exemption to Small Scale Service Providers: Exemption is given with regard to service tax to Small Scale Service Providers when the value of taxable services provided does not exceed Rs 1.0 million. Earlier this limit for availing exemption was Rs. 0.8 million.

Export/ Import of Services: The Export of Services Rules, 2005 & Import of

Services Rules, 2006 respectively specify the criteria based on which a particular service would qualify as an export or import. In case of export of services, no service tax is payable. Further the exporter can also claim rebate/refund of excise duty/ service tax paid on inputs/ input services used in the export of the service.

CENVAT Credit: The provisions of CENVAT Credit are also applicable in case of Service tax i.e. credit of tax on input/ input services can be availed. Further credit Rules also allow a service provider to avail & utilize the credit of additional duty of excise/customs (on inputs as well as capital goods) for the payment of service tax.

## *Stamp Duty*

Almost all documents executed in India are chargeable to Stamp Duty at specified rates as mentioned in the relevant Acts. The rate structure is decided by the states. The legal enforceability of any document requiring bearing stamp duty is considered by any authority only when it bears stamp at the prescribed rate applicable in the place of its execution.

## *Octroi Duty/Entry Tax*

This is a tax levied by the municipalities of various towns and cities at the time of

entry of goods into such towns and cities. It is also identified as entry tax for entry of goods in the respective jurisdiction of the local authorities. Exemptions and concessions in the duty are being offered by local authorities depending upon their requirements. There is no proposal to extend VAT to entry tax or Octroi levied by local authorities. These will continue.

***Research and Development Cess:***

Under the Research and Development Cess Act, 1986, cess is levied by Central Government at the rate of 5% on the import of technology into India. Such cess is required to be paid by the importer on payments made for such imports.

## *Special Economic Zones and Software Parks*

With a view to giving impetus to its export drive, the government has set up Export Processing Zones (EPZ's), which provide almost free trade environment for export production to make Indian export products more competitive in the world market.

The Government has introduced various schemes to offer special incentives and tax concessions to businesses engaged in exports such as the 100% Export Oriented Units (EOU's) Scheme, Software Technology Parks (STP's) Scheme and the Electronic Hardware Technology Parks (EHTP's) Scheme. The schemes provide for a minimum value addition to the cost of production and the units have to be a net positive foreign exchange earner.

### **SPECIAL ECONOMIC ZONE (SEZ)**

Foreign Trade Policy provides for setting up of SEZs in the country with a view to enable an internationally competitive and hassle-free environment for exports. The SEZ Scheme has become operational after issuing of notifications by the Government on 30th May 2000.

The important features of the SEZ policy are enumerated below:

- SEZs are to be specifically delineated duty free enclaves and shall be deemed to be foreign territory for the purposes of trade operations and duties and tariffs.
- Goods going into the SEZ area from Domestic Tariff Area (DTA) shall be treated as deemed exports and goods coming from the SEZ area into DTA shall be treated as if the goods are being imported.
- SEZ units can be set up for manufacture of goods and rendering of services, production, processing, assembling, trading, repair, remaking, reconditioning, re-engineering including making of gold/silver/platinum jewellery and articles thereof or in connection therewith.
- SEZs may be set up in the public, private or joint sector or by State Governments.
- SEZ should have the minimum prescribed area as per the policy.
- SEZ units would have to be positive Net Foreign Exchange Earners and would not be subject to any minimum value addition norms for export obligations.
- 100% FDI would be permitted for all investments in SEZs except a few

- activities under the negative list (tobacco, alcoholic beverages, arms and ammunition, etc).
- The Development Commissioner would be responsible for administrative control of the zone.

### *Fiscal Incentives Available to SEZ Developers/Units*

#### Direct Tax Incentives for SEZ Developers

- 100% tax holiday for the business of developing SEZ available for a period of any 10 consecutive years out of 15 years beginning from the year in which the SEZ is notified.
- The above benefits are also available in respect of co-developers providing infrastructure facilities.

#### Direct Tax Incentives for SEZ Units

- 15 year tax holiday (100% for first 5 years, 50% for next 5 years and up to 50% for next 5 years subject to creation of reserves) on export profits available to units commencing business after April 1, 2005.

#### Indirect Tax Incentives for SEZ Developers/Units

SEZ developers and entrepreneurs are eligible for the following benefits for carrying out authorised operations in the SEZ:

- Exemption from customs duty on goods/services imported or exported. [Supplies from Domestic Tariff Area (DTA) to SEZ to be treated as exports while those from SEZ to DTA to be treated as imports].
- Exemption from excise duty on goods procured from DTA.
- Drawback or any other admissible benefits on goods brought or services rendered by DTA.
- Exemption from service tax on taxable input services.
- Exemption from Central Sales Tax on interstate sale or purchase of goods except for newspaper.
- Removal of goods into DTA also permitted subject to prescribed conditions and on payment of all applicable customs duty leviable on importation of such goods into India.

### **SOFTWARE TECHNOLOGY PARKS - STP SCHEME**

The STP scheme is a 100 percent export oriented scheme for the development and export of computer software, including export of professional services using communication links or physical media. This scheme is unique in its nature as it focuses on one product/sector, i.e. computer software.

The scheme integrates the government concept of 100 percent Export Oriented Units (EOUs) and Export Processing Zones (EPZs) and the concept of Science Parks/Technology Parks, as operating elsewhere in the world.

- Approvals are given under single window clearance scheme.
  - A company can set up a STP unit anywhere in India.
  - 100% Foreign Equity is permitted and approved by the jurisdictional Director of STPI.
  - All the imports of Hardware & Software in the STP units are completely duty free.
  - Import of secondhand capital goods is also permitted.
  - It shall be a positive net foreign exchange earner which shall be achieved over a block of 5 years.
  - Use of computer system for commercial training purposes is permissible subject to the condition that no computer terminals are installed outside the STP premises.
  - Sales in the Domestic Tariff Area (DTA) shall be permissible up to 50% of exports in value terms.
- STP units are exempted from payment of corporate income tax up to 2010.
  - The capital goods purchased from the Domestic Tariff Area (DTA) are entitled to benefits like exemption from excise Duty & reimbursement of Central Sales Tax (CST)
  - Capital invested by Foreign Entrepreneurs, know-how Fees, Royalty, Dividend etc., can be freely repatriated after payment of Income Taxes due on them, if any.
  - Repatriation of foreign currency for payments can be freely done.

# *Other Economic Laws & Regulations*

## **Indian Contract Act, 1872**

As per the Act, all agreements are contracts if they are made by the free consent of parties competent to contract, for a lawful consideration and a lawful object, and are not expressly declared to be void. Every person who is a major (adult 18 years and above) according to the law to which he is subject, and who is of sound mind and is not disqualified from contracting by any law to which he is subject, is competent to contract.

## **The Information Technology Act, 2000**

An Act to provide legal recognition for transactions carried out by means of electronic data interchange, commonly referred to as "electronic commerce" and which involve the use of alternatives to paper-based methods of communication and storage of information to facilitate electronic filing of documents with the Government agencies.

## **The Consumer Protection Act, 1986**

The Act provides for better protection of the interests of consumers and for the purpose makes provision for the establishment of consumer councils and other authorities for the settlement of consumers' disputes.

## **The Competition Act, 2002**

The Act provides for the establishment of a Commission to prevent practices having an adverse effect on competition; to promote and sustain competition in markets; to protect the interests of consumers and to ensure freedom of trade carried on by other participants in markets.

## **The Sale of Goods Act, 1930**

Though contracts for sale of goods are subject to the general principles of the law relating to contracts i.e. the Indian Contract Act, 1872, but they have certain peculiar features such as, transfer of ownership of the goods, rights and duties of the buyer and seller, conditions and warranties implied under a contract for sale of goods, etc. which are the subject matter of the provisions of the Sale of Goods Act, 1930.

## **The Payment of Bonus Act, 1965**

The Act provides for payment of bonus to persons employed in certain establishments (every factory and every other establishment where 20 or more workmen are employed on any day during an accounting year) on the basis of either profits or production or productivity.

### **The Payment of Gratuity Act, 1972**

The Act is applicable to every factory, shop or an establishment in which ten or more persons are employed, or were employed on any day of the proceeding twelve months and the said factory, shop or establishment shall continue to be governed by the provisions even if the number of persons employed therein fall below ten.

### **The Workmen Compensation Act, 1923**

The Act's aim is to provide workmen and/or their dependents some relief by certain classes of employers in case of accidents arising out of and in the course of employment and causing either death or disablement of workmen.

### **Employees Provident Fund And Miscellaneous Provisions Act, 1952 (EPFMPA)**

The Act was enacted with the main object of "making some provision for the future of the industrial worker after he retires or for his dependants in case of his early death" and accordingly to provide for the institution of provident funds, pension fund and deposit linked insurance fund for employees in the factories and other establishments.

### **The Industrial Dispute Act, 1947**

An Act to make provision for the investigation and settlement of industrial disputes and for certain other purposes.

### **The Minimum Wages Act, 1948**

It was enacted to protect and safeguard the interest of workmen. Its main object is to ensure that the wage period is fixed and the payment of proper wages is made in time to workmen. In case of any violation, it provides a right to make claims.

### **The Negotiable Instruments Act, 1881**

The aim of the Act is to regulate commercial transactions and was drafted to suit requirements of business conditions prevailing when it was passed in 1881. The instrument is mainly an instrument of credit readily convertible into money and easily passable from one hand to another.

### **The Factories Act, 1948**

The Act is social legislation which has been enacted for occupational safety, health and welfare of workers at work places. It applies to the industries in which 10 or more than 10 workers are employed (in manufacturing process being carried out with the aid of power) or in which 20 or more than 20 workers

are employed (in manufacturing process being carried out without the aid of power) on any day of the preceding 12 months.

### **The Trademark Act, 1999**

An Act to amend and consolidate the law relating to trade marks, to provide for registration and better protection of trademarks for goods and services and for the prevention of the use of fraudulent marks. The Act consists of several provisions relating to the speedy disposal of appeals, rectification of applications and simplification of procedures for the registration of the registered user and for enlarging the scope of the permitted use of trademarks and prohibition on the use of someone else's trademarks as part of corporate names or names of business concerns.

### **The Copyright Act, 1957**

As per the Act, copyright subsists in original literary, dramatic, musical and artistic work or a cinematographic film or a sound recording.

Under this act several measures have been adopted to strengthen and streamline the enforcement of copyright protection. The amendments made to the copyright law have ushered in comprehensive changes and brought it in line with the new developments in

satellite broadcasting, computer software and digital technology.

### **Indian Patents Act, 1970**

The Act provides for the grant, revocation, registration, license, assignment and infringement of patents in India. The main aim of the amendments made to the Act was to grant product patents for invention relating to drugs and medicines.

### **Arbitration and Conciliation Act, 1996**

The main purpose of the Act is to provide quick redress in commercial disputes by private arbitration which is necessary for the smooth functioning of business and industry. The object of arbitration is settlement of dispute in an expeditious, convenient, inexpensive and private manner so that they do not become the subject of future litigation between the parties.

# Appendices

## APPENDIX A

### VISA-TYPES AND PROCEDURES

The following types of visas are normally granted for entry to India.

#### *Temporary Visas*

Visitors to India need visas to enter the country unless they are Indian citizens. Non-resident Indians holding citizenship of another country are also required to obtain visas before arriving in India unless they hold a Person of Indian Origin (PIO) card issued by the Indian government. Visas must be obtained from the Indian embassy or consulate in the applicant's home country. Tourist visas are valid for one to six months, generally beginning on the date the visa was issued and not on the date of entry into India. Tourist visas are generally multiple-entry visas, however, this option must be specifically requested at the time of application.

#### *Business Visa*

This visa is required by persons visiting India on business. It is necessary to provide a letter from the applicant's overseas employer stating the exact purpose of the visit, and the expected duration with the application. A letter of invitation from the Indian Company

should also be provided. Business visas are normally Multiple Entry and may be granted for up to two years. Business Visas are issued for visits of more than a 180-days with multiple entries. Although a Business visa is usually valid for a period of up to five years, there is no hard and fast rule for the same. Business visas valid for up to ten years with multiple entries is available to foreign businessmen who have set up or intend to set up joint ventures having governmental approval in India.

#### *Employment Visa (Work Permits)*

A Multiple Entry employment visa is granted on a case by case basis to foreign nationals wishing to take up an employment in India. Indian companies are allowed to engage the services of foreign nationals without any approval. An employment visa must be obtained from the Indian Consulate in the country of residence of the applicant, prior to departure for India. Normally the following main papers are required to be filed with the application for employment visa:

- A letter of secondment from the overseas company and an employment letter from the Indian company.
- Expected duration of the employment.

## *Entry Visa/X-Visa*

This visa is granted to those persons who wish to visit India for long term or permanent residence but do not belong to any of the above categories. Foreign nationals coming to India on an employment visa may obtain an X-visa for their spouses before coming to India. If such a spouse decides to take up any employment in India, then the spouse will be required to go back to the port of origination and obtain the requisite employment visa. According to the rules currently in force, a change of category of visa is not permitted. Any breach in the purpose / category of the visa granted to a foreign national is illegal and can result in his / her deportation.

The foreign national can however apply for an extension of visa duration.

## *Spouse Work Rights*

Generally spouses of foreign nationals arrive on an X-visa, which does not allow any employment or business in India. In cases where the spouse wants to work in India, then an appropriate visa (that is, a business or employment visa) is required. Once the spouse reaches India with an X-visa, and decides to take up any employment, then the spouse would need to go back to the port of origination and obtain the requisite employment visa.

## *Registration Requirements*

Foreign national entering India for the first time on a visa (whether tourist, business or any other) which is valid for a period of more than 180 days, would be required to register themselves with the appropriate Foreigner's Regional Registration Office ("FRRO") within fourteen (14) days of his/her arrival in India. Such a visa holder would be required to register with the relevant FRRO notwithstanding the fact that the visa holder intends to remain in India for a period that is less than the duration of the visa in question. Therefore, the implication of such a visa is that the foreign national holding the visa would be deemed to have the intention of remaining in India for the entire duration of the visa.

In case foreign nationals are required to move around the country to comply with the demands of their jobs/profession. Under such circumstances, the foreign national would be required to obtain registration with the "relevant FRRO", i.e., either in the first port of entry or where the residential address has been provided.

## *Conversion/Extension of Visa*

In the event that a foreign national holding a visa valid for a period of less than one year desires to convert it into a

visa valid for a period of more than one year, then he/she would be required to approach the Ministry of Home Affairs for conversion/extension of the said visa.

### *Drivers Permit*

Foreign nationals are not allowed to drive in India using their home country drivers' licenses. Foreign nationals must obtain international drivers' licenses in their home countries. International drivers' licenses are generally valid for six months. To obtain an Indian driver's license, individuals must apply to the Regional Transport Authority, which issues learners' permits. This enables the individual to drive if accompanied by an adult who has a valid Indian driver's license. One month after the learner's permit is issued, a driving test and a verbal examination of the local driving laws must be taken. On successful completion of the examinations, the Regional Transport Authority issues a driver's license.

## APPENDIX B

### FDI CAPS FOR DIFFERENT SECTORS

Sector wise list of Foreign Direct Investment permitted under automatic route

<b>Illustrative list of Sector</b>	<b>Investment Cap – Automatic route</b>
Airports – Greenfield Projects	100%
Air Transport Services	49%
Banking Private Sector	74%
IT Services like ITES, BPO, Software services	100%
Power	100%
SEZ	100%
Insurance	26%
Coffee and Rubber processing and warehousing	100%
Alcohol – Distillation & brewing	100%
Coal & Lignite mining for Captive consumption	100%
Construction development projects	100%
Floriculture, Horticulture, Animal Husbandry, Pisciculture, Aquaculture etc.	100%
Hazardous chemicals	100%
Industrial Explosives- Manufacture	100%
Mining: Exploration & Mining precious stones	100%
NBFCs – Only approved activities	100%
Petroleum & Natural gas – other than Refining	100%
Petroleum & Natural gas – Refining	100% for Pvt. Co.s
	100%

Trading – Wholesale/Cash & Carrying	100%
Trading – For Exports (Guidelines)	100%
Telecom – Manufacture of Equipments	Cap – 74%, FIPB beyond 49%
Telecom – Basic and cellular, unified access services etc.	Cap – 74%, FIPB beyond 49%
Telecom – ISP with Gateways	Cap – 100%, FIPB beyond 49%
Telecom – ISP without Gateways	Cap – 100%, FIPB beyond 49%

Note: The permission limit is subject to further conditions.

Sector wise list of Foreign Direct Investment permitted under approval route

<b>Illustrative list of Sector</b>	<b>Investment under FIPB approval Cap</b>
Asset Reconstruction companies	49%
Atomic Minerals & Satellite establishment	74%
Broadcasting - FM Radio	20%
Broadcasting - Direct to Home	20%
Broadcasting - Cable Network	49%
Broadcasting – Hardware Facilities	49%
Up-linking a Non-News & Current Affairs TV Channel	100%
Up-linking a News & Current Affairs TV Ch.	26%
Trading of Item Sourced from Small Scale Sector	100%
Cigars & Cigarettes	100%
Courier Services	100%
Defence Production	26%
Investing Co.s in Infrastructure/Services	49%
Petroleum & Natural gas – Refining	26% for PSUs

Illustrative list of Sector	Investment Cap under FIPB approval
Print Media – news papers & periodicals	26%
Print Media – Scientific Magazines etc	100%
Tea Sector	100%
Trading - Test Marketing	100%
Retailing – Single Brand	51%
Note: The permission limit is subject to further conditions.	

# *Notes*

# *Notes*



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