A close-up, angled view of a globe focusing on the Indian subcontinent and surrounding regions. The map shows countries like India, Pakistan, Iran, Saudi Arabia, and others, with various cities labeled. The globe is set against a background of a clear blue sky with soft, wispy white clouds.

Doing Business in India

Doing business in India



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This Doing Business in India guide contains general information existing at the time of its preparation only (up to June 2015). It is intended as a point of reference and is not intended to be comprehensive nor to provide specific accounting, business, financial, investment, legal, tax or other professional advice or opinion or services. This publication is not a substitute for such professional advice or services, and it should not be acted on or relied upon or used as a basis for any decision or action that may affect you or your business. Before making any decision or taking any action that may affect you or your business, you should consult a qualified professional adviser and also refer to the source pronouncement/documents on which this publication is based.

Professional advisers, such as accountants, lawyers and advisers, will find that the guide provides them with the broad information that they need to discuss their clients' overseas requirements before directing them to the relevant specialist.

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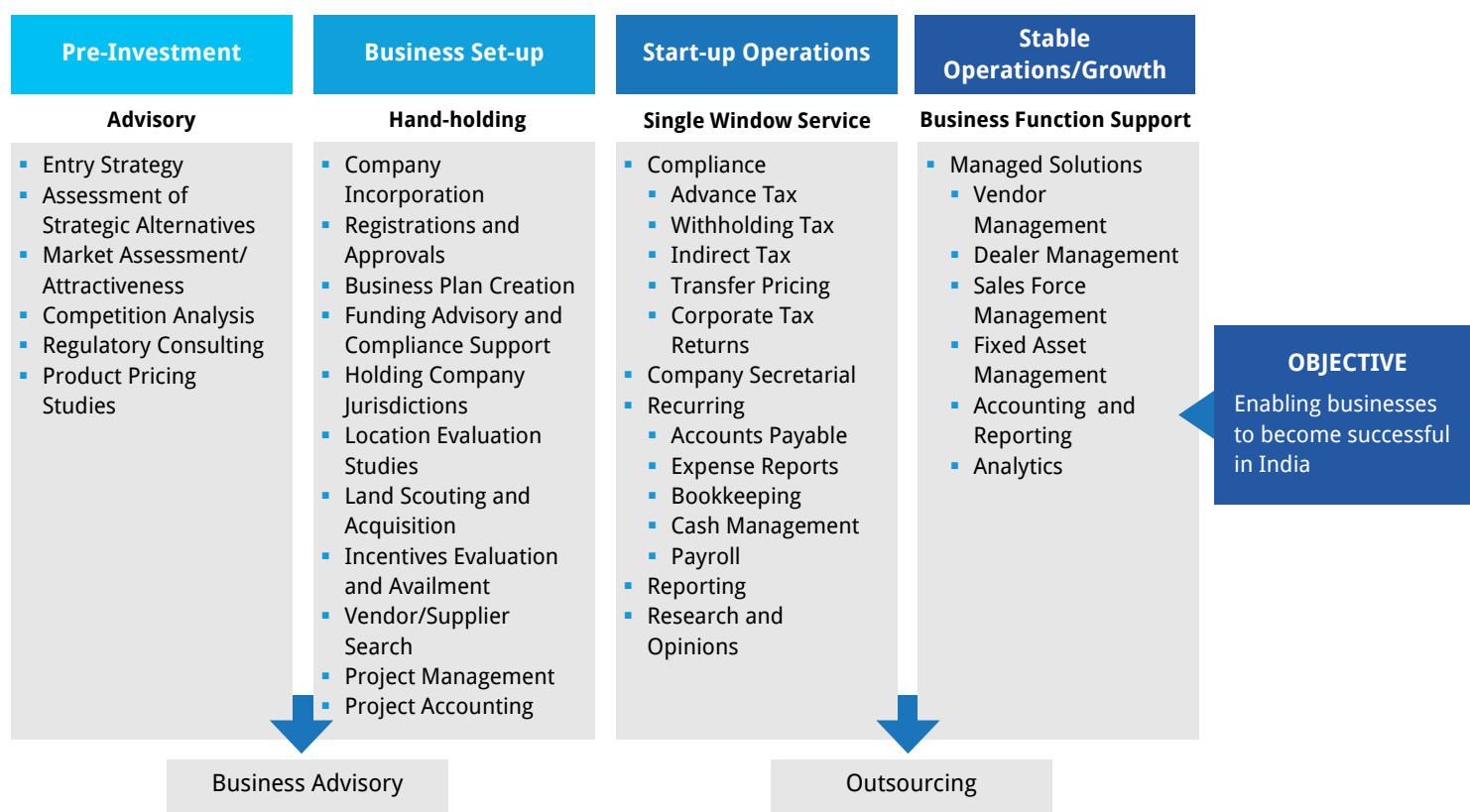
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About SKP

SKP is a long established and rapidly growing professional services group located in six major cities across India. We specialise in providing sound business and tax guidance and accounting services to international companies that are currently conducting or initiating business in India as well as those expanding overseas. We serve over 1,200 clients including multinationals, companies listed on exchanges, privately held and family-owned businesses from 49 countries.

From consulting on entry strategies to implementing business set-ups and M&A transactional support, the SKP team assists clients with assurance, domestic and international tax, transfer pricing, corporate services, and finance and accounting outsourcing matters, all under one roof. Our team is dedicated to ensuring clients receive continuity of support, across the business lifecycle.

The SKP Value Chain



Our clients value our collaborative approach. Right from inception, SKP's founders have emphasised the importance of professional standards and personalised service; and to this day, we continue to reflect this progressive mindset by serving our clients with integrity, delivering high quality, innovative results. Our ability to easily identify, confront and resolve a variety of issues and concerns for our clients comes from our years of experience across a wide range of industries and geographies, combined with a versatile group of professionals and a multi-disciplinary team.

To know more, visit www.skpgroup.com.

The Team



Sapan Parekh, CEO

A Chartered Accountant and an MBA from Duke University, USA, Sapan has been a catalyst in building each business division at SKP. He is the key driving force behind the dynamic Group strategy and business focus. He has the unique ability of blending international expertise with a local perspective and bringing the right cultural complement to an assignment. With his viewpoint extending well beyond monetary gain, he strives to build partnerships with clients focusing on innovative, solution-oriented work.



Deepti Ahuja, Partner, Business Advisory

A Chartered Accountant by qualification, Deepti heads SKP's transaction support and business advisory team. She has experience across industries and has been actively involved in valuations, due diligence, restructuring, synergy estimation in mergers, intangible valuations, transaction structuring, greenfield set-up services and all phases of transaction advisory services.



Manoj Gidwani, Partner, Business Advisory

Manoj heads SKP's business set-up and advisory arm and also looks at the Group's overall marketing and business development initiatives. A Chartered Accountant by qualification, he is proficient in greenfield set-ups, mergers and acquisitions and regulatory issues associated with inward and outward investments. He has been instrumental in developing relationships with European companies and has helped several businesses with their internationalisation plans.



Mehul Shah, Partner, Finance and Accounting

A Chartered Accountant by qualification, Mehul heads SKP's process consulting and business process management function that he helped set up in 2004. With his deep insight into processes in the context of client businesses, he works with clients on performance improvement projects. He also spearheaded the implementation of SKP's quality management system and its certification under ISO 9001:2008.



Nimish Shah, Partner, Finance and Accounting

Nimish heads business development for SKP's finance and accounting outsourcing function. He is also involved in building relationships in the North American market for SKP's business advisory services. With his expertise in information technology, he heads the IT and automation teams and has brought about dramatic efficiencies in how rule-based, repetitive tasks are performed. He also led the ISO 27001 certification of SKP's information security management system.



Pakzad Nussirabad, Director, People (Human Resources)

With an MBA from Cardiff Metropolitan University, UK, Pakzad heads the People function at SKP. He is adept at end-to-end people management, spanning the entire employee lifecycle from pre-inception to separation. Besides having led several innovative people-acquisition initiatives, he places great emphasis on coaching and people development. In addition, he works closely with SKP's business advisory and corporate services teams on HR consulting assignments.



Pratik Shah, Partner, Indirect Taxation

Pratik heads the indirect tax practice at SKP. A Chartered Accountant by qualification, he also holds an Advance Diploma in Indirect Taxes. He has worked across sectors and specialises in handling VAT compliances across India, advising clients on supply chain set-up and distribution, conducting diagnostic reviews on potential leakages, preparing financial models and structuring transactions to mitigate tax exposure.



Pushkar Bagmar, Partner, Corporate Services

Pushkar heads SKP's corporate services function. A Chartered Accountant by qualification, he also holds a Diploma in Information Security Audit. He provides financial-controller-level services to the Indian entities of multinational companies and has handled clients from over 30 countries. He focuses on companies setting up in India and on servicing them throughout their business lifecycle, providing a full suite of services including accounting, payroll, tax and regulatory compliances.



Saloni Jhaveri, Director, Business Advisory

With an MBA from the Pennsylvania State University, USA, Saloni is a part of SKP's business advisory arm. With experience in private equity and corporate finance, she has executed several cross-border and domestic transactions involving mergers, acquisitions, joint ventures, private equity funding as well as entry-strategy assignments across sectors such as healthcare, retail, consumer and real estate. She has led deal teams to successfully close transactions involving the preparation and review of financial models and business plans, development of transaction strategy and deal structures.

Chapter 1

Introducing India

At a glance

Location: North of the Equator

(Latitude: 8°4' to 37°6' North; Longitude: 68°7' to 97°25' East)

Capital: New Delhi

Population: 1.27 billion (2014-15 estimate)

Area: 3.3 million sq km

Indian Standard Time: GMT + 5:30

Telephone country code: +91

Official language: Hindi is one of the 22 official languages (English is used for official communication)

Geography and climate¹

Covering an area of 3.3 million square kilometres, India is the seventh largest country in the world, occupying a major portion of the south Asian subcontinent. Extending from the Himalayas in the north, it stretches southwards to the Tropic of Cancer, and tapers off into the Indian Ocean between the Bay of Bengal on the east and the Arabian Sea on the west.

India's climate varies significantly from the permanently snow-capped Himalayas in the north to the tropical south. In spite of much of the north of India lying beyond the tropical zone, the entire country has a tropical climate marked by relatively high temperatures and dry winters. There are four seasons in India: winter (December–February), summer (March–June), south-west monsoons (June–September) and the post-monsoon season (October–November).

Political system²

India is a sovereign socialist secular democratic republic with a parliamentary system of government. It is governed by the Constitution of India, which came into force on 26 January 1950. It has a federal government with 29 states and seven union territories and is the largest democracy in the world. The central/union government is further divided at the state and local levels.

The government is divided into three structural segments: the executive, the legislature and the judiciary.

Executive: The executive branch comprises the President as the head of state, the Vice President and the Council of Ministers. The Council, headed by the Prime Minister, aids and advises the President, who exercises his/her functions accordingly. Thus, the real executive power is vested in the Council of Ministers and the Prime Minister (head of the government). Mr Pranab Mukherjee is the current President of India and Mr Narendra Modi is the Prime Minister.

Legislature: India has a bicameral parliament with the Council of States (Rajya Sabha) and the House of the People (Lok Sabha). Elections to the Lok Sabha are held at an interval of five years, after which the Prime Minister is appointed by the President.

Judiciary: The Supreme Court is the apex body of the Indian legal system, followed by the High Courts and subordinate courts. The judiciary is independent of the executive and legislative branches of the government.

The 16th Lok Sabha elections were held in April–May 2014. The National Democratic Alliance (NDA), which is an alliance of several parties led by the Bharatiya Janata Party (BJP), secured over 300 of the 543 seats. The leading party, BJP, won more than 272 seats, the minimum requirement for a party or alliance to form a government. The former ruling alliance, the United Progressive Alliance, led by the Indian National Congress, secured 58 seats, of which 44 were won by the Congress. Other major political parties in India include the Nationalist Congress Party, Bahujan Samaj Party, Communist Party of India, and the Communist Party of India (Marxist).

¹ National Portal of India, <http://india.gov.in/india-glance/profile>, accessed 30 April 2015

² Ibid.

Legal system³

India has one of the oldest legal systems in the world. The Constitution of India is the supreme law of the country, which gives due recognition to statutes, case laws and customary laws consistent with its dispensations. There is also a vast body of laws known as subordinate legislations in the form of rules, regulations and bylaws made by the central and state governments and local authorities.

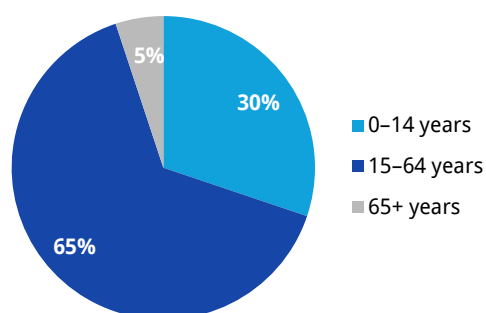
The Constitution has generally provided for a single integrated system of courts to administer both union and state laws. As mentioned previously, the judiciary is divided into various levels, with the courts forming a strict hierarchy of importance: the Supreme Court of India, High Courts (of respective states/groups of states), District Courts and other subordinate courts.

Population

India is currently the second most populous country in the world. Provisional estimates for 2014-15 suggest India's population stands at around 1.27 billion.⁴ It will soon have the largest and youngest workforce the world.⁵ With 65% of the population being in the age range of 15–64 years and a median age of 25.5 years, India has a favourable demographic dividend.

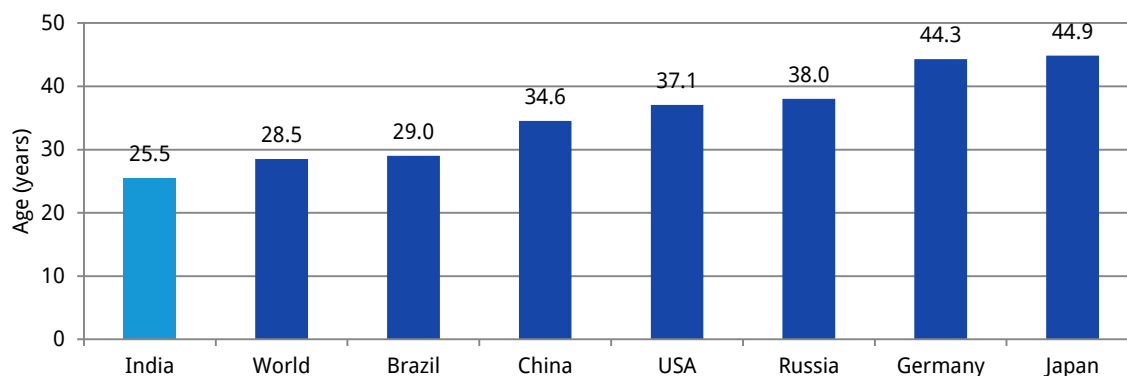
Population distribution by age group: 2010

% share



Median age of the total population: 2010

Years



Source: United Nations, Department of Economic and Social Affairs, Population Division, World Population Prospects: The 2012 Revision

³ Supreme Court of India, <http://supremecourtindia.nic.in/constitution.htm>, accessed 30 April 2015

⁴ Provisional estimates of annual national income, 2014-15, http://mospi.nic.in/Mospi_New/upload/nad_press_release_29may15.pdf, accessed 1 June 2015

⁵ World Bank, India, <http://www.worldbank.org/en/country/india/overview>, accessed 30 April 2015

According to the 2001 census, Hinduism, Islam, Christianity and Sikhism are the four main religions in India. Others include Buddhism, Jainism, Judaism and Zoroastrianism.

Language

While English is used for all official communication across the country, the Constitution of India recognises 22 different languages, of which Hindi is an official language. Other Indian languages recognised by the constitution are Assamese, Bengali, Gujarati, Kannada, Kashmiri, Konkani, Malayalam, Manipuri, Marathi, Nepali, Oriya, Punjabi, Sanskrit, Sindhi, Tamil, Telugu, and Urdu. However, according to the 2001 census, about 30 languages are spoken by more than a million native speakers, and 122 are spoken by more than 10,000 speakers. According to the 2011 census, the literacy rate stands at 74.04% (82.14% for males and 65.46% for females).

Currency

India's currency is the Indian Rupee (ISO code: INR; symbol: ₹). One rupee consists of 100 paise. The Reserve Bank of India, which is the central bank of the country, has the sole authority to issue banknotes and coins.

Business hours

Typically, a work day is 8 hours long from 9am to 5pm IST (GMT + 05:30) and working days vary between 5 to 6 days a week. Business hours could vary from 8 to 10 hours a day depending on the type of the organisation i.e. government, private company, multinational corporation, etc.

Public holidays

India has three national holidays:

- Republic Day – 26 January
- Independence Day – 15 August
- Mahatma Gandhi's Birthday – 2 October

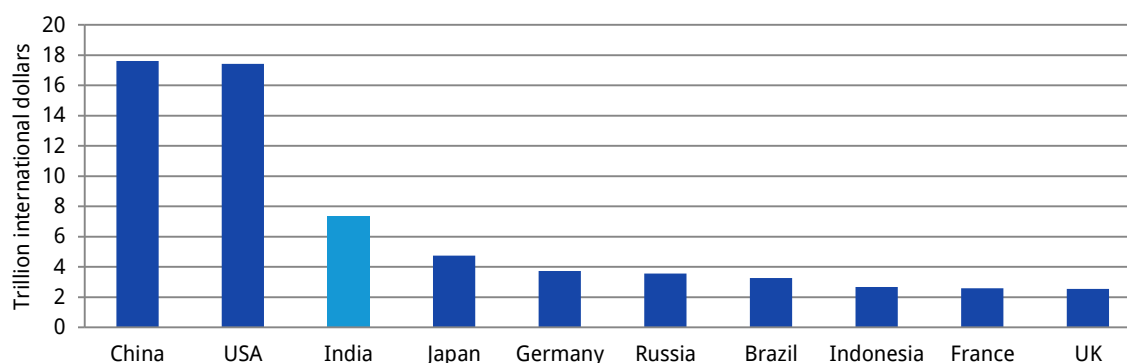
In addition, there are about 15 gazetted holidays and 29 restricted holidays on the official calendar.⁶ These public holidays are set by every state government each year under the Negotiable Instruments Act, 1881.

Economy

India is among the fastest growing economies in the world. It is the third largest economy in terms of gross domestic product (GDP) based on purchasing power parity (PPP) and the tenth largest by nominal GDP.

The world's largest economies by GDP (PPP): 2014

Trillion international dollars



Source: International Monetary Fund, World Economic Outlook Database, April 2015

⁶ Holiday calendar, National Portal of India, <http://india.gov.in/calendar/2015>, accessed 30 April 2015

The services sector has been driving economic growth in India, accounting for 60.6% of GDP in 2014-15, followed by industry with a 23.2% share and agriculture accounting for 16.2%.⁷ However, agriculture still has the largest share in employment (47.1% of the total workforce in 2011-12), followed by services (28.5%).⁸

Well-regulated and stable financial markets, coupled with rising per capita income, a growing middle class, rapid urbanisation, and a strong domestic market (private consumption accounts for 57% of GDP), offer significant promise and potential for investors. India offers opportunities to investors across sectors, including automobiles, chemicals, defence manufacturing, infrastructure, information technology, pharmaceuticals, steel and space technologies among others.

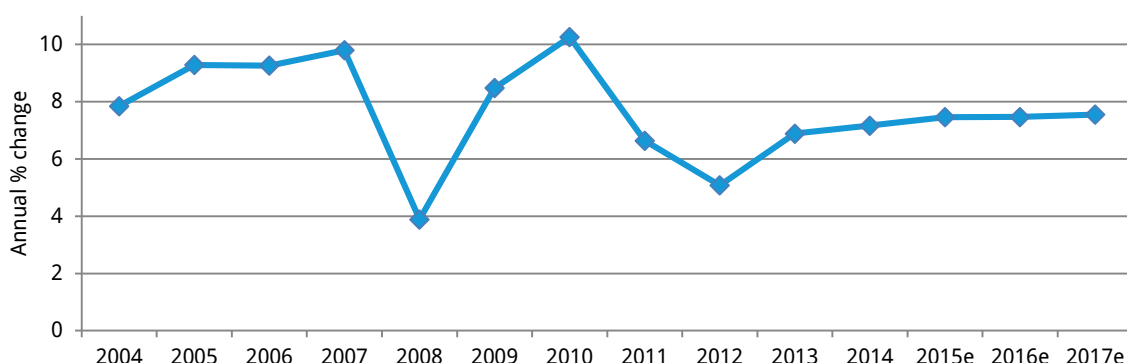
The current business-friendly government's policies are expected to boost foreign investments further as it aims to:

- focus on reviving growth by fuelling investments in infrastructure and manufacturing;
- promote foreign direct investment (FDI) selectively in sectors;
- introduce administrative reforms to expedite project implementation;
- have a stable, predictable and investor-friendly taxation regime;
- increase transparency and establish systems to eliminate corruption; and
- strengthen and expand India's trade network with regional, bilateral and multilateral trade agreements.

According to India's Central Statistics Office, real GDP grew by 7.3% in 2014-15, compared to 6.9% growth in 2013-14.⁹ As a result of recent policy reforms, a consequent pickup in investment, and lower oil prices, India's GDP growth is expected to accelerate to 7.5% by 2015 compared to the slow growth in recent years.¹⁰

Real GDP growth in India: 2004–2017

Annual % change



Source: International Monetary Fund, World Economic Outlook Database, April 2015

Foreign trade: Exports of goods and services accounted for 22.9% of GDP in 2014-15, while imports accounted for 24.2%.¹¹ Exports of services grew by 3.7% to USD 160 billion in 2014-15, and imports of services rose by 4.5% to USD 86 billion in 2014-15.¹² The ratio of exports of services to GDP went up to nearly 9% in 2008-09,

⁷ Reserve Bank of India (RBI) Bulletin, April 2015, <http://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/0BULLEFL10042015.pdf>, accessed 30 April 2015

⁸ Economic Survey 2014-15, Vol.2, <http://indiabudget.nic.in/es2014-15/echapter-vol2.pdf>, accessed 30 April 2015

⁹ Provisional estimates of annual national income, 2014-15, http://mospi.nic.in/Mospi_New/upload/nad_press_release_29may15.pdf, accessed 1 June 2015

¹⁰ World Economic Outlook, April 2015, International Monetary Fund, <http://www.imf.org/external/pubs/ft/weo/2015/01/pdf/text.pdf>, accessed 30 April 2015

¹¹ Provisional estimates of annual national income, 2014-15, http://mospi.nic.in/Mospi_New/upload/nad_press_release_29may15.pdf, accessed 1 June 2015

¹² India's International Trade in Services, RBI, https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=33949, accessed 1 June 2015

while manufacturing exports were less buoyant. After the global financial crisis, however, manufacturing exports seem to have done better than services exports, though both have slowed down in the last five years.¹³ India's top trading partners are China, USA, UAE, Saudi Arabia, Switzerland, Germany, Indonesia, Hong Kong, Korea and Singapore.¹⁴

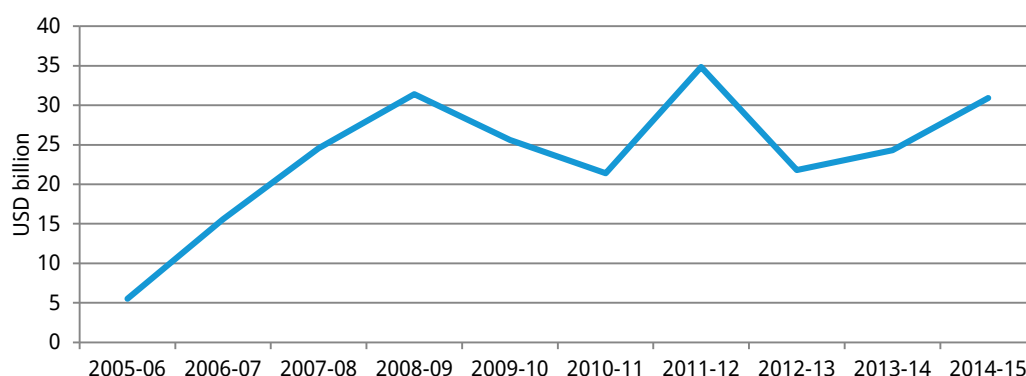
Merchandise exports fell by 0.7% to USD 310 billion in 2014-15, while imports dropped by 0.6% to USD 447 billion, largely driven by a decline in oil prices. However, non-oil exports grew by 1.8% to USD 254 billion and non-oil imports went up by 8.5% to USD 309 billion during the year.¹⁵

India's top export commodities include petroleum products; gems and jewellery; vehicles and parts and accessories; nuclear reactors, boilers, machinery and mechanical appliances; chemicals; pharmaceuticals; cereals; textiles and apparel; iron and steel; and machinery. These account for almost 70% of India's exports. Besides oil imports, which accounted for 31% of India's imports in 2014-15, major import commodities include precious and semi-precious stones; machinery; nuclear reactors, boilers, machinery and mechanical appliances; chemicals; and iron and steel.¹⁶

Foreign direct investment: According to UNCTAD's World Investment Prospects Survey 2013–2015, India is one of the top three destinations for FDI.¹⁷ Cumulative FDI equity inflows into India stood at USD 248 billion during April 2000–March 2015. In 2014-15, FDI equity inflows went up by 27% to USD 30.9 billion, compared to 8% growth in the previous year.¹⁸

Annual FDI equity inflows into India: financial years 2005-06 to 2014-15

USD billion



Source: Department of Industrial Policy and Promotion, FDI Statistics, March 2015

From April 2000 to March 2015, cumulative FDI equity inflows from Mauritius stood at USD 87.5 billion, making it the largest source of FDI into India. In 2014-15, Mauritius was the top investor into India with USD 9.03 billion, followed by Singapore, Netherlands, Japan, USA, UK, Germany, France, Cyprus and UAE.

¹³ Economic Survey 2014-15, Vol. 1, <http://indiabudget.nic.in/es2014-15/echapter-vol1.pdf>, accessed 1 June 2015

¹⁴ Total trade: Top 25 countries, Department of Commerce, <http://www.commerce.nic.in/eidb/iecnttopn.asp>, accessed 1 June 2015

¹⁵ RBI Bulletins, May 2015 and June 2014, https://www.rbi.org.in/scripts/BS_ViewBulletin.aspx, accessed 1 June 2015

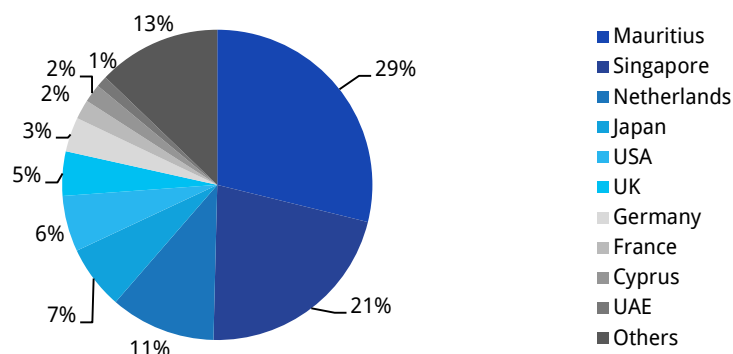
¹⁶ Total trade: Top 25 countries, Department of Commerce, <http://www.commerce.nic.in/eidb/iecnttopn.asp>, accessed 1 June 2015

¹⁷ UNCTAD World Investment Prospects Survey 2013–2015, http://unctad.org/en/PublicationsLibrary/webdiaeia2013d9_en.pdf, accessed 30 April 2015

¹⁸ Department of Industrial Policy and Promotion, Fact Sheet on Foreign Direct Investment, March 2015, http://dipp.nic.in/English/Publications/FDI_Statistics/2015/india_FDI_March2015.pdf, accessed 10 June 2015

Country-wise FDI equity inflows: 2014-15

% share

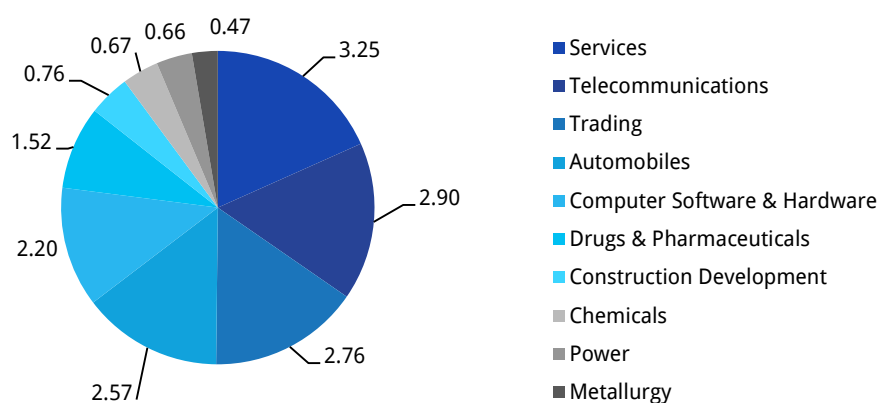


Source: Department of Industrial Policy and Promotion, FDI Statistics, March 2015

Considering sector-wise inflows, services attract the highest amount of FDI in India and accounted for 17% of total inflows during April 2000–March 2015. In 2014-15, besides services (financial and non-financial), the top sectors for FDI were telecommunications, trading, automobiles, computer software and hardware, drugs and pharmaceuticals, construction development, chemicals and power.

Sector-wise FDI equity inflows: 2014-15

USD billion



Source: Department of Industrial Policy and Promotion, FDI Statistics, March 2015

Investments (equity and debt) by foreign portfolio investors saw a dramatic increase to USD 46.2 billion during the year compared to a meagre USD 8.6 billion in 2013-14.¹⁹

As on 5 June 2015, India's foreign exchange reserves stood at USD 352.7 billion.²⁰

For FDI regulations in India, please see the [FDI section in Chapter 2](#).

¹⁹ FPI/FII investment details, NSDL, <https://www.fpi.nsdl.co.in/web/Reports/Yearwise.aspx?RptType=5>, accessed 10 June 2015

²⁰ Foreign Exchange Reserves, Weekly Statistical Supplement, RBI, <https://www.rbi.org.in/scripts/WSSView.aspx?Id=19884>, accessed 15 June 2015

Chapter 2

Government policies and business regulatory environment

Business regulations

Companies Act

The Ministry of Corporate Affairs (MCA) regulates corporate affairs in India through the Companies Act, 1956, 2013 and other allied Acts, Bills and Rules. Companies incorporated in India or foreign companies having a place of business in India are regulated by the Companies Act, 1956 and 2013 (to the extent notified). The new Act consolidates and amends the law relating to companies. Some of the provisions of the new Act have been implemented while some provisions of the Companies Act, 1956 are still in force.

The Registrar of Companies (ROC), Company Law Board (CLB) and National Company Law Tribunal (NCLT) are responsible to administer the Act and to ensure compliance. Following the constitution of NCLT, the CLB will cease to exist and all the powers of CLB will be vested in the NCLT. Companies are broadly classified into public and private companies. A public company may further be listed or unlisted. Listed public companies have to additionally comply with the regulations issued by the Securities and Exchange Board of India (SEBI).

The Industrial Policy, 1991 looks at industrial licensing, foreign investment, foreign technology agreements, public sector policy, and the Monopolies and Restrictive Trade Practices (MRTP) Act, 1969.²¹ States have their own industrial policies that may have different focus areas.

Foreign direct investment²²

A foreign company planning to set up business operations in India can incorporate a company under the Companies Act as a joint venture or a wholly owned subsidiary. A foreign company could also set up a liaison office/representative office, project office or branch office of the foreign company, which can undertake activities permitted under the Foreign Exchange Management (Establishment in India of Branch Office or Other Place of Business) Regulations, 2000. A foreign company may also invest in a limited liability partnership (LLP) under the Limited Liability Partnership Act, 2008, a relatively new but popular concept in India. Please also see [Chapter 4 Business entities](#).

An Indian company may receive foreign direct investment (FDI) under the automatic route or the government (approval) route. FDI is allowed under the automatic route without prior approval either of the government or of the Reserve Bank of India (RBI) in all activities/sectors as specified in the Consolidated FDI Policy Circular issued by the Indian government from time to time. The latest Circular came into effect on 12 May 2015.²³

FDI in activities under the government route is considered by the Foreign Investment Promotion Board (FIPB) under the Ministry of Finance. An Indian company receiving FDI is required to comply with other provisions of the FDI Policy such as reporting requirements, allotment of securities and pricing guidelines.

FDI is prohibited in atomic energy, lottery business, gambling and betting, business of chit fund, Nidhi company, agriculture (excluding floriculture, horticulture, development of seeds, animal husbandry, pisciculture and cultivation of vegetables, mushrooms, etc. under controlled conditions and services related to agro and allied sectors) and plantation activities (other than tea plantations), housing and real estate business (except development of townships, construction of residential/commercial premises, roads or bridges), trading in Transferable Development Rights (TDRs), manufacture of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes.

Depending on the nature of business to be carried out by the Indian entity, specific registrations, approvals and licences such as Permanent Account Number (PAN), Tax Account Number (TAN), Shops and Establishments registration/Factories licence, Central Sales Tax and Value Added Tax (VAT) registrations, excise registration, Import Export Code (IEC) are required to be obtained.

²¹ Industrial Policy Highlights, Office of the Economic Adviser, http://www.eaindustry.nic.in/industrial_handbook_200809.pdf, accessed 30 April 2015

²² Foreign Investments in India, RBI, <http://www.rbi.org.in/scripts/FAQView.aspx?Id=26>, accessed 30 April 2015

²³ Consolidated FDI Policy 2015, DIPP, http://dipp.nic.in/English/policies/FDI_Circular_2015.pdf, accessed 15 June 2015

Recent policy measures include allowing 100% FDI in telecommunications, medical devices, single-brand retail and asset reconstruction companies. Now, 100% FDI in the construction, operation and maintenance of railways is also allowed under the automatic route. The FDI cap for insurance and defence was raised from 26% to 49% and that for credit information was raised to 74%.²⁴ While 100% FDI is allowed in business-to-business (B2B) e-commerce, FDI is not permitted in the business-to-consumer (retail) segment yet. FDI norms for the construction development sector were also eased.²⁵

FDI in several services that was previously permitted only through the government route now fall under the automatic route. These include commodity exchanges, stock exchanges and depositories, power exchanges, petroleum refining by public sector units and courier services.

Government agencies supporting business growth

The Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce & Industry, is the main government agency that facilitates investment and technology flows by formulating and implementing policies and monitors industrial development in India. Other agencies include state industrial corporations, investor facilitation centres, and bilateral chambers of commerce.

Invest India is the country's official agency dedicated to investment promotion and facilitation. Set up as a joint venture between the Federation of Indian Chambers of Commerce and Industry (FICCI) (51% equity), DIPP (35% equity) and state governments of India (0.5% each), its mandate is to become the first reference point for global investors considering entering India. It provides sector- and state-specific information to foreign investors, assists in expediting regulatory approvals, and offers hand-holding services.²⁶

eBiz is India's government-to-business (G2B) online portal aimed at creating an investor-friendly business environment in India by making all regulatory information – starting from the establishment of a business, through its ongoing operations, and even closure – easily available to various stakeholders. It aims to develop a transparent, efficient and convenient interface through which the government and businesses can interact, reducing delays in various regulatory processes required to start and run businesses.²⁷ It is a single-window portal to apply for and obtain clearances from various government agencies. eBiz has integrated 14 services including the application for an Industrial Licence and Industrial Entrepreneur Memorandum.²⁸

The 'Make in India' campaign

In September 2014, the government launched the 'Make in India' campaign, focusing on initiatives to facilitate investments into India and promoting it as a global manufacturing hub. The scheme aims to improve the ease of doing business in India by reducing red tape, improving infrastructure, opening up more sectors to FDI, and most importantly, changing the mindset of the government being a 'permit-issuing authority' to a true business partner. With the large amount of FDI expected to come in, factors such as regulations, infrastructure, skill development, technology, financing, etc. that are critical for manufacturing have been scrutinised.

The government has identified 25 sectors, including automobiles, aviation, biotechnology, chemicals, construction, defence, etc., details for which are available on www.makeinindia.com. Ministries related to these industries are working on sector-specific targets with action plans for the next one year and three years.

Several initiatives have already been undertaken to improve the business environment. New de-licensing and deregulation measures are reducing complexity and increasing speed and transparency. Now applications for industrial licences can be made at any time through eBiz. Also, their validity has been extended from two years to three years, giving adequate time to procure land and get the necessary clearances from authorities. India's

²⁴ Foreign Direct Investment, Make in India, <http://www.makeinindia.com/policy/foreign-direct-investment/>, accessed 15 June 2015

²⁵ Consolidated FDI Policy 2015, DIPP, http://dipp.nic.in/English/policies/FDI_Circular_2015.pdf, accessed 15 June 2015

²⁶ Invest India, <http://www.investindia.gov.in>, accessed 15 June 2015

²⁷ eBiz, India's G2B portal, <https://www.ebiz.gov.in/aboutus>, accessed 15 June 2015

²⁸ Major Initiatives on Improving Ease of Doing Business in India, DIPP, http://dipp.nic.in/English/Investor/EoDB_Initiatives_01June2015.pdf, accessed 15 June 2015

manufacturing infrastructure is poised for phenomenal growth with smart cities and industrial corridors being developed. Youth-focused programmes and institutions are dedicated to developing specialised skills. Innovation is being encouraged through better management of patent and trademark registration.²⁹

The campaign aims to achieve an increase in manufacturing sector growth to 12–14% per year, an increase in the share of manufacturing in the country's GDP from 16% to 25% by 2022, and create 100 million additional jobs by 2022 in the manufacturing sector alone.³⁰

Invest India will act as the first reference point for guiding foreign investors on all aspects of regulatory and policy issues and assist them in obtaining regulatory clearances. Its dedicated Investor Facilitation Cell will answer queries of business entities within 72 hours.

Government incentives and assistance

Industry-specific incentives: These are available to promote specific industries in India, which include agriculture, food processing, textile, power and infrastructure. These incentives can be governed by both central and state government legislation and mainly provide capital and interest subsidies for investments in specified industries.

State-level incentives: These are governed by state industrial policies and depend on the amount of investment and location of the industrial project. The incentives are mainly in the form of a VAT/Central Sales Tax refund, interest subsidies, power tariff/electricity duty exemptions, stamp duty exemptions, etc.

Trade policy and import and export controls

In India, exports and imports are regulated by the Foreign Trade (Development and Regulation) Act, 1992 and the Foreign Trade Policy. The Department of Commerce, Ministry of Commerce & Industry, formulates, implements and monitors the policy. The Directorate General of Foreign Trade (DGFT) runs various schemes for trade promotion and facilitation.

The new Foreign Trade Policy 2015–2020 (FTP) was announced on 1 April 2015. It provides a framework for foreign trade in goods and services as well as employment generation and increasing value addition. It aims to link rules, procedures and incentives for exports and imports with other initiatives such as Make in India and Digital India to create an 'Export Promotion Mission', which will provide an institutional framework to work with state governments to boost India's exports. The focus of the new policy is to support both the manufacturing and services sectors, with a special emphasis on improving the ease of doing business in India.

Some key features of the new FTP are as follows:³¹

- The FTP introduces two new schemes, Merchandise Exports from India Scheme (MEIS) for export of specified goods to specified markets and Services Exports from India Scheme (SEIS) for increasing exports of notified services, in place of a plethora of schemes earlier. Duty credit scrips issued under these schemes and the goods imported against them are fully transferable.
- The number of mandatory documents required for exports and imports have been reduced to three, which is comparable with international standards.
- Measures have been taken to boost exports of defence and hi-tech items.
- Manufacturers (who are also status holders) will now be able to self-certify their manufactured goods in phases, as originating from India with a view to qualifying for preferential treatment under bilateral and regional trade agreements. This 'Approved Exporter System' will help these manufacturer exporters in getting fast access to international markets.

²⁹ Press release: Meeting challenges of 'Make In India' campaign, <http://pib.nic.in/newsite/PrintRelease.aspx?relid=121224>, accessed 19 June 2015

³⁰ Press release: Make in India: A lion's step to boost manufacturing <http://www.pib.nic.in/newsite/efeatures.aspx?relid=110166>, accessed 19 June 2015

³¹ Press release: Foreign Trade Policy 2015-2020 unveiled, Ministry of Commerce, <http://pib.nic.in/newsite/PrintRelease.aspx?relid=117917>, accessed 15 June 2015

- 108 micro, small and medium enterprise (MSME) clusters have been identified for focused interventions to boost exports.
- Several steps are being taken to move towards a paperless/digital environment. A robust electronic data interchange (EDI) system has been set up to facilitate overall ease of exports and good governance. Various documentation-related activities including import and export authorisations requiring interacting with other administrative departments, such as customs, banks and export promotion councils (EPCs) can be done online. This has reduced the physical interaction of exporters and importers with the government and will help reduce transaction costs.

Free Trade Agreements (FTAs) are an important element of India's trade strategy. A web portal on FTAs, indiantradeportal.in, provides both most-favoured nation and preferential tariff rates, rules of origin, sanitary and phytosanitary (SPS) standards and technical barriers to trade (TBT) under various FTAs signed by India. It also captures the trade flows from major trading partners. As preferential imports account for only a small part of total imports, utilisation of FTAs must be improved to derive maximum benefits. A comprehensive list of India's FTAs can be viewed on the Department of Commerce's website, commerce.nic.in/trade/international_ta.asp.

Export incentives: Special Economic Zones (SEZs) and Export Oriented Units (EOUs): The SEZ Act, 2005 aims at attracting larger foreign investments into India by providing quality infrastructure complemented by an attractive fiscal package at the centre and the state level, with minimal regulations. This Act along with the SEZ Rules drastically simplified procedures and provided for single-window clearance on matters related to the central and state governments.³² Incentives provided to units in an SEZ differ from state to state but may include duty-free imports of specified goods, exemptions from income tax, service tax, Central Sales Tax, Minimum Alternate Tax, etc.³³ The government has decided to extend benefits of both the MEIS and SEIS reward schemes to units located in SEZs as well.

Units undertaking to export their entire production of goods and services may be set up under the EOU Scheme, Electronics Hardware Technology Park (EHTP) Scheme, Software Technology Park (STP) Scheme or Bio-76Technology Park (BTP) Scheme for manufacture of goods, including repair, re-making, reconditioning, reengineering, rendering of services, agriculture, etc. 100% FDI is permitted through the automatic route, similar to SEZ units.³⁴

In order to encourage manufacturing and exports under the 100% EOU/EHTP/STPI/BTP schemes, these units have been provided with a fast-track clearance facility, and are allowed to share infrastructure, transfer goods and services between units, set up warehouses near the port of export, and use duty-free equipment for training.

The Export Promotion Capital Goods (EPCG) Scheme allows the import of capital goods for pre-production, production and post-production at zero customs duty. Measures have been adopted to increase procurement of capital goods from indigenous manufacturers under this scheme by reducing the specific export obligation from 90% to 75% of the normal export obligation.³⁵

Duty exemption schemes enable duty-free import of inputs required for export production. These include Advance Authorisation and Duty-Free Import Authorisation (DFIA). A duty remission scheme enables post-export replenishment/remission of duty on inputs used in export products and includes the Duty Drawback (DBK) Scheme.

Customs regulations: The Customs Act, 1962 provides for levy and collection of customs duty on imports and exports, import/export procedures, prohibitions on trade of certain goods, penalties, offences, etc. The central

³² Special Economic Zones in India, <http://sezindia.nic.in/about-introduction.asp>, accessed 15 June 2015

³³ Facilities and Incentives, SEZs in India, <http://www.sezindia.nic.in/about-fi.asp>, accessed 15 June 2015

³⁴ Foreign Trade Policy 2015–2020, <http://dgft.gov.in/exim/2000/ftp2015-20E.pdf>, accessed 15 June 2015

³⁵ Ibid.

government levies customs duty on import and export of goods at the rates and on the basis of classification under the Customs Tariff Act, 1975. The Central Board of Excise and Customs (CBEC) is the apex body that deals with the formulation of policy concerning the levy and collection of customs and central excise duties, prevention of smuggling and administration of matters relating to customs, central excise, service tax and narcotics to the extent under CBEC's purview.³⁶ The Customs/Import tariff for various goods can be viewed on the CBEC website.

Bank accounts

India has a well-developed banking system regulated by the Reserve Bank of India (RBI). Established in 1935, the RBI is the central bank of India. The RBI regulates the issue of bank notes and keeping of reserves, controls the credit system, regulates and supervises the financial system, regulates foreign exchange, acts as banker to governments and to other commercial banks and plays a developmental and promotional role in the banking system. Public and private sector banks coexist in India and are subject to the control and supervision of the RBI. The Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949 are the core legislations pertaining to the banking sector in India.³⁷

A foreign company setting up in India typically opens a current (checking) account with an Authorised Dealer (AD) bank. An AD bank functions under the direction and supervision of the RBI and handles both current and capital account transactions. Current account transactions such as payments in the course of foreign trade and banking and credit facilities in the ordinary course of business are usually freely permitted. Capital account transactions such as transfer or issue of any foreign security by an Indian resident, transfer or issue of security by a non-resident, any borrowing or lending, acquisition of immovable property by a non-resident and giving of a guarantee in respect of a debt or liability are regulated by the RBI.³⁸ The ease with which banking account transactions can be carried out is also dependent on whether an entity is operating under the automatic route or government route.

Intellectual property

Internationally, India is a member of the World Trade Organisation and committed to the Agreement on Trade Related Aspects of Intellectual Property (TRIPS). India is also a member of the World Intellectual Property Organization (WIPO), a body responsible for the promotion of protection of intellectual property rights throughout the world. India is also a signatory to several important WIPO-administered international treaties and conventions related to intellectual property.³⁹

Acts covering intellectual property in India include the Patents Act, 1970 (as amended in 2005); Copyright Act, 1957 (as amended); Trade Marks Act, 1999 (as amended in 2010); Designs Act, 2000; and Geographical Indications of Goods (Registration & Protection) Act, 1999. Intellectual property needs to be registered with the Controller General of Patents, Designs and Trademarks.⁴⁰

Patents

Patent law in India is governed by the Patents Act, 1970 as amended by the Patents (Amendment) Act, 2005 and the Patents Rules, 2003 as amended by the Patents (Amendment) Rules, 2006. Under the Patents Act, 1970, any invention that has the following three essential ingredients may be patented:

- Novelty
- Utility/usefulness
- Non-obviousness/inventive step

³⁶ Central Board of Excise and Customs, <http://www.cbec.gov.in/whoweare/whoweare.htm>, accessed 15 June 2015

³⁷ About Us, RBI, <http://www.rbi.org.in/scripts/AboutusDisplay.aspx>, accessed 9 June 2015

³⁸ Ministry of Finance, http://finmin.nic.in/the_ministry/dept_eco_affairs/capital_market_div/FEMA_act_1999.pdf, accessed 9 June 2015

³⁹ Intellectual Property Facts, Make in India, <http://www.makeinindia.com/policy/intellectual-property-rights/>, accessed 9 June 2015

⁴⁰ Controller General of Patents, Designs and Trademarks, <http://www.ipindia.nic.in/>, accessed 9 June 2015

Normally, a patent obtained in India is not enforceable in another country as patent protection is a territorial right. However, India is a signatory to the Patent Cooperation Treaty (PCT), under which applicants can file a single international patent application and simultaneously seek protection for an invention in 148 countries under the PCT.⁴¹

India is also a signatory to the Paris Convention for the Protection of Industrial Property. The Convention provides for the right of priority, due to which based on a regular first application filed in one of the contracting states, the applicant may, within a certain period of time, apply for protection in any of the other contracting states. The applicant will have priority over other states during that period.⁴²

India follows a first-to-file patent system. A patent application can be filed either by the true and first inventor or his/her assignee, either alone or jointly with any other person, or the legal representative of a deceased person.⁴³ An applicant can file a patent application if they have a place of residence, business or domicile in India. A patent application can be filed with the Patent Office at any of its four locations, Kolkata, Delhi, Chennai and Mumbai, depending on territorial jurisdiction. The Patent office also accepts applications online through its website, www.ipindia.nic.in.⁴⁴ Foreign applicants who do not have a place of business in India can file their applications through an Indian patent agent.

The term of a patent is 20 years from the date of application. A renewal fee has to be paid every year to keep the patent valid for the term of 20 years.⁴⁵

The Patents Act, 1970 provides for the enforcement of patents by way of suits on infringement. The patentee may file an action for patent infringement in either a District Court or a High Court. The relief that a court may grant in any suit for infringement includes an injunction and, at the option of the patentee, either damages or an account of profits. The court may also order that the infringing goods be seized, forfeited or destroyed without payment of any compensation.

Copyright

The Copyright Act, 1957 protects original literary, dramatic, musical and artistic works and cinematograph films and sound recordings from unauthorised use. Unlike patents, copyright protects the expression and not ideas. There is no copyright protection for ideas, procedures, methods of operation or mathematical concepts as such. It is not necessary to register a work to claim copyright in India. Acquisition of copyright is automatic – it comes into existence as soon as a work is created and requires no formalities. However, a certificate of registration of copyright and the entries made therein serve as prima facie evidence in a court of law with reference to disputes on ownership of copyright. The Copyright Office has been set up to provide registration facilities to all types of works and is headed by a Registrar of Copyrights. The Copyright (Amendment) Act, 2012 extends copyright protection in the digital environment, ensuring the right to receive royalties for authors, and music composers, exclusive economic and moral rights to performers, equal membership rights in copyright societies for authors and other right owners, and exception of copyrights for the physically disabled to access any works.⁴⁶

Trademarks

Under the Trade Marks Act, 1999, a person who is the proprietor of the trademark can apply to the Registrar of Trade Marks for the registration of its mark for goods and services. A trademark is a mark capable of being

⁴¹ World Intellectual Property Organization, <http://www.wipo.int/pct/en/>, accessed 27 May 2015

⁴² World Intellectual Property Organization, http://www.wipo.int/treaties/en/ip/paris/summary_paris.html, accessed 27 May 2015

⁴³ Patent FAQs, Controller General of Patents, Designs and Trademarks, http://ipindia.nic.in/ipr/patent/faq_patent.htm, accessed 27 May 2015

⁴⁴ Filing of Patent Applications, <http://www.ipindia.nic.in/ipr/patent/manual/HTML%20AND%20PDF/Manual%20of%20Patent%20Office%20Practice%20and%20Procedure%20-%20html/Chapter%203.htm>, accessed 27 May 2015

⁴⁵ Patent FAQs, Controller General of Patents, Designs and Trademarks, http://ipindia.nic.in/ipr/patent/faq_patent.htm, accessed 27 May 2015

⁴⁶ Copyright Office, <http://copyright.gov.in>, accessed 27 May 2015

represented graphically and which is capable of distinguishing the goods or services of one person from those of another. The 'Mark' includes a device, brand, heading, label, ticket, name, signature, word, letter, numeral, shape of goods, packaging or combination of colours or any combination thereof.⁴⁷

Design⁴⁸

The essential purpose of design law is to promote and protect the design element of industrial production. It is also intended to promote innovative activity in industries. The existing legislation on industrial designs in India is contained in the New Designs Act, 2000.

The essential requirements for the registration of a 'design' under the Designs Act, 2000 are as follows:

- The design should be new or original, not previously published or used in any country before the date of application for registration.
- The design should relate to features of shape, configuration, pattern or ornamentation applied or applicable to an article.
- The design should be applied to any article by any industrial process.
- The features of the design in the finished article should appeal to and be judged solely by the eye.
- Any mode or principle of construction or operation or any thing which is in substance a mere mechanical device cannot be registered as a design.
- The design should not include any trademark or property mark or artistic works as defined under the Copyright Act, 1957.

The registration of a design confers upon the registered proprietor a 'copyright' on the design for the period of registration. It gives the proprietor the exclusive right to apply it to any article in the registered class. A registered proprietor of the design is entitled to a better protection of his intellectual property. He can sue for infringement (recoverable amount cannot exceed INR 50,000), and licence or sell his design as legal property for a consideration or royalty.

Any person (including a firm, partnership or body corporate) claiming to be the proprietor of the design can apply for its registration. The application can be filed by the applicant directly or through an agent. The duration of the registration of a design is initially 10 years from the date of registration, which may be extended by five years through the relevant application.

Geographical indications

Geographical indications are covered as an element of intellectual property under the Paris Convention as well as the TRIPS agreement. A geographical indication identifies agricultural or natural or manufactured goods as originating or manufactured in the territory of a country or region or locality in that territory, where a given quality, reputation or other characteristic of such goods is essentially attributable to its geographical origin and in case where such goods are manufactured goods one of the activities of either. The production or of processing of preparation of the goods concerned takes place in such territory, region, or locality as the case may be. The Geographical Indications of Goods (Registration & Protection) Act, 1999 is the relevant Act in India.⁴⁹

Privacy

The Indian Constitution does not expressly guarantee the right to privacy, but the Supreme Court of India has time and again protected the right to privacy by reading it into the fundamental right to life and personal liberty available to all persons. Privacy rules in India are contained in the Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Data or Information) Rules, 2011 (Privacy Rules) notified under

⁴⁷ Controller General of Patents, Designs and Trademarks, http://ipindia.nic.in/tmr_new/tmr_act_rules/TMRAct_New.pdf, accessed 27 May 2015

⁴⁸ Designs, Controller General of Patents, Designs and Trademarks, <http://www.ipindia.nic.in/>, accessed 27 May 2015

⁴⁹ Geographical indications, Make in India, <http://www.makeinindia.com/policy/intellectual-property-rights/>, accessed 8 June 2015

the Information Technology Act, 2000. The Privacy Rules are applicable to bodies corporate across industries and sectors.

Under the Privacy Rules, a body corporate handling or collecting personal information from any person is required to:

- provide a privacy policy and make it accessible to the providers of information;
- have in place reasonable security practices and procedures;
- obtain consent from the providers of information regarding use of such personal information;
- use the personal information only for the purposes for which it has been collected;
- retain information only for such time period as may be required;
- keep the information secure and not publish it;
- obtain permission of the provider of information prior to disclosure of such information unless required to be disclosed by law or to certain government agencies.
- take reasonable steps while collecting information directly from the person concerned to ensure that the person concerned is having the knowledge of:
 - the fact that the information is being collected;
 - the purpose for which the information is being collected;
 - the intended recipients of the information; and
 - the name and address of (i) the agency that is collecting the information; and (ii) the agency that will retain the information
- permit the providers of information, as and when requested by them, to review the information they had provided and ensure that any personal information or sensitive personal data or information found to be inaccurate or deficient is corrected or amended as feasible;
- provide an option to the provider of information to not provide the data or information sought to be collected or to withdraw the consent given earlier. In such cases, the body corporate shall have the option of not providing goods or services for which the said information was sought; and
- address any discrepancies and grievances of the provider of information with respect to processing of information in a timely manner. For this purpose, the body corporate has to designate a Grievance Officer and publish his name and contact details on its website. The Grievance Officer will have to redress the grievances of provider of information expeditiously, within one month from the date of receipt of grievance.⁵⁰

Certain industries where technology and data transfer are critical are closely monitored by the government. E.g. [licenced defence industries in the private sector](#).

Mergers and monopolies

Mergers: Mergers are a popular form of corporate restructuring in India. The Companies Act, 2013, the Company Court Rules, the Income Tax Act, 1961, the Indian Stamp Act, 1899 and the Competition Act, 2002 are the key regulations concerning mergers. Public companies have to additionally comply with the regulations issued by SEBI. Companies that have foreign capital will have to meet the requirements under FEMA.

A merger in India typically needs to be sanctioned by the court (tribunal under the new Companies Act, 2013) and requires, in most cases, reports from the offices of the Registrar of Companies, Official Liquidator and Regional Director under the Ministry of Corporate Affairs. The RBI would administer the provisions relating to mergers under FEMA. Valuation, accounting treatment and stamp duty are other critical aspects of a merger.

⁵⁰ Department of Electronics & Information Technology, [http://deity.gov.in/sites/upload_files/dit/files/GSR313E_10511\(1\).pdf](http://deity.gov.in/sites/upload_files/dit/files/GSR313E_10511(1).pdf), accessed 8 June 2015

Monopolies: The erstwhile Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act) controlled monopolies and prohibited monopolistic and restrictive trade practices in India. The MRTP Act was completely replaced by the Competition Act, 2002 with effect from 1 September 2009.

The Competition Act moved away from the earlier emphasis of curbing monopolies towards promoting and sustaining competition to enhance consumer welfare and support economic growth. Accordingly, the Competition Commission of India (CCI) was constituted to eliminate practices having an adverse effect on competition; promote and sustain competition; protect interests of consumers; and ensure freedom of trade in markets through the enforcement of competition law. The Act prohibits anti-competitive agreements, regulates abuse of one's dominant position, and regulates mergers and acquisitions that cross prescribed thresholds.⁵¹

Consumer protection

The Department of Consumer Affairs, Ministry of Consumer Affairs, Food and Public Distribution, is responsible for the formulation of policies for consumer cooperatives, monitoring prices, the consumer movement in the country and controlling statutory bodies, including the Bureau of Indian Standards (BIS) and Weights and Measures.⁵²

The Consumer Protection Act, 1986 is a social legislation that lays down the rights of consumers and provides for the promotion and protection of consumer rights in India. The provisions of this Act cover 'goods' as well as 'services'. Goods covered are those that are manufactured or produced and sold to consumers through wholesalers and retailers. Services include transport, telephone, electricity, housing, banking, insurance, medical treatment, etc. The remedy available under the Consumer Protection Act is in addition to that already available to an aggrieved consumer by way of civil suit.

To provide inexpensive and speedy redressal of consumer disputes, quasi-judicial bodies have been set up in each district, state and at the national level, called District Forums, State Consumer Disputes Redressal Commissions and the National Consumer Disputes Redressal Commission, respectively. Also, aggrieved consumers can file their complaints with Consumer Forums that can award compensation and provide other relief to the consumer.⁵³ They could also call the toll-free National Consumer Helpline on 1800-11-4000.⁵⁴

Building regulations

The National Building Code of India, 2005 (NBC) is a comprehensive building code providing guidelines for regulating building construction activities across the country. It serves as a model code for adoption by all agencies involved in building construction, such as Public Works Departments, construction departments, local bodies or private construction agencies. The NBC mainly contains administrative regulations, development control rules and general building requirements; fire safety requirements; stipulations regarding building materials, structural design and construction (including safety); and building and plumbing services.⁵⁵ Local bylaws are also formulated and adopted by state governments, urban local bodies and development authorities to regulate construction activities in the area that they are framed for.

Environment, pollution and waste management

There are various laws governing environmental and pollution control matters, including the Water (Prevention and Control of Pollution) Act, 1974; the Air (Prevention and Control of Pollution) Act, 1981; Environment (Protection) Act, 1986; the Biomedical Waste Management & Handling) Rules, 1998; the Manufacture, Storage and Import of Hazardous Chemicals Rules, 1989; and the Hazardous Waste (Management, Handling and Transboundary Movement) Rules, 2008. Contravention of the above acts attracts a fine and imprisonment. The Ministry of Environment, Forest and Climate Change (MoEFCC) is the nodal agency of the central government

⁵¹ Annual Report 2013-14, CCI, <http://www.cci.gov.in/May2011/Advocacy/ar2014.pdf>, accessed 8 June 2015

⁵² Department of Consumer Affairs, <http://consumeraffairs.nic.in/Home.aspx>, accessed 8 June 2015

⁵³ National Consumer Disputes Redressal Commission, <http://ncdr.nic.in>, accessed 8 June 2015

⁵⁴ National Consumer Helpline, <http://www.nationalconsumerhelpline.in/>, accessed 8 June 2015

⁵⁵ National Building Code of India, 2005, <http://www.bis.org.in/sf/nbc.htm>, accessed 8 June 2015

for planning, promoting, coordinating and overseeing the implementation of India's environmental and forestry policies and programmes.⁵⁶ The process of applying for environment and forest clearances has been made online through the MoEFCC's portals environmentclearance.nic.in and forestsclearance.nic.in.

In India, the Public Liability Insurance Act, 1991 applies to all owners associated with the production or handling of any hazardous chemicals. It provides for damages to victims of an accident that occurs as a result of handling any hazardous substance.⁵⁷

The Central Pollution Control Board (CPCB) is a statutory organisation under the MoEFCC that advises the central government on any matter concerning the prevention and control of water and air pollution and coordinates the activities of the State Pollution Control Boards (SPCB) among other things.⁵⁸ Each SPCB provides detailed guidelines for necessary approvals and conditions required for setting up operations in the state.

Recent developments⁵⁹

- The DIPP has requested all Secretaries of the government and Chief Secretaries of the states to simplify and rationalise the regulatory environment with the following measures:
 - All returns should be filed online through a single form;
 - A checklist of required compliances should be placed on the DIPP website;
 - All registers required to be maintained by the business should be replaced with a single electronic register;
 - No inspection should be undertaken without the approval of the Head of the Department; and
 - A system of self-certification should be introduced for all non-risk, non-hazardous businesses.
- Six best practices were identified following a comparative study of practices followed by the states for granting clearance and ensuring compliances. These were circulated among all states for peer evaluation and adoption. The study also identified important bottlenecks faced by industries and important steps required to improve the business environment in states.

⁵⁶ Ministry of Environment, Forest and Climate Change, <http://envfor.nic.in/about-ministry/about-ministry>, accessed 8 June 2015

⁵⁷ Public Liability Insurance, Ministry of Environment & Forests, <http://envfor.nic.in/rules-regulations/public-liability-insurance>, accessed 8 June 2015

⁵⁸ Central Pollution Control Board, <http://cpcb.nic.in/Functions.php>, accessed 8 June 2015

⁵⁹ Major Initiatives on Improving Ease of Doing Business in India, DIPP, http://dipp.nic.in/English/Investor/EoDB_Initiatives_01June2015.pdf, accessed 15 June 2015

Chapter 3

Banking and finance

The banking system

The banking and financial sector in India functions under the superintendence and control of the central bank of the country, the Reserve Bank of India (RBI). It was established in 1935 with the main aim of maintaining monetary and financial stability.

The RBI performs the following functions⁶⁰:

Monetary authority

- Formulates, implements and monitors the monetary policy.
- Objective: maintaining price stability and ensuring adequate flow of credit to productive sectors.

Regulator and supervisor of the financial system

- Prescribes a broad operational framework for the country's banking and financial system.
- Objective: to maintain public confidence in the system, protect depositors' interests and provide cost-effective banking services.

Manager of foreign exchange

- Manages the Foreign Exchange Management Act, 1999.
- Objective: to facilitate external trade and payment, and promote orderly development and maintenance of the foreign exchange market in India.

Issuer of currency

- Issues and exchanges/destroys currency and coins not fit for circulation.

Other functions

- Banker and debt manager to the government: performs merchant banking function for the central and state governments; also acts as their banker.
- Banker to banks: maintains banking accounts of all scheduled banks.

Existing banking structure⁶¹

Different departments of the RBI oversee the various entities that comprise India's financial infrastructure, such as commercial banks, financial institutions, cooperative banks, and non-banking financial companies.

Types of banks	Number of banks
Public sector banks	26
Private Indian banks	23
Private foreign banks	43
Regional rural banks	56
Scheduled urban cooperative banks	50
Non-scheduled urban cooperative banks	1531
District cooperatives	366
Scheduled state cooperatives	18
Non-scheduled state cooperatives	14

Legal framework⁶²

The primary acts governing this sector are the Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949 (also the Banking Laws (Amendment) Act, 2012). Several other Acts govern specific functions (e.g. the Foreign Exchange Management Act, 1999), banking operations and individual institutions.

⁶⁰ About Us, RBI, <https://www.rbi.org.in/Scripts/AboutusDisplay.aspx#ME>, accessed 2 June 2015

⁶¹ Banks in India, RBI, <https://rbi.org.in/commonman/English/Scripts/BanksInIndia.aspx>, accessed 2 June 2015

⁶² About Us, RBI, <https://www.rbi.org.in/Scripts/AboutusDisplay.aspx#LF>, accessed 2 June 2015

Setting up a bank in India⁶³

The Banking Regulation Act, 1949 provides that a company intending to carry on banking business must obtain a licence from the RBI except for those banks (public sector banks and regional rural banks) that are established under specific enactments.

The RBI issues licences only after 'tests of entry' are fulfilled. These tests include minimum capital requirements, ownership structure, operating plans and controls, ability of the bank to pay its present and future depositors in full, quality of management and whether the licensing of the bank would be in public interest.⁶⁴ Currently, the minimum paid-up capital requirement for setting up a bank is INR 5 billion.

Foreign banks in India⁶⁵

With increasing globalisation, the presence of foreign banks must expand, particularly because they specialise in providing sophisticated financial products and facilitate the flow of foreign capital. Their increased presence would meet the requirements of the growing Indian economy.

Currently, foreign banks can operate in India through branches, by setting up a wholly owned subsidiary (WOS), or a subsidiary with aggregate foreign investment up to 74% of paid-up capital in a private bank (up to 49% under the automatic route). Also, at least 26% of the paid-up capital will have to be held by Indian residents at all times. A foreign bank can establish a WOS either through conversion of existing branches into a subsidiary or through a fresh banking licence.

A subsidiary of a foreign bank will be subject to the licensing requirements and conditions broadly consistent with those for new private sector banks. Guidelines for setting up a WOS will be issued separately by the RBI.

In case of NRIs, individual holding is restricted to 5% of the total paid-up capital and the aggregate limit cannot exceed 10% of the total paid-up capital both on repatriation and non-repatriation basis. This can be raised to 24% by a special resolution by its General Body.

In case of foreign institutional investors (FIIs)/foreign portfolio investors (FPIs)/qualified foreign investors (QFIs), individual holding is restricted to less than 10% of the total paid-up capital. The aggregate limit for all FIIs/FPIs/QFIs cannot exceed 24% of the total paid-up capital, which can be raised to 49% by the bank through a resolution by its Board of Directors followed by a special resolution by its General Body. For public sector banks, FDI and portfolio investment is limited to 20%.

Capital requirements

The RBI has instructed banks to maintain adequate capital on a continuous basis for credit risk, market risk, operational risk and other risks. Capital adequacy is measured in terms of the Capital to Risk-Weighted Assets Ratio (CRAR). Basel III Capital Regulations specifying minimum capital requirements have been implemented in India from 1 April 2013 in phases and will be fully implemented by 31 March 2019.

With respect to the Basel III liquidity standards, the RBI has already started phasing in implementation of the Liquidity Coverage Ratio (LCR) from January 2015 and is looking to implement the Net Stable Funding Ratio (NSFR) from 1 January 2018 for banks in India.⁶⁶ On 28 May 2015, the RBI released draft guidelines on NSFR for comments.

⁶³ Discussion Paper on Banking Structure in India - The Way Forward, <http://rbi.org.in/Scripts/PublicationReportDetails.aspx?ID=713>, accessed 15 June 2015

⁶⁴ Core Principles of Effective Banking Supervision, <http://www.rbi.org.in/upload/publications/pdfs/10115.pdf>, accessed 15 June 2015

⁶⁵ Consolidated FDI Policy 2015, DIPP, http://dipp.nic.in/English/policies/FDI_Circular_2015.pdf, accessed 15 June 2015

⁶⁶ First Bi-monthly Monetary Policy Statement, 2015-16, 7 April 2015, https://rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=33628, accessed 15 June 2015

Currency exchange control⁶⁷

The RBI supervises and regulates the foreign exchange market in India through the Foreign Exchange Management Act, 1999 (FEMA). It issues licences to banks and other institutions to act as Authorised Dealers in the foreign exchange market. The RBI has undertaken substantial elimination of licensing, quantitative restrictions, and other regulatory and discretionary controls.

The foreign exchange market in India comprises Authorised Persons (banks, money changers and other entities) in the foreign exchange business, foreign exchange brokers who act as intermediaries, and customers – individuals as well as companies – who need foreign exchange for their transactions. The customer segment is dominated by major public sector entities, the Indian government and large private sector companies. FIIs have emerged as an important constituent in the equity market and thus contribute significantly to foreign exchange market activity. The Indian foreign exchange market primarily comprises two segments – the spot market (the dominant segment) and the derivatives market.

A unified, single, market-determined exchange rate system based on the demand and supply of foreign exchange has been effective from 1 March 1993. The RBI's exchange rate policy focuses on ensuring orderly conditions in the foreign exchange market; therefore, it closely monitors developments in financial markets in India and abroad. When necessary, it intervenes in the market by buying or selling foreign currencies. Market operations are undertaken either directly or through public sector banks.

Non-banking financial institutions/companies

Non-banking financial institutions cater to a wide range of financial requirements and can broadly be divided into financial institutions (FIs) and non-banking financial companies (NBFCs).

There are four FIs under the regulation and supervision of the RBI: Export-Import Bank of India (EXIM), National Bank for Agriculture and Rural Development (NABARD), National Housing Bank (NHB), and Small Industries Development Bank of India (SIDBI).

With the growing importance of financial inclusion, NBFCs have evolved as important financial intermediaries, particularly for the small-scale and retail sectors. An NBFC is a company registered under the Companies Act, engaged in the business of loans and advances, acquisition of shares/stocks/bonds/debentures/securities issued by the government or local authority or other marketable securities of a like nature, leasing, hire-purchase, insurance business, chit business. A non-banking institution that is a company with the principal business of receiving deposits under any scheme or arrangement in one lump sum or in instalments by way of contributions or in any other manner is also an NBFC (residuary non-banking company). It does not include any institution whose principal business is agriculture activity, industrial activity, purchase or sale of any goods (other than securities) or providing any services and sale/purchase/construction of immovable property. The RBI regulates and supervises NBFCs.

NBFCs are categorised in terms of the type of liabilities into (i) Deposit (NBFC-D) and Non-Deposit (NBFC-ND) accepting NBFCs, (ii) NBFC-NDs by their size into systemically important (NBFC-ND SI) and other non-deposit holding companies and (iii) by the kind of activity they conduct.⁶⁸

100% FDI is permitted under the automatic route for NBFCs involved in specific activities and subject to certain minimum capitalisation norms.⁶⁹

The RBI issued a revised regulatory framework for NBFCs in November 2014, (which was further amended on 27 March 2015) as NBFCs are increasingly exposed to risks arising out of counterparty failures, funding and

⁶⁷ Reserve Bank of India: Functions and Working, <http://rbidocs.rbi.org.in/rdocs/Content/PDFs/FUNCWWE080910.pdf>, accessed 15 June 2015

⁶⁸ Frequently asked questions on NBFCs, RBI, <https://rbi.org.in/scripts/FAQView.aspx?Id=71>, accessed 15 June 2015

⁶⁹ Consolidated FDI Policy 2015, DIPP, http://dipp.nic.in/English/Policies/FDI_Circular_2015.pdf, accessed 15 June 2015

asset concentration, interest rate movement, and risks pertaining to liquidity and solvency. The changes cover regulations with respect to minimum net owned fund requirements, deposit acceptance and capital adequacy norms, thresholds defining systemic significance, asset classification and provisioning norms, corporate governance and disclosure norms. These changes will strengthen the NBFC sector by addressing risks, simplifying compliance and strengthening governance standards.⁷⁰

Recent developments

Initiatives in the banking sector in India

Following the RBI's guidelines for licensing of new banks in the private sector issued in February 2013, in April 2014, the RBI granted two applicants in-principle approval to set up new banks in the private sector within 18 months.

Revision to priority-sector lending guidelines⁷¹

Revised priority-sector lending guidelines were released in April 2015, according to which lending to sub-sectors including renewable energy, social infrastructure and medium enterprises would be treated as priority-sector lending. Other priority sectors include agriculture, micro and small enterprises, export credit, education and housing.

The concept of a tradable Priority Sector Lending Certificate (PSLC) has also been introduced, which would enable 'deficit' banks to buy these certificates from 'surplus' banks to meet their targets. Also, in order to make finance available to those who most need it, banks are now required to progressively achieve 8% of lending to small and marginal farmers and 7.5% to micro enterprises.

Priority-sector target for foreign banks⁷²

Foreign Banks with 20 branches and above already have priority sector targets and sub-targets for agriculture and weaker sections, which are to be achieved by 31 March 2018 as per the action plans submitted by them and approved by the RBI. The sub-targets for small and marginal farmers and micro enterprises would be made applicable post 2018 after a review in 2017. Foreign banks with less than 20 branches will move to a Total Priority Sector Target of 40% of Adjusted Net Bank Credit (ANBC) or Credit Equivalent Amount of Off-Balance Sheet Exposure, whichever is higher, on par with other banks by 2019-20, and the sub-targets for these banks, if to be made applicable post 2020, would be decided in due course.

Financial inclusion

Financial inclusion is an important priority of the current government in order to increase savings, security and empower the weaker sections and low-income groups. On 28 August 2014, the Prime Minister launched the Pradhan Mantri Jan-Dhan Yojana (PMJDY) – a national mission for financial inclusion. The objective of the scheme is to ensure universal access to various financial services, including a basic savings bank account, access to need-based credit, remittance facility, insurance and pension to the excluded sections of society.⁷³ With the objective of providing basic banking and financial services to every household in the country, this scheme also paves the way for banks and insurance companies to cater to the growing consumer base of India.

Besides a bank account, other benefits include a RuPay debit card, INR 100,000 accident insurance cover, and an additional INR 30,000 life insurance cover. Based on account performance, an overdraft facility would also be given. On the first day itself, 15 million bank accounts were opened across 77,000 locations. The scheme entered the Guinness World Records for opening the most bank accounts in one week as a part of financial inclusion. As on 10 June 2015, more than 161 million bank accounts have been opened and 144 million Rupay

⁷⁰ Revised Regulatory Framework for NBFCs, RBI, 10 November 2014, <https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=9327&Mode=0>, accessed 15 June 2015

⁷¹ Indian Banking Sector: Emerging Challenges and Way Forward, RBI, https://rbi.org.in/Scripts/BS_SpeechesView.aspx?Id=955, accessed 15 June 2015

⁷² Priority Sector Lending - Targets and Classification, RBI, <https://rbi.org.in/scripts/NotificationUser.aspx?Id=9688&Mode=0>, accessed 15 June 2015

⁷³ Pradhan Mantri Jan-Dhan Yojana, http://pmjdy.gov.in/Pdf/PMJDY_BROCHURE_ENG.pdf, accessed 15 June 2015

cards issued. Total deposits amounted to INR 183 billion. Of the total number of accounts, 60% are from rural areas.⁷⁴

Migration from cash to electronic payments

With the introduction of the new RuPay cards, the government has provided a new method of payment to a large portion of the untapped market. This will be of paramount importance for business-to-consumer companies where electronic payments are common. RuPay also has complete interoperability between multiple payment channels. With over 144 million RuPay cards in the market, there is a huge scope for businesses as they will help penetrate rural and semi-urban areas and move the economy from cash to electronic transactions.⁷⁵

Integrated bill payment system

The Bharat Bill Payment System (BBPS) will function as a tiered structure for operating the bill payment system in the country with a single brand image providing the convenience of 'anytime anywhere' bill payment to customers. It will be an integrated, interoperable bill payment system for millions of customers and replace the segmented bill payments taking place at present. Existing players (both banks & non-banks) catering to the requirements of bill payments as well as aggregation of payment services will be a part of BBPS. The eligibility criteria have been specified by the RBI. FDI would be allowed according to the current FDI Policy and regulations framed under the Foreign Exchange Management Act (FEMA).⁷⁶

Thrust on mobile banking

With over 970 million mobile users in India, only about 4% are mobile banking customers, signalling the tremendous growth potential in the sector. In March 2015, the number of mobile banking transactions nearly doubled to 19.7 million transactions worth INR 169 billion in value, almost four times the value of INR 34 billion in March 2014.⁷⁷

Guidelines for licensing of payments banks and small banks

Following the announcement in the Union Budget 2014-15 for setting up differentiated banks to serve niche interests such as local area banks and payment banks, the RBI released guidelines in November 2014 for the licensing of payments banks and small finance banks in the private sector. These banks are expected to meet the savings, credit and remittance needs of small businesses, the unorganised sector, low-income households, farmers and migrant work force. They will enable high-volume, low-value transactions in a secure technology-driven environment and could be pivotal in supporting the government's financial inclusion goal.

The RBI has invited applications for setting up small banks and payments banks. Foreign shareholding in both these types of banks will be subject to the FDI Policy for private sector banks.

⁷⁴ Progress report, PMJDY, <http://pmjdy.gov.in/account-statistics-country.aspx>, accessed 15 June 2015

⁷⁵ RuPay, National Payments Corporation of India, <http://www.npci.org.in/RuPayBenefits.aspx>, accessed 15 June 2015

⁷⁶ Implementation of BBPS – Guidelines, RBI, <https://rbi.org.in/scripts/NotificationUser.aspx?Id=9368&Mode=0>, accessed 15 June 2015

⁷⁷ Bankwise volumes in ECS/NEFT/RTGS/mobile transactions, March 2015, RBI, <https://www.rbi.org.in/scripts/NEFTUserView.aspx?Id=83>, accessed 15 June 2015

Chapter 4

Business entities

Sole proprietorship

A sole proprietorship is an organisation where a single individual owns, manages and controls the business. There is no requirement for registration of the firm. The firm has no legal existence separate from its owner. However, the sole proprietor may be required to obtain a licence for carrying out business from the local administration. The required capital is supplied wholly by the owner himself, who alone enjoys the profits of the business and he alone bears the losses. The liability of the proprietor is unlimited i.e. it extends beyond the capital invested in the firm. This form of organisation is suitable for businesses that involve moderate risk.⁷⁸

A non-resident Indian (NRI) or Person of Indian Origin (PIO) may invest in a sole proprietorship concern with repatriation benefits only with the prior approval of the Secretariat for Industrial Assistance (SIA), Indian government or the Reserve Bank of India (RBI). No person resident outside India other than NRIs/PIOs can make any investment by way of contribution to the capital of a proprietorship concern. However, the RBI may, on an application made to it, permit a person resident outside India subject to terms and conditions as may be considered necessary.⁷⁹

Partnership

A partnership is the relation between persons who have agreed to share the profits of a business carried on by all or any of them acting for all. Persons who have entered into partnership with one another are called individually, 'partners' and collectively 'a firm', and the name under which their business is carried on is the 'firm name'. It is governed by the Indian Partnership Act, 1932.⁸⁰

A partnership can be formed by an agreement, which may be either written or oral. If the written agreement is duly stamped and registered, it is known as a 'Partnership Deed'. If the firm is not registered, it will be deprived of certain legal benefits, such as when there are disputes between partners. The Registrar of Firms is responsible for registering partnership firms. There must be a minimum of two partners, while the maximum number can be 10 in case of a banking business and 20 in all other types of businesses. The firm has no separate legal existence i.e. the firm and the partners are the same in the eyes of law. The liability of the partners is unlimited – they are jointly and severally liable for the liabilities of the firm. There are restrictions on the transfer of interest i.e. none of the partners can transfer their interest in the firm to any person (except to the existing partners) without the unanimous consent of all other partners. The firm must be dissolved on the retirement, lunacy, bankruptcy, or death of any partner.⁸¹

NRIs/PIOs may invest in partnership firms with repatriation benefits only with the prior approval of the Secretariat for Industrial Assistance (SIA), Indian government or the RBI. No person resident outside India other than NRIs/PIOs can make any investment by way of contribution to the capital of a firm. However, the RBI may, on an application made to it, permit a person resident outside India subject to such terms and conditions as may be considered necessary.⁸²

Limited companies

The Companies Act, 2013 (to the extent applicable) broadly recognises four types of companies:

- Public Limited Company
- Private Limited Company
- Dormant Company
- One Person Company

⁷⁸ Sole Proprietorship, http://www.archive.india.gov.in/business/starting_business/sole_proprietorship.php, accessed 8 May 2015

⁷⁹ Foreign Investments in India – Investment in Proprietorship Concern/ Partnership Firm A.P. (DIR Series) Circular No.39 (December 3, 2003), RBI, <http://rbidocs.rbi.org.in/rdocs/notification/PDFs/40493.pdf>, accessed 8 May 2015

⁸⁰ Partnership Act, 1932, http://www.mca.gov.in/Ministry/actsbills/pdf/Partnership_Act_1932.pdf, accessed 8 May 2015

⁸¹ Procedure for Registration of a Partnership Firm, http://www.archive.india.gov.in/business/starting_business/org_partnership.php, accessed 8 May 2015

⁸² Foreign Investments in India – Investment in Proprietorship Concern/ Partnership Firm A.P. (DIR Series) Circular No.39 (December 3, 2003), <http://rbidocs.rbi.org.in/rdocs/notification/PDFs/40493.pdf>, accessed 8 May 2015

Private Limited Company

A private company⁸³ is one that restricts (by its Articles of Association):

- the rights of its shareholders to transfer shares;
- the number of shareholders (excluding present- and past-employee shareholders) to 200;
- the company from making invitation to the public to subscribe to any shares or debentures of the company; and
- a minimum of two shareholders are required to form a private limited company.

The name of a private company carries the suffix 'Private Limited' (Pvt Ltd).

Public Limited Company

A public company is a company, which is not a private company⁸⁴. The abovementioned restrictions applicable to a private company are not applicable to a public company. A minimum of seven shareholders are required to form a public company.

Also, a private company that is a subsidiary of a public company is defined as a public company. The name of a public company carries the suffix 'Limited' (Ltd).

Under the Companies Act, a private limited company enjoys certain privileges and exemptions from various provisions of the Act unlike a public company, which is subject to greater scrutiny, transparency and compliance regulations. Furthermore, a public company (which is listed on a stock exchange in India) is also regulated by the Securities and Exchange Board of India (SEBI).

Dormant Company (notified under the new Companies Act, 2013)

A company formed and registered under this Act for a future project or to hold an asset or intellectual property and having no significant accounting transactions, may make an application to the Registrar of Companies (ROC) for obtaining the status of a dormant company if it satisfies the terms and conditions as mentioned in the relevant provisions of Companies Act, 2013, and the rules made there under. The ROC, on consideration of the application, would allow the status of a dormant company to the applicant and issue a certificate.

One Person Company (notified under the new Companies Act, 2013)

'One person company' is a new concept introduced by the Companies Act, 2013. As the name suggests, it is formed with only one person as its member. Since such companies have only one member, these companies enjoy certain privileges or exemptions as compared to other companies. It can be formed by a person who is a resident and citizen of India; a foreign national is not eligible to incorporate a one person company under existing regulations.

Object/activity: A company incorporated under the provisions of the Companies Act, 2013 can undertake only those business activities as specified in its 'Main Objects' under its Memorandum and Articles of Association. The proposed business activities to be carried out by an Indian entity owned by non-residents shall be subject to the FDI Policy of the Indian government as amended from time to time.

You may also wish to see [Chapter 5 Company formation and administration](#) and [Chapter 7 Company taxation](#).

Trusts⁸⁵

Trusts can be public or private. Public trusts are generally formed for charitable or religious purposes and not for commercial activities. A public charitable trust is one which benefits the public at large while income from a private trust is available only to specified beneficiaries.

⁸³ Section 2(68) of the Companies Act, 2013, <http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf>, accessed 8 May 2015

⁸⁴ Section 2(71) of the Companies Act, 2013

⁸⁵ Taxation of Trusts: Public or Private, http://www.archive.india.gov.in/business/taxation/public_pvt_trust.php, accessed 8 May 2015

Public and private trusts differ in the process of their creation. In creating a charitable or religious trust, a formal deed or any writing is not necessary, while private trusts are created and governed by the Indian Trusts Act, 1882. In case of a private trust declared by a will, registration is not necessary, whether it involves movable or immovable property. In all other cases, registration of a private trust is necessary under the Indian Trusts Act, 1882. For public trusts, registration is optional but desirable.

Trusts (public and private) are subject to taxation under the Income Tax Act, 1961. However, charitable and religious trusts enjoy several tax exemptions and benefits.

Entity options for foreign companies

A foreign company planning to set up business operations in India can⁸⁶:

- set up a liaison office/representative office, project office or branch office of the foreign company to undertake activities permitted under the Foreign Exchange Management (Establishment in India of Branch Office or Other Place of Business) Regulations, 2000;
- incorporate a company under the Companies Act as a joint venture or a wholly owned subsidiary; or
- invest in a limited liability partnership (LLP) under the Limited Liability Partnership Act, 2008.

Liaison office/Representative office⁸⁷

A liaison office (LO) can undertake only liaison activities, i.e. it can act as a channel of communication between the Head Office abroad and parties in India. It is not allowed to undertake any business activity in India and cannot earn any income in India. Expenses of such offices are to be met entirely through inward remittances of foreign exchange from the Head Office outside India. The role of such offices is, therefore, limited to collecting information about possible market opportunities and providing information about the company and its products to prospective Indian customers.

The RBI allows LOs to undertake the following activities in India:

- represent in India the parent company/group companies;
- promote export/import from/to India;
- promote technical/financial collaborations between parent/group companies and companies in India;
- act as a communication channel between the parent company and Indian companies.

Permission to set up LOs is initially granted for a period of three years and this may be extended from time to time by the Authorised Dealer in whose jurisdiction the office is set up. No extension would be considered for LOs of entities that are NBFCs and those engaged in construction and development (excluding infrastructure development companies). Upon expiry of the validity period, these entities must either close down or be converted into a joint venture/wholly owned subsidiary, in conformity with the current FDI Policy.⁸⁸

Branch office⁸⁹

Companies incorporated outside India and engaged in manufacturing or trading activities are allowed to set up branch offices (BO) in India with specific approval of the RBI. Such BOs are permitted to represent the parent/group companies and undertake the following activities in India:

- export/import of goods;
- render professional or consultancy services;
- carry out research work, in areas in which the parent company is engaged;

⁸⁶ Foreign Investments in India, RBI, <http://www.rbi.org.in/scripts/FAQView.aspx?Id=26>, accessed 8 May 2015

⁸⁷ Liaison/Branch/Project Offices of foreign entities in India, <http://www.rbi.org.in/scripts/FAQView.aspx?Id=100>, accessed 8 May 2015

⁸⁸ Master Circular on Establishment of Liaison/Branch/Project Offices in India by Foreign Entities, RBI, http://www.rbi.org.in/scripts/BS_CircularIndexDisplay.aspx?Id=7312, accessed 8 May 2015

⁸⁹ Liaison/Branch/Project Offices of foreign entities in India, RBI, <http://www.rbi.org.in/scripts/FAQView.aspx?Id=100>, accessed 8 May 2015

- promote technical or financial collaborations between Indian companies and the parent or overseas group company;
- represent the parent company and act as a buying/selling agent in India;
- render services in information technology and development of software in India;
- render technical support to the products supplied by the parent/group companies;
- foreign airline/shipping company.

A BO is not allowed to carry out manufacturing or processing activities in India, directly or indirectly, or any retail trading activities. Profits earned by BOs can be freely remitted from India, subject to payment of applicable taxes.

Foreign entities wanting to set up an LO/BO in India are required to submit their application (Form FNC) to the Foreign Investment Division of the RBI through an Authorised Dealer bank. The applications will be considered by the RBI under two routes:

- Reserve Bank route: where the principal business of the foreign entity falls under sectors where 100% FDI is permissible under the automatic route.
- Government route: where the principal business of the foreign entity falls under sectors where 100% FDI is not permissible under the automatic route. Applications from entities in this category and those from non-government organisations/non-profit organisations/government bodies/departments are considered by the RBI in consultation with the Ministry of Finance.

The following additional criteria are also considered by the RBI while sanctioning an LO/BO of foreign entities:

Track record

- For LO: a profit-making track record during the immediately preceding three financial years in the home country.
- For BO: a profit-making track record during the immediately preceding five financial years in the home country.

Net worth

- For LO: not less than USD 50,000 or its equivalent
- For BO: not less than USD 100,000 or its equivalent

Project office⁹⁰

The RBI has granted general permission to foreign companies to establish project offices in India if they have secured a contract from an Indian company to execute a project in India, and

- the project is funded directly by inward remittance from abroad; or
- it is funded by a bilateral or multilateral international financing agency; or
- it has been cleared by an appropriate authority; or
- the company or entity in India awarding the contract has been granted a term loan by a public financial institution or a bank in India for the project.

However, if the above criteria are not met, or if the parent entity is established in Pakistan, Bangladesh, Sri Lanka, Afghanistan, Iran, China, Hong Kong or Macau, such applications have to be forwarded to the Foreign Exchange Department of the RBI for approval.

Wholly owned subsidiary/Joint venture⁹¹

A foreign company may set up a wholly owned subsidiary in sectors where 100% FDI is permitted under the FDI Policy. Alternatively, it could enter into a joint venture with an Indian partner, which may entail the following advantages for a foreign investor:

⁹⁰ Ibid.

⁹¹ Entry Strategies for Foreign Investors, DIPP, <http://dipp.nic.in/English/policy/entry.htm>, accessed 8 May 2015

- established distribution/marketing set-up of the Indian partner;
- available financial resources of the Indian partner;
- established contacts of the Indian partner, which help smoothen the process of setting up operations.

A foreign company incorporated as either of these two entities under the Companies Act is treated at par with any domestic Indian company within the scope of approval and subject to all Indian laws and regulations as applicable to other domestic Indian companies.

Limited liability partnership

A limited liability partnership (LLP) is an alternative corporate business form that gives the benefits of limited liability of a company and the flexibility of a partnership. It is governed by the provisions of the Limited Liability Partnership Act, 2008, and not the Indian Partnership Act, 1932.

An LLP can continue its existence irrespective of changes in partners. It is capable of entering into contracts and holding property in its own name. It is a separate legal entity, and is liable to the full extent of its assets but the liability of the partners is limited to their agreed contribution in the LLP. Furthermore, no partner is liable on account of the independent or unauthorised actions of other partners, thus individual partners are shielded from joint liability created by another partner's wrongful business decisions or misconduct. Mutual rights and duties of the partners within an LLP are governed by an agreement between the partners or between the partners and the LLP as the case may be. The LLP, however, is not relieved of the liability for its other obligations as a separate entity. Also, an LLP will have more flexibility and lesser compliance requirements compared to a company.⁹²

The LLP Act, 2008 allows a person resident outside India or an entity incorporated outside India to invest in LLPs. An LLP, existing or new, operating in sectors/activities where 100% FDI is allowed under the automatic route would be eligible to receive FDI.⁹³

⁹² FAQs on LLPs, Ministry of Corporate Affairs, http://www.mca.gov.in/LLP/faq_llp_basic_concept.html, accessed 8 May 2015

⁹³ Foreign Direct Investment in LLPs, RBI, <http://www.rbi.org.in/scripts/NotificationUser.aspx?Id=8844&Mode=0>, accessed 8 May 2015

Chapter 5

Company formation and administration

Forming a company

The process of incorporating a company in India can be broadly divided into the following four steps⁹⁴:

1. Director Identification Number (DIN) and Digital Signature Certificate (DSC)
Obtaining a DIN and DSC for all directors of the company is a pre-requisite for checking the availability of the company name and making an application to register the company. All relevant forms and documents have to be filed electronically.
2. Application for name availability
Select a few suitable names, up to a maximum of six names, indicative of the main objectives of the company. The proposed name should not resemble the name of any other company already registered and should not violate the provisions of the Name Availability Guidelines issued by the Ministry of Corporate Affairs (MCA). The Name Application must be submitted online with the concerned Registrar of Companies (ROC) for their approval.
3. Drafting the Memorandum and Articles of Association
The Memorandum and Articles of Association (the governing charter) of the proposed company need to be drafted in accordance with the applicable provisions of the Companies Act, 2013 and are subject to the FDI Policy of the Indian government as amended from time to time.
4. Application for company incorporation
The fourth step is to apply for the registration of the company. After the name is approved, prescribed forms along with the prescribed filing fees and stamp duty are to be submitted through the MCA portal along with the Memorandum and Articles of Association and other supporting documents duly signed and certified. The ROC, after scrutiny of documents submitted online, approves the company incorporation application and issues the digitally signed Certificate of Incorporation.

In order to simplify the incorporation process, effective 1 May 2015, the MCA introduced the Integrated Incorporation Form: INC-29.⁹⁵ This form integrates three previously separate processes with a single application for obtaining a DIN, reserving a name and incorporating a new company. (In case one wants to avail any of these services separately, the old/separate e-forms can be used.) The form must be accompanied by supporting documents including details of directors and subscribers, Memorandum and Articles of Association, etc. Once the form is processed and found complete, the company would be registered and the Corporate Identity Number (CIN) would be allocated. DINs get issued to proposed directors who do not have a valid DIN and a maximum of three directors are allowed to be listed for allotment of DIN using this form while incorporating a company.

Advantages of Form INC-29

The integrated form can be used to apply for the following registrations at once:

1. Application for DIN
2. Name reservation
3. Incorporation of a company
4. Application for Permanent Account Number (PAN) and Tax Deduction Account Number (TAN): All companies in India are required to have a PAN and TAN for filing income tax and other tax returns with the regulatory authority. Under previous provisions, this application was made once the company was incorporated, which would take 10–15 days from the date of application. However, this form will expedite the process.
5. Employee State Insurance Corporation (ESIC): The ESIC is required for prescribed companies under the ESIC Act.

⁹⁴ Steps to be taken to incorporate a new company, MCA, <http://www.mca.gov.in/MinistryV2/steps.html>, accessed 5 May 2015

⁹⁵ Company forms, MCA, http://www.mca.gov.in/MinistryV2/Download_eForm_choose.html#inc29, accessed 5 May 2015

6. Digital Signature Certificate (DSC): Unlike previous provisions, with INC-29, all directors are not required to have a DSC as the form must be signed digitally by any one of the directors of the proposed company.

According to the Companies (Amendment) Act, 2015, a company (private or public) is no longer required to obtain a Certificate of Commencement of Business. Hence, companies are no longer required to file Form INC-21 with the ROC. Once the company receives its Certificate of Incorporation, it can commence business activities.

Timeline: The entire process of incorporation can be completed in 3–4 weeks.

Formation cost: The cost of formation depends upon the authorised capital of the company. Also, the total statutory fees payable to the regulatory authority vary depending on the state in which the registered office will be situated.

Shares and capital structures

The requirement of minimum share capital has been withdrawn in the Companies (Amendment) Act, 2015. Hence, a company can carry on business activities with any amount of share capital from inception.

Classification of share capital

The share capital of a company limited by shares can be classified into equity and preference. Preference share capital is that part of the issued share capital of a company limited by shares which gives the concerned shareholder preference rights in respect of payment of dividend and repayment in case of winding up. Equity share capital means all share capital that is not preference share capital. Preference share capital can be:

- Redeemable or irredeemable
Redeemable preference shares can be redeemed on or after a period fixed for redemption under the terms of issue or after giving a proper notice of redemption to preference shareholders. The Companies Act, however, imposes certain restrictions for the redemption of preference shares. Irredeemable preference shares are those shares which cannot be redeemed during the lifetime of a company.

As per the provisions of the Companies Act, 2013, a company limited by shares cannot issue irredeemable preference shares. Furthermore, except in case of infrastructure projects, only preference shares that are liable to be redeemed within a period not exceeding 20 years from the date of issue can be issued.

- Convertible or non-convertible
Preference shares that are convertible into equity shares are convertible preference shares, and the ones that are not convertible into equity shares are non-convertible preference shares.

Shares or debentures or other interest of any member in a company shall be movable property transferable in the manner provided by the Articles of the company. A company may, if so authorised by its Articles, pay dividends in proportion to the amount paid up on each share.

Directors

Every company must have a Board of Directors which is responsible for the conduct of its business. According to the Companies Act, the minimum number of directors required in case of private companies is 2 and in case of public companies is 3; and the maximum directors a company can have is 15. Every company belonging to prescribed classes shall have the following full-time key managerial personnel:

- managing director, or Chief Executive Officer or manager and in their absence, a whole-time director;
- company secretary; and
- chief financial officer.

Role of directors

The Companies Act empowers the Board to do all such activities, in accordance with the company's Memorandum and Articles of Association, as the company is authorised to do, unless any law or the Memorandum requires any act to be done by the company by way of resolution of the shareholders in their general meeting.

Since directors act as agents of a company, all acts done and contracts entered into by them are binding on the company, unless such acts are outside the scope of authority of such directors. Since directors of a company occupy a fiduciary position, and are persons responsible for the management of the affairs of the company, they are subject to duties and liabilities, including penal liabilities in case of default or misconduct on their part, in circumstances mentioned under the Companies Act.

Appointment of directors

- Unless the Articles provide, individuals who are subscribers to the Memorandum of Association shall be deemed to be the first directors of the company until the directors are duly appointed.
- Otherwise expressly provided in the Act, every director shall be appointed by the company in the general meeting.
- Every proposed director shall have a DIN.

Disqualification for appointment of directors

A person shall not be eligible for appointment as a director of a company if he/she:

- is of unsound mind and stands so declared by competent court
- is undercharged insolvent
- has applied to be adjudicated as an insolvent and his application is pending
- has been convicted by court and sentenced to imprisonment for at least six months and five years have not lapsed from the expiry of the sentence
- has been convicted and sentenced to imprisonment for seven years or more
- has been disqualified as a director by an order passed by a court or tribunal
- has not paid any calls of any shares held by him and six months have lapsed from the last day fixed for the payment
- has been convicted of related-party transactions during the preceding five years
- has not obtained a DIN.

Removal of directors

- A company may remove a director before the expiry of the period of his office through an ordinary resolution.
- On receipt of notice of the resolution, the company shall send a copy of the notice to the concerned director, who shall be entitled to be heard on the resolution at the meeting.
- A vacancy shall be filled by the company in the meeting in which he was removed by the appointment of another director in his place but special notice is required. The director so appointed shall hold office till the date up to which his predecessor would have held office if he had not been removed.
- A director who is removed from office shall not be re-appointed as a director by the Board.

Resignation of directors

- A director may resign from office by giving a notice to the company, who shall intimate the ROC within 30 days of receiving the notice.
- The resignation shall be mentioned in the Board's report in the next general meeting of the company.
- The director shall also forward his resignation along with detailed reasons for the resignation to the ROC within 30 days of resignation.
- Resignation shall take effect from the date on which the notice is received by the company or the date specified by the director in the notice, whichever is later.

- A director who has resigned shall be responsible for offences that have occurred during his tenure even after his resignation.

Types of directors

First directors: The number of directors and the names of the first directors shall be determined in writing by the subscribers of the Memorandum or a majority of them. However, where no provision is made in the Articles of a company for the appointment of first directors, the subscribers of the Memorandum, who are individuals, shall be deemed to be the first directors of the company until the directors are duly appointed in accordance with provisions of the Companies Act.

Executive and non-executive directors: Directors who are in whole-time employment or are entrusted with the day-to-day operations of the company are termed as executive directors. Non-executive directors are from outside the company. They do not take part in the day-to-day activities of the company and do not have knowledge about the company's routine operations.

Resident director: As per the Companies Act, 2013, at least one of the directors of a company must be a person who has stayed in India for a total period of not less than 182 days in the previous calendar year.

Independent directors in case of public companies: As per the Companies Act, 2013, the appointment of an independent director is mandatory to certain classes of companies. Every listed public company shall have at least one-third of the total number of directors as independent directors. However, private limited companies need not appoint an independent director.

Woman director: A new provision of the Companies Act, 2013, requires certain classes of companies to appoint at least one woman director on the Board of the company. This is not mandatory for private limited companies.

Director elected by small shareholders: Under the Companies Act, 2013, only listed companies may appoint a small shareholders' director. Shareholders holding shares of nominal value of not more than INR 20,000 or such other prescribed sum may appoint one director from amongst them.

Additional director: The Board may appoint an additional director at any time, if the Articles confer such powers.

- A person who fails to get appointed in a general meeting cannot be appointed as an additional director.
- An additional director shall hold office until the next Annual General Meeting (AGM) or the last date on which the AGM should have been held, whichever is earlier.

Alternate director: The Board may appoint an alternate director at any time, if the Articles confer such powers.

- The person to be appointed as an alternate director shall not hold another alternate directorship for any other director in the company.
- An alternate director can only be appointed in case a director leaves India for a period of at least three months.
- An alternate director to an independent director should also satisfy the criteria for an independent director.
- The office of the alternate director shall be vacated if and when the director in whose place he has been appointed returns to India.
- Provisions of automatic re-appointment of the retiring director shall apply to the original director and not to the alternate director.

Nominee directors: Subject to the Articles, the Board may appoint any person as a director nominated by an institution as a nominee director in pursuance of any law or agreement or by the central or state government by virtue of its shareholding in a government company.

Permanent directors: The Articles may also provide for the appointment of permanent directors. Such directors continue to be lifetime directors subject to other provisions of the Companies Act.

Duties of directors

Fiduciary duties

The Companies Act, 2013 enlists the specific fiduciary duties of a director. A director of a company:

- shall act in accordance with the Articles of the company;
- shall act in good faith in order to promote the objects of the company for the benefit of its members as a whole, and in the best interests of the company, its employees, the shareholders, the community and for the protection of the environment;
- shall exercise his duties with due and reasonable care, skill and diligence and shall exercise independent judgment;
- shall not get involved in a situation in which he may have a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the company;
- shall not achieve or attempt to achieve any undue gain or advantage either to himself or to his relatives, partners, or associates and if found guilty of making any undue gain, he shall be liable to pay an amount equal to that gain to the company;
- shall not assign his office and any assignment so made shall be void.

A director who contravenes the provisions of this section (166) shall be punishable with a fine not less than INR 100,000, which may extend to INR 500,000.

Compliances by directors under the Companies Act, 2013

- Obtain a Director Identification Number (DIN)
- Give a declaration that he is not disqualified to become a director under the Act
- Disclose his interest in any company or body corporate, firms, or other association of individuals at the first Board meeting, at the first Board meeting in every financial year, or whenever there is any change in the disclosures already made, then at the first Board meeting held after such change
- Mention his DIN while furnishing any return, information or particulars, as required to be furnished under the Act
- Restructure his directorships as per the maximum number allowed, within one year from commencement of the Act
- The total number of companies in which a person can hold office as a director shall not exceed:
 - 10 in public companies
 - 20 in private companies
 - 20 in both public and private companies

Company secretary

The functions of the company secretary include:

- to report to the Board about compliance with the provisions of the Companies Act, 2013, the rules made there under and other applicable laws;
- to ensure that the company complies with the applicable secretarial standards;
- to discharge such other duties as may be prescribed.

Other statutory requirements

The Board of Directors of every listed company shall constitute an Audit Committee. The committee shall consist of a minimum of three directors with independent directors forming a majority, provided that a majority of members should be able to read and understand financial statements.

The Board of every listed company shall constitute a Nomination and Remuneration Committee consisting of three or more non-executive directors, of which not less than half shall be independent directors. This committee shall formulate the criteria for determining qualifications, positive attributes and independence of a director and recommend to the Board a policy relating to the remuneration for the directors, key managerial personnel and other employees.

The Board of a company that has more than 1,000 shareholders, debenture-holders, deposit-holders and any other security holders at any time during a financial year shall constitute a Stakeholders' Relationship Committee consisting of a chairperson who shall be a non-executive director and such other members as may be decided by the Board. This committee shall consider and resolve the grievances of security holders of the company.

Meetings

One of the statutory requirements under the Companies Act is to conduct meetings.

Meetings of Directors

Board meetings: According to the Companies Act, 2013, there must be at least one meeting of the Board of Directors every three months. Directors are allowed to participate in person, through video conferencing or other audiovisual means capable of recording and recognising the participation of the directors, and recording and storing the proceedings along with the date and time.

Committee meetings: The Board of Directors may delegate any of its powers to committees if so authorised and in accordance with its Articles of Association, and such committees must conform to any regulations that may be imposed upon it by the Board.

Shareholders'/Members' Meetings

Annual General Meeting (AGM): The Companies Act, 2013 states that every company must hold one AGM in each calendar year. It must be held within 18 months of incorporation or 9 months of the closing of accounts, whichever is earlier, or in other cases within 15 months from the date of the last AGM or 6 months from the closing of accounts, whichever is earlier. Furthermore, a One Person Company is not required to hold an AGM.

Extraordinary General Meeting: Any general meeting held between two AGMs is called an Extraordinary General Meeting. Business arising between two AGMs that is urgent and cannot be deferred until the next AGM is transacted at an Extraordinary General Meeting.

Class Meetings: These are meetings of shareholders holding a particular class of shares. Resolutions passed at such meetings bind only the members of the concerned class.

Liquidations

A company can be closed in the following ways:⁹⁶

- Strike off a company under section 560 of the Companies Act: Any defunct company wanting to strike off its name from the Register of Companies can apply under the Fast Track Exit Mode by filing Form FTE. Similarly, the ROC also has the power to strike off any defunct company after being satisfied of the need to strike it off and has reasonable cause.
- Winding up of a company is a process by which the business of the company is wound up, and the company ceases to exist. All the assets of the company are sold, and the proceedings collected are used to discharge the liabilities on a priority basis.⁹⁷ The winding up of a company may either be (a) a

⁹⁶ Close a Company, MCA, <http://www.mca.gov.in/MCA21/CloseCompany.html> , accessed 8 May 2015

⁹⁷ Company Liquidators, MCA, http://www.companyliquidator.gov.in/winding_up.html, accessed 2 June 2015

compulsory winding up by the Tribunal (b) or a voluntary winding up by its members or creditors or (c) subject to the supervision of the Court.

Corporate social responsibility

According to the Companies Act, 2013, every company having a net worth of INR 5 billion or more, or turnover of INR 10 billion or more, or a net profit of INR 50 million or more, during any financial year shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of three or more directors, of which at least one must be an independent director. Every company, its holding or subsidiary company, or a foreign company having a branch or project office in India, which individually fulfils any one of the criteria mentioned above will be considered as a 'qualifying company' and would then need to mandatorily perform all the CSR activities mentioned in section 135 of the Companies Act read with the CSR Rules during any financial year.

The CSR Committee must:

- formulate and recommend to the Board, a CSR Policy which shall indicate the activities to be undertaken by the company;
- recommend the amount of expenditure to be incurred on these activities; and
- monitor the CSR Policy of the company from time to time.

The Act expressly states that during implementation of the CSR Policy, preference must be given by the company to the local area and the area around which it operates. The CSR Rules lay down the method of implementation of CSR activities.

The Act provides the following roles and responsibilities for the Board of Directors:

- Approval of the CSR Policy of the company;
- Disclosing the content of the Policy in the report of the Board of Directors;
- Placing the Policy on the company's website;
- Ensuring that the CSR Policy is implemented and the activities undertaken by the company are carried out;
- Ensuring that the company spends, in every financial year, at least 2% of the average net profits of the company made during the three immediately preceding financial years;
- Ensuring that, if the earmarked amount is not spent, the same is specified in its report;
- The Board shall have the power to make any change(s) in the Committee constitution.

To know more about CSR requirements in India, please see our publication '[An insight into Corporate Social Responsibility in India](#)' on our website.⁹⁸

⁹⁸ An insight into CSR in India, SKP, http://www.skpgroup.com/data/resource/skp_corporate_social_responsibility_rules_in_india_.pdf, accessed 1 June 2015

Chapter 6

Financial reporting and audit requirements

Financial reporting requirements and deadlines

Type of entity	Preparation of financial statements mandatory	Relevant statutes*	Reporting standards of accounting records	Remarks	Reporting deadline
Proprietorship	Yes	Income Tax Act, 1961	Accounting Standards as issued by the Institute of Chartered Accountants of India (ICAI)	Applicable only if the turnover exceeds the limits specified in the relevant statute ⁹⁹	30 September**
Partnership Firm	Yes	Income Tax Act, 1961	Accounting Standards as issued by ICAI	Applicable only if the turnover exceeds the limits specified ¹⁰⁰	30 September**
Limited Liability Partnership	Yes	Limited Liability Partnership Act, 2008	Accounting Standards as issued by ICAI	Applicable only if the turnover exceeds the limits specified ¹⁰¹	30 September**
Listed Public Limited Company	Yes	Companies Act, 1956 and 2013 (to the extent notified), SEBI Guidelines and any other relevant statute ¹⁰²	Accounting Standards as notified under the Companies Act or another specified statute along with Indian GAAP	In case the company falls under a special statute, the requirements of such special statute shall prevail ¹⁰³	Two months from the end of the financial year
Unlisted Public and Private Limited Company	Yes	Companies Act, 1956 and 2013 (to the extent notified)	Accounting Standards as notified under the Companies Act	In case the company falls under a special statute, the requirements of such special statute shall prevail ¹⁰⁴	Six months from the end of the financial year

⁹⁹ INR 10 million in case of business and INR 0.25 million in case of profession

¹⁰⁰ Ibid.

¹⁰¹ Ibid.

¹⁰² Banking, Financial Services, Insurance and Electricity companies where the form and contents of the financial statements are governed by their respective statutes

¹⁰³ Ibid.

¹⁰⁴ Ibid.

Trusts	Yes	Trust Act ¹⁰⁵ , and Income Tax Act, 1961	Accounting Standards as issued by ICAI		30 September
Societies	Yes	Respective Societies Act ¹⁰⁶ , and Income Tax Act, 1961			30 September
Liaison Office/ Branch Office/ Project Office	Yes	FEMA and Companies Act, 2013	Accounting Standards as notified under the Companies Act		Six months from the end of the financial year ¹⁰⁷

* The Preface to the Statements of Accounting Standards issued by the ICAI states that "Efforts will be made to issue Accounting Standards which are in conformity with the provisions of the applicable laws, customs, usages and business environment of our country. However, if due to subsequent amendments in the law, a particular Accounting Standard is found to be not in conformity with such law, the provisions of the said law will prevail and the financial statements should be prepared in conformity with such law." E.g. Banks need to prepare financial statements as per the Banking Regulation Act, 1949.

** This deadline shall be extended to 30 November where transfer pricing regulations become applicable.

The complete set of financial statements comprises the following:

- Directors' Report (applicable in case of specific types of entities only)
- Balance Sheet as at the end of the reporting period
- Statement of Profit and Loss/Income and Expenditure Account for the reporting period
- Statement of Cash Flows (applicable in case of specific types of entities only, exemptions available for certain entities)
- Notes forming part of the financial statements consisting of schedules to the balance sheets and Statement of Profit and Loss/Income and Expenditure Account, summary of Significant Accounting Policies, other explanatory information that may be required under relevant statutes.

The following key records are to be maintained by most entities:

- All sums of money received and expended and the matters in respect of which the receipt and expenditure take place
- All sales and purchases of goods/services
- Assets and liabilities
- If the entity is engaged in manufacturing, processing, mining, etc., particulars related to the utilisation of material/labour or other items of cost
- In addition, there may be a need to maintain additional records under relevant statutes.

¹⁰⁵ Depending upon the territory of registration and the purpose of the Trust

¹⁰⁶ Depending upon the territory of registration and the purpose of the Society

¹⁰⁷ In case where Form No. 49C or an annual activity certificate is required to be filed/furnished then the date of furnishing such form/certificate

Audit requirements

Types of mandatory audits to be conducted by an independent practicing Chartered Accountant:

Type of audit ¹⁰⁸	Timeline	Applicability
Statutory audit	Within six months from the end of the financial year	All companies
Limited reviews	Within 45 days from the end of the quarter	Listed companies
Audit of financial statements for tax purpose	30 September if transfer pricing regulations are not applicable, else 30 November	Companies: where the statutory year-end is different from the tax year-end and where tax audit is applicable ¹⁰⁹ Entities other than companies: where tax audit is applicable ¹¹⁰
Tax audit certification	30 September if transfer pricing regulations are not applicable, else 30 November	(see previous footnote)
Cost audit	180 days from the end of the financial year	Depends on the type of goods as well as turnover or net worth
VAT audit	Differs from state to state	Differs from state to state. E.g. In some states, there is no provision of VAT audit (filing of Annual Return may be applicable instead). In some other states, applicability depends on the turnover. ¹¹¹

Application of IFRS to financial reports

Consequent to the announcement made in the Union Budget 2014-15, India's accounting standards were converged with the International Financial Reporting Standards (IFRS) and framed in consultation with the ICAI and National Advisory Committee on Accounting Standards. These 39 standards, called the Indian Accounting Standards (Ind-AS) were notified on 16 February 2015 as Companies (Indian Accounting Standards) Rules, 2015. These accounting standards are significantly congruent with the global standards, with minimum carve-outs and are expected to boost investor confidence.¹¹²

The Ind-AS will be applicable to companies as follows¹¹³:

- on a voluntary basis, for financial statements for accounting periods beginning on or after 1 April 2015 with the comparatives for the periods ending 31 March 2015 or thereafter;
- on a mandatory basis, for accounting periods beginning on or after 1 April 2016 with the comparatives for the periods ending 31 March 2016 or thereafter, for companies with a net worth of INR 5 billion or more and holding, subsidiary, joint venture or associates of such companies;
- on a mandatory basis, for accounting periods beginning on or after 1 April 2017 with the comparatives for the periods ending 31 March 2017 or thereafter for:

¹⁰⁸ This does not include any other audit that is specifically needed under special statutes

¹⁰⁹ In India, companies are allowed to follow a different statutory year-end than the fiscal year-end (31 March). However the new Companies Amendment Bill mandates the same year-end which is yet to be notified. The old Companies Act, 1956 is currently in the process of being replaced by the new Companies Act, 2013. Since the new Companies Act, 2013 has not been fully notified, the above document does not take into consideration any implication that the new Companies Act, 2013 may have on any of the contents of the said document.

¹¹⁰ Applicable when turnover is over INR 10 million in case of business and INR 0.25 million in case of profession

¹¹¹ Based on the Maharashtra Value Added Tax Act, 2002 as applicable for FY 2013-14, if the aggregate sales turnover and the value of goods transferred to any other place of his business, or his agent, or principal situated outside the state, not by reason of sale, or turnover of purchases exceeds INR 10 million in any year, a VAT audit is required. The Audit report should be submitted by 15 January.

¹¹² Press release, Ministry of Corporate Affairs, <http://pib.nic.in/newsite/mbErel.aspx?relid=122083>, accessed 28 May 2015

¹¹³ Notification dated 16 February 2015, MCA, http://www.mca.gov.in/Ministry/pdf/Notification_20022015.pdf, accessed 28 May 2015

Doing business in India

- listed companies (irrespective of net worth);
- unlisted companies with net worth of INR 2.5 billion or more;
- companies whose equity and/or debt security are in the process of being listed with net worth of less than INR 5 billion; and
- holding, subsidiary, joint venture or associates of the companies mentioned above.

However, companies that are listed or in the process of being listed on small and medium enterprise (SME) exchanges shall not be required to apply Ind-AS.

Once a company opts to follow the Ind-AS, it shall be required to follow these standards for all subsequent financial statements.

Companies not covered by the above criteria shall continue to apply existing accounting standards prescribed in the annexure to the Companies (Accounting Standards) Rules, 2006.

Insurance companies, banking companies and non-banking finance companies shall not be required to apply Ind-AS for preparing their financial statements either voluntarily or mandatorily.

Note: This notification was issued by the Ministry of Corporate Affairs (MCA) on 16 February 2015 but has not been published in the Gazette of India at the time of preparation.

Chapter 7

Company taxation

Company taxation

All domestic companies are liable to tax in India on their global income, while foreign companies are liable to tax in India with respect to income received or deemed to be received in India, or income accruing or deemed to be accruing in India. The effective corporate tax rate (base rate + surcharge + education cess) depends on the type of the company i.e. domestic or foreign and the quantum of its taxable income in the previous year. The year refers to the financial year (FY) beginning on 1 April and ending on 31 March; previous year means the previous financial year. The rate of tax and surcharge and cess could be changed by the Finance Act passed every year by the Indian government.

The corporate tax structure for FY 2015-16 is as follows:

Particulars	Taxable income > INR 100 million	INR 10 million < taxable income < INR 100 million	Other cases
Domestic company	34.608% (30% base rate + 12% surcharge + 3% education cess)	33.063% (30% base rate + 7% surcharge + 3% education cess)	30.90% (30% base rate + 3% education cess)
Foreign company	43.26% (40% base rate + 5% surcharge + 3% education cess)	42.02% (40% base rate + 2% surcharge + 3% education cess)	41.20% (40% base rate + 3% education cess)

The Income Tax Act, 1961 (ITA) also provides for tax on 'book profits' in case the tax on the company's book profit (post certain adjustments) is greater than the tax on income computed as per the normal provisions of the ITA. This is commonly known as MAT (Minimum Alternate Tax) which is charged @ 18.5% on book profits plus applicable surcharge and 3% education cess on the tax and surcharge. The limits for applicability of the surcharge are the same as mentioned in the table above. Credit for MAT paid can be carried forward and claimed against normal corporate tax payments arising in the future subject to a limitation period of 10 years. However, in case of income earned by FIIs/FPIs and foreign companies, from various sources such as capital gains, interest, royalty and fees for technical services, MAT provisions will not be applicable from FY 2015-16 onwards.

Apart from the above, foreign companies engaged in the business of shipping, exploration of mineral oils, operation of air craft and civil construction in relation to turnkey power projects can opt for presumptive taxation where income is taxed at a certain fixed percentage of the gross receipts and then the above referred corporate tax, surcharge and cess would be applied.

In addition to corporate tax, Dividend Distribution tax (DDT) is levied on all companies on the payment or distribution of dividend. The effective rate of DDT is 20.36% (17.65% base rate + 12% surcharge + 3% education cess).

Resident companies

A company incorporated in India under the Companies Act, 1956/2013 would always be a 'resident' in India. A foreign company is regarded as a 'resident' in India only if, during the previous year, its place of effective management (POEM) is situated in India (i.e. key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance, made in India). This would imply that a foreign company would be treated as a resident if, during the previous year, the control and management of its affairs is either wholly or partly situated in India.

Tax incidence on companies depends on their residential status:

Particulars	Resident	Non-resident
Income received or deemed to be received in India	Taxable	Taxable
Income accruing or arising or deemed to accrue or arise in India	Taxable	Taxable
Income accruing or arising outside India from: <ul style="list-style-type: none">• Business controlled in India or profession set up in India• Any other source	Taxable	Not taxable
	Taxable	Not taxable

Thus, if a foreign company can prove that its POEM is wholly outside India, only then can it avoid taxation of global income; and only its income accruing or arising in India or deemed to accrue or arise in India or received in India would be taxable.

Wealth tax

Wealth tax legislation has been abolished from FY 2015-16 onwards.

Foreign companies

Income tax

Under the ITA, a foreign company is liable to income tax in India on income received in India or income accruing or arising in India or deemed to accrue or arise in India.

Income deemed to accrue or arise in India would include:

- Income arising from a business connection in India or a property or asset or source of income in India;
- Capital gains from the transfer of capital assets situated in India; and
- Interest, royalties and fees for technical services received from a resident.

An asset or capital asset being any share or interest in a foreign company is deemed to be situated in India if it derives its value, directly or indirectly, substantially from assets situated in India. Accordingly, any indirect transfer of such shares would also be taxable in India. In order to provide clarity, the criteria when such taxation would trigger has been laid down from FY 2015-16 onwards. The criteria are as follows:

- Share of a foreign company shall be deemed to derive substantial value from Indian assets if the fair value of the Indian assets:
 - exceeds INR 100 million; and
 - the said value is equal to or greater than 50% of the value of all assets owned by the foreign company;
- The fair value of assets (without deduction of liabilities against such assets) to be decided as per rules which are to be prescribed;
- Amount to be taxed in India to be proportional to the value of Indian assets to global assets of the foreign company;
- Exemption provided from indirect transfers to:
 - small shareholders i.e. shareholders who hold less than 5% voting power/share capital and do not have management or control
 - foreign amalgamations and demergers, subject to certain conditions;
- An Indian company whose ownership or control gets transferred directly or indirectly would be required to report such a transaction to the tax authorities.
 - Failure of reporting will attract a penalty of 2% of the transaction value in case the transfer has the effect of transferring the right of management or control;

- In other cases, INR 500,000.

Taxability of business income

In case non-residents have a business connection/permanent establishment (PE) in India, income attributable to such business connection/PE would be taxable in India @ 40% (plus applicable surcharge and education cess). However, while calculating the taxable income, deduction for the expenses incurred for earning such income and some part of general administrative expenses are allowed as an expense.

Business connection includes any business activity carried out by a non-resident through a person or a person acting mainly or wholly on its behalf.

PE means some presence in India in the form of fixed place, employee presence, etc. through which business activities are carried in India by the non-resident.

Where a non-resident constitutes a business connection/PE in India, it is required to carry out compliances as required of a domestic company (i.e. maintaining books of accounts, getting accounts audited, various regulatory filings, etc).

Fund managers in India not to constitute business connection or PE

- To date, the presence of a fund manager in India was deemed to constitute a business connection in India even though the fund manager was an independent person. Thus, when the manager located in India undertook any fund management activity with respect to investments outside India for an off-shore fund, the profits earned by the fund from such investments could be liable to tax in India.
- It is clarified as per the Finance Act, 2015 that the presence of a fund manager in India will not give rise to a business connection/PE in India in respect of offshore funds subject to the fulfilment of certain conditions and compliances by both the offshore fund and the fund managers.

Presumptive taxation

As stated earlier, the ITA also provides for a mechanism wherein income in case of specified businesses such as shipping, aircraft, civil construction, etc. is computed on a presumptive basis, which results in a lower effective tax rate.

Taxability of income (other than business income) under the Income Tax Act

- Royalty/Fees for Technical Services: Income earned by a foreign company in the nature of royalty/fees for technical services is taxable in India on a gross basis @ 10% (plus applicable surcharge and education cess).
- Interest: Interest income earned by non-residents for loans provided in a foreign currency is taxable in India @ 20% (plus applicable surcharge and education cess).

However, the interest from foreign currency loans and any long-term bonds would be taxable at a concessional rate of 5% (plus applicable surcharge and education cess) provided the loan or bonds are acquired during a specified period and subject to specified conditions. Further, the said concessional rate of 5% would apply even if the non-resident does not have a Permanent Account Number (PAN) in India.

- Dividend: Dividend income received from an Indian company on which Dividend Distribution Tax is paid is exempt from tax in the hands of foreign companies.
- Other Income: Other income earned by foreign companies would be liable to be taxed at the maximum rate (i.e. 40% plus applicable surcharge and education cess).

However, with respect to the above, where a beneficial rate/provision is prescribed under any treaty entered into by India with a foreign country, a non-resident can claim such beneficial rate/provision subject to conditions mentioned under the treaty with the respective country.

Wealth tax

Wealth tax legislation has been abolished from FY 2015-16 onwards.

Tax returns and assessment

The Indian fiscal year as well as corporation tax year runs from 1 April to 31 March. All companies (irrespective of having made a profit or loss) are required to file their tax returns electronically by 30 September each year. However, for those that have entered into international transactions with associated enterprises or into Specified Domestic Transactions (SDT) (see section [Transfer Pricing](#)), the due date to file tax returns electronically is 30 November.

Even foreign companies are required to file tax returns with respect to income earned in India except in certain specified circumstances where income consists of dividend, specified interest, and due taxes have been withheld on the same. Tax returns must be digitally signed by the Managing Director of the company and in case the company does not have one, then by any director. However, in case of a foreign company, the tax return can be digitally signed by an individual holding a valid power of attorney.

It is mandatory for the company and the signatory to get a PAN in India.

The company is also required to obtain and furnish electronically the report of a Chartered Accountant in respect of its transaction with the Associated Enterprise. Similarly, it must obtain and furnish electronically the report of a Chartered Accountant if its annual turnover exceeds INR 10 million.

In case of any error or omission in the tax returns, the same can be revised within two years from the end of the relevant fiscal year or before the completion of the tax assessment, whichever is earlier. Similarly, a belated tax return can be filed within a period of two years from the end of the relevant fiscal year or the completion of the tax assessment, whichever is earlier. In case of a belated tax return, the company cannot carry forward its tax losses and it also loses the right to revise its tax return.

Revenue audits

Tax returns filed by companies can be subjected to a revenue audit, popularly known as a scrutiny assessment in India. The tax authorities lay down certain parameters every year and if a company fits those parameters, it would mandatorily be selected for assessment. For other companies, the same is based on random selection through the computer-aided selection systems (CASS). In the assessment proceedings, the tax authorities could either accept the income as in the return if they are satisfied with the correctness of the income and expenditure, or make adjustments to the income either by increasing revenues or disallowing the expenditure. A company can file an appeal against the adjustments made. There is an exhaustive and robust appeal mechanism and tax judiciary system in India.

Profits subject to tax

The taxable income for a business is computed in accordance with the common business or accounting principles to which necessary tax adjustments in accordance with the ITA are required to be made. Profits from the business are chargeable to tax on a receipt or accrual basis as per the accounting method adopted by the assessee. However, companies have to offer the profits to tax on an accrual basis as the Indian Companies Act does not allow them to follow the cash system of accounting. Principally, deductions are allowed for all business-related revenue expenses incurred during the fiscal year. Capital expenses (other than those specifically allowed) and personal expenses are not deductible. The onus of proving that the expenditure has been incurred wholly and exclusively for the purpose of the business is squarely on the company. Furthermore, any expenditure that is considered against public policy is not allowable as a deduction. In case of fixed assets,

depreciation is available at prescribed rates and in accordance with the provisions of the ITA. Certain revenue expenditures that are necessary to bring the fixed asset into its existing condition have to be added to the cost of the fixed asset. Certain specified expenses are allowable only on the basis of actual payment irrespective of the accrual system of accounting followed by the company. The following sections of this Chapter cover some specific allowable and disallowable deductions in calculating taxable business profits.

Employee taxes

An employee is liable to pay taxes on the salary earned by him/her. For an income to be regarded as 'salary', it is imperative to have an employer-employee relationship. The income under the head 'salary' is liable to tax either on a receipt basis or accrual basis, whichever event is earlier. It would also include arrears of salary.

Components of salaries mainly include basic salary, fees, commission, bonus, retirement benefits, contribution for social security in excess of the specified limits, allowances, perquisites, etc. Perquisites are benefits provided in kind and would, *inter alia*, include rent-free accommodation, interest-free loans or subsidised loans, provision of movable assets for use or transfer of such assets to the employees at subsidised cost, free or concessional education, provision of motor cars, provision of domestic help, club membership, etc.

The ITA also provides for several exemptions and deductions while computing income under the head 'salaries'. These, *inter alia*, include medical reimbursement, conveyance allowance, professional taxes paid, house rent allowance subject to specified limit and conditions, etc. The mechanism of calculating the exempt allowances is based on the Income Tax Rules. However, the quantum of deduction and/or exemption is not very significant and most of the limits specified in the ITA/Rules have outlived their utility.

Employers are required to compulsorily withhold tax on taxable salary if income exceeds the minimum exemption limit. Tax is to be withheld at an average rate based on the estimated income of the employee for the whole year at the time of actual payment of salary every month. While calculating the estimated income of the employee, the applicable deductions and exemptions are also considered.

Calculating trading profits

Trading profits represent profits as per the Profit and Loss Account drawn in accordance with the provisions of the Indian Companies Act, which is further adjusted considering the admissible/inadmissible expenses as per the provisions of the ITA (see section [Profits subject to tax](#)).

According to the ITA, for the purpose of calculating profits, all incomes accrued/earned during the fiscal year should be considered. Capital receipts are not considered while calculating trading profits. However, what constitutes a capital receipt is a matter of considerable litigation.

As explained earlier, capital expenses are not deductible. However, the ITA has prescribed certain capital expenses that can be allowed as deductions, but over a period of time. For example:

- Preliminary expenses incurred prior to the set up of or in connection with the extension of the business are allowed over a period of five years subject to certain conditions;
- Expenditure incurred on amalgamation is allowed over a period of five years;
- Expenditure on the prospecting of certain minerals is allowed over a period of 10 years;
- Expenditure on obtaining a telecommunication licence over the licence period.

Furthermore, according to the ITA, certain capital expenditures are allowed in the year that they are incurred in. For example:

- Capital expenditure on scientific research related to the business carried on by the company;
- The entire capital expenditure in case of specified businesses that have commenced in the specified time period;

- Weighted deduction of 200% in case of expenditure on an in-house scientific research and development facility as approved by the prescribed authority, which *inter alia* includes capital expenditure except that on land and building.

Similarly, a company is eligible to claim depreciation on fixed assets according to the rate prescribed in the Income Tax Rules. A company is also eligible to claim bad debts, provided the sales in respect thereof have been offered to tax either in the same previous year or in the earlier previous year.

Besides allowing the claim for expenditure, the ITA also allows claims for business losses provided they are in the revenue field and discovered in the year under consideration. Examples of business losses are loss on account of obsolete stock, loss on account of fire/theft/burglary/fraud, etc.

The ITA also restricts the allowance of certain revenue expenses, if certain requirements are not met:

- If tax is not withheld on domestic payments and deposited in the government treasury within the prescribed time, 30% of the expense claimed by the company shall be disallowed. The said 30% of the expense can be claimed by the company in year in which the due tax has been paid.
- Certain statutory expenses in the nature of tax, duty, cess or fees, are not allowed as deduction unless they are actually paid either during the year or up to the time allowed to file tax returns.

Certain expenses are expressly not allowed while computing taxable income. For example:

- Tax on profits, tax on capital (wealth tax);
- Tax paid by an employer on behalf of an employee on non-monetary perquisites;
- Expenditure incurred with respect to exempt income – a controversial provision.

The computation of trading/business profits for tax purposes would be as follows:

	Particulars	Amount (INR)	Amount (INR)
A.	Net Profit as per Profit and Loss Account		XXX
B.	Inadmissible Expenses debited to Profit and Loss Account		
	Disallowable expenses/claims	XXX	
	Depreciation as per the Companies Act	XXX	
	Deemed income not credited to Profit and Loss Account	XXX	XXX
C.	Total = (A + B)		XXX
D.	Admissible Deduction		
	Allowable claims/deduction	XXX	
	Depreciation as per the Income Tax Act	XXX	
	Incomes chargeable under other heads credited to Profit and Loss Account	XXX	XXX
E.	Profits and Gains of Business or Profession (C – D)		XXX

Income Computation and Disclosure Standards (ICDS)

The Indian government has notified 10 Income Computation and Disclosure Standards (ICDS) that are applicable for computing income chargeable as 'Business income' and 'Income from other sources'. ICDS would be applicable to both residents as well as non-residents, to individuals as well as companies. Furthermore, with the introduction of separate standards for income tax, this would not result in maintaining separate books of accounts for income tax purposes. However, a reconciliation statement would have to be prepared to keep track of the differences. In case of any conflict, the provisions of the ITA would prevail over the ICDS. In such a scenario, whether the interpretation of law rendered by higher courts in India would also prevail over ICDS would be a litigative issue.

The 10 ICDS that would be applicable to both residents and non-residents are as follows:

- ICDS I relating to accounting policies
- ICDS II relating to valuation of inventories
- ICDS III relating to construction contracts
- ICDS IV relating to revenue recognition
- ICDS V relating to tangible fixed assets
- ICDS VI relating to the effects of changes in foreign exchange rates
- ICDS VII relating to government grants
- ICDS VIII relating to securities
- ICDS IX relating to borrowing costs
- ICDS X relating to provisions, contingent liabilities and contingent assets.

Interest deduction

Interest on capital borrowed for the purpose of business or profession is allowed as a deduction. However, interest payable on capital borrowed for acquiring a capital asset for extension of business or a new business, until the date such asset is first put to use, is not allowable as a revenue deduction. Such interest shall be loaded on the cost of the capital asset and would be eligible for depreciation. Utilisation of loans is an important factor in deciding the allowability of interest on the same. Interest on borrowings utilised for granting interest-free advances to related parties or sister concerns may not be allowed, if the business expediency of such advance is not proved. Furthermore, interest on borrowings utilised for the purpose of earning tax-free income (e.g. dividend income) would be disallowed due to special provisions of the ITA.

Thin capitalisation rules

A number of jurisdictions across the globe have specific thin capitalisation rules to deter erosion of the tax base through excessive debt and thereby excessive interest payments. There is no specific thin capitalisation provision under the ITA. As there are no enabling provisions to question whether a business should have raised funds through equity instead of a loan, interest deduction is allowed solely on the basis of principles laid down in the above paragraph. Interest payments to overseas related parties and in some specific instances to domestic related parties would, however, be subject to transfer pricing provisions. Furthermore, with effect from 1 April 2017, if the transaction of debt is construed by the tax authorities as solely for the purpose of tax benefit then the arrangement could be examined and disregarded under the General Anti-Avoidance Rules (GAAR).

Capital assets

According to the ITA, capital assets have been defined to mean property of any kind including, business assets but excluding stock-in-trade and moveable personal effects such as wearing apparel, personal furniture, personal car, etc. Thus, broadly 'capital assets' can be classified as business-related assets and personal capital assets excluding the ones specified above. Business-related capital assets can be further classified as 'depreciable capital assets' and 'non-depreciable capital assets'.

The tax treatment of personal capital assets and non-depreciable assets has been dealt with separately in the section [Capital Gains Tax](#). The tax treatment of 'depreciable capital assets' is explained here:

According to the ITA, depreciation for tax purposes has to be calculated on the Written Down Value (WDV) of the 'block of assets' at the prescribed rates (except for undertakings engaged in the generation or generation and distribution of power, that have the option of claiming depreciation on a straight line basis). A 'block of assets' has been defined as a group of assets falling within a class of assets comprising of 'tangible' and 'intangible' assets in respect of which same percentage of depreciation is prescribed.

The rates of depreciation are given in the following table:

Asset class	Rate of depreciation (%)
General plant and machinery	15
Cars other than those used in the business of running them on hire	15
Computers (including software)	60
Purely temporary erections	100
Residential buildings	5
Buildings other than above	10
Furniture and fittings including electrical fittings	10
Ships	20
Intangible assets: knowhow, patents, copyrights, trademarks, licences, franchises or any other business or commercial right of similar nature	25

The WDV of a block of assets is calculated as under:

First year:

Cost of the asset at the time of acquisition of assets		XXX
Less: Depreciation as calculated based on the above rates	XXX	
Closing WDV of the block of assets		XXX

Subsequent year:

Opening WDV of the block at the beginning of the next year		XXX
Add: Actual cost of assets acquired during the year		XXX
Less: Sales proceeds from the disposal of any asset during the year	XXX	
WDV for the purpose of calculating depreciation		XXX

The actual cost of a depreciable asset comprises its purchase price (including import duties and other non-refundable taxes or levies) and any directly attributable cost of bringing the asset to its working condition for its intended use.

The sale of an individual depreciable asset does not result in any capital gains as long as the sales proceeds of those individual assets are less than the WDV of that particular 'block of assets'. If the sales proceeds are more than the WDV of the 'block of assets' then the resultant gain is regarded as a 'deemed short-term capital gain' irrespective of the holding period of the individual assets and would be chargeable to tax at the normal corporate tax rate.

The concepts of short-term and long-term capital gains are explained in the section on [Capital Gains Tax](#). This concept of taxation differentiates capital gains on depreciable assets as compared to capital gains on non-depreciable assets and personal assets.

Furthermore, additional or accelerated depreciation @ 20% is allowed to taxpayers engaged in the manufacture or production of any article or product in the year in which new plant and machinery acquired is first put to use.

Double taxation relief

India allows relief from double taxation of income in the following ways:

Unilateral relief: A resident of India deriving income from a country with which India does not have a tax treaty is eligible to claim credit for taxes paid in the foreign country. However, such credit would be restricted to Indian taxes on such foreign income or actual foreign taxes paid, whichever is less.

Bilateral relief: India has a comprehensive tax treaty network with more than 120 countries to avoid double taxation of income. Under the Indian tax laws, a taxpayer can avail the provisions of the tax treaty or domestic tax laws, whichever is beneficial to the taxpayer. Typically, bilateral relief is provided through the 'credit method' or 'exemption method'. To avail beneficial provisions of a tax treaty, non-resident companies and entities are required to obtain a valid Tax Residency Certificate (TRC) from the government of the country of residence along with other prescribed documents and information.

Withholding tax

Withholding tax, known as tax deducted at source (TDS) in India, aims to collect revenue at the very source of income. Its significance to the government lies in the fact that this tax is collected in advance, it ensures a regular source of revenue, provides for a greater reach and widens the tax base. The ITA requires the payer to withhold tax at source at:

- the appropriate rate considering the nature of payment and status of the recipient i.e. corporate or non-corporate assessee;
- the time of payment or credit of the amount, whichever is earlier, except salary payments where tax is required to be deducted only on actual payment of salary.

Please see [Appendix 1](#) for TDS rates on some common payments to residents and [Appendix 2](#) for TDS rates on payments made to non-residents and foreign companies.

If the rates prescribed in a tax treaty are lower than the rates in the table in [Appendix 2](#), the lower rates can be adopted. A person availing the treaty benefit is required to furnish the Tax Residency Certificate (TRC) as stated earlier and is also required to give a declaration in the specified form.

If the recipient does not have a Permanent Account Number (PAN) in India, TDS would be the maximum of the:

- tax rate prescribed in the ITA, or
- rates in force (i.e. tax rate specified in the Finance Act or the rate specified in the treaty, whichever is lower), or
- 20%.

The person deducting the tax has a tedious compliance burden post deduction of tax as follows:

- In case of expenses other than salary, deposit the tax within seven days from the end of the month in which tax has been deducted except in case of tax deduction for the month of March. In respect of tax deducted in March, the due date of payment is 30 April.
- In respect of TDS on salary, the same timeline as specified above applies except that even for the month of March, tax needs to be deposited by 7 April.
- Apart from the deposit of taxes, a corporate is required to file the statement of TDS within 15 days from the end of each quarter, specifying the details of taxes paid and the deductees on whose behalf the taxes were paid. However, for the quarter ending March, the due date is 15 May and not 15 April. This statement is required to be filed separately in three different forms for salary payments, payments to non-residents and all other payments.
- A corporate is also required to issue a TDS certificate to the persons from whose payments the tax has been deducted within the specified time.

There are stringent penal provisions, including prosecution, for not complying with these TDS provisions.

Capital Gains Tax (CGT)

According to the ITA, an assessee is chargeable to pay capital gains tax on transfer of 'capital assets'. See the section on [Capital assets](#) for the definition of the term. The rate of capital gains tax depends on whether the capital asset is a short-term or long-term capital asset.

Any capital asset held for less than 36 months is regarded as a short-term capital asset; otherwise it is considered to be a long-term capital asset. However, securities listed on a recognised stock exchange in India, units of an equity-oriented mutual fund, and zero-coupon bonds held for more than 12 months are considered as long-term assets.

The sale of capital assets is taxable based on the following rate structure:

	Particulars	Tax rates*
		Resident and non-residents
1	Sale of short-term capital assets: listed equity shares and units of equity-oriented mutual funds, which have been charged to Securities Transaction Tax (STT) in India	15%
2	Sale of short-term capital assets: other than the above	Based on corporate tax rate/individual tax rate
3	Sale of long-term capital assets: listed equity shares and units of equity-oriented mutual funds, which have been charged to STT in India	Exempt
4	Sale of long-term capital assets: listed securities or zero-coupon bonds, which have not been charged to STT	If costs are not adjusted for inflation – 10%
		If costs are adjusted for inflation – 20%
5	Sale of long-term capital assets: other than those mentioned in points 3 and 4 above	20% with adjustment for inflation

*applicable surcharge and education cess @ 3% shall also be levied.

However, exceptions in case of taxability of capital gains in the hands of a non-resident are:

- Capital gains arising from the transfer of a capital asset, being shares and debentures of an Indian company that have been initially purchased and sold in foreign currency, are required to be computed in the foreign currency and the net gain in foreign currency would be converted to Indian Rupees considering the prevailing exchange rate on the last day of the month immediately preceding the month in which the capital asset is transferred. Furthermore, the cost of such capital assets cannot be adjusted for inflation in spite of the same being a long-term gain.
- Long-term capital gains arising from the transfer of unlisted securities would be chargeable to tax @ 10%. However, the cost of the said asset cannot be adjusted for inflation.

Transfer of capital assets as a consequence of amalgamation, demerger or business reorganisation, in compliance with conditions of the Indian income tax law is not taxable in India.

Capital gains arising on account of long-term capital assets are also exempt up to INR 5 million, if the gain is invested in specified bonds within six months of the transfer of the long-term capital asset. Also, there are a few other avenues available to save tax on capital gains in case of an individual.

Tax losses

The ITA deals with the losses arising under the following heads of income:

- Losses under the head 'income from house property'
- Losses under the head 'business income', further split into 'business loss' and 'unabsorbed depreciation'
- Losses under the head 'speculation business income'
- Losses under the head 'capital gains', further classified into 'long-term capital loss' and 'short-term capital loss'
- Losses under the head 'income from other sources'

These losses are computed under the different provisions of the ITA and there are various provisions governing the set off and carry forward of such losses. The losses under the head 'income from house property' and 'business income' can be set off against income from any other head computed for the same year. However, losses under the head 'speculation loss' and 'capital loss' can be set off only against the speculation gain and capital gain respectively computed for the year. This is shown in the following table:

Loss under the head	Can be set off against						
	Salaries	Income from house property	Business income	Speculation business income	Short-term capital gains	Long-term capital gains	Income from other sources
Loss from house property	✓	✓	✓	✓	✓	✓	✓
Business loss	X	✓	✓	✓	✓	✓	✓
Speculation business loss	X	X	X	✓	X	X	X
Unabsorbed depreciation	✓	✓	✓	✓	✓	✓	✓
Short-term capital loss	X	X	X	X	✓	✓	X
Long-term capital loss	X	X	X	X	X	✓	X
Loss from income from other sources	✓	✓	✓	✓	✓	✓	✓

Also, there are restrictions on the utilisation of tax losses under each head when they are carried forward to subsequent years, as shown in the following table:

Loss under the head	Can be set off against						
	Salaries	Income from house property	Business income	Speculation business income	Short-term gains	Long-term gains	Income from other sources
Loss from house property	X	✓	X	X	X	X	X
Business loss	X	X	✓	✓	X	X	X
Speculation business loss	X	X	X	✓	X	X	X
Unabsorbed depreciation	✓	✓	✓	✓	✓	✓	✓

Short-term capital loss	X	X	X	X	✓	✓	X
Long-term capital loss	X	X	X	X	X	✓	X
Loss from income from other sources	X	X	X	X	X	X	X

There are specific provisions for carrying forward losses with respect to the head of income against which they can be set off and the time limit for each:

Nature of loss	Can be set off against	Number of years that it can be carried forward for
Business loss	Business income	8 years
Speculation business loss	Speculation profits	4 years
Unabsorbed depreciation	Against any head of income	Indefinite
Short-term capital loss	Capital gain (short-term or long-term)	8 years
Long-term capital loss	Long-term capital gain	8 years
Loss from house property income	Income from house property	8 years
Loss from income from other sources	Not applicable	Cannot be carried forward

It is pertinent to note that closely held companies are required to satisfy a 51% continuity of ownership criteria for carrying forward business losses.

General anti-avoidance provisions

In an effort to curb tax avoidance and evasion, the Indian government introduced the General Anti-Avoidance Rules (GAAR) in the Income Tax Act. GAAR will be implemented from FY 2017-18 i.e. 1 April 2017. Once GAAR comes into effect as proposed, it will empower the tax authorities to declare an arrangement as an impermissible avoidance arrangement (IAA) if it was entered into with the main purpose of obtaining a tax benefit. Once an agreement is declared to be an IAA, the tax authorities will be entitled to, *inter alia*, re-characterise the transaction, ignore the transaction, disregard accommodating parties, reallocate income/expenses, etc.

Planning points for foreign investors

According to Indian exchange control regulations, a foreign business can have a presence in India in the form of a liaison office, branch office, project office, company and limited liability partnership (LLP).

The factors to be looked at are as follows:

Particulars	Liaison office	Branch office and Project office	Subsidiary company	Limited liability partnership (LLP)
Regulatory approval	Reserve Bank of India (RBI) ¹¹⁴ , Registrar of	RBI, ROC and local registrations	ROC and local registrations	Prior approval of the Indian government and

¹¹⁴ Could be under automatic or approval route involving post-facto intimation or prior approval, respectively

	Companies (ROC) and local registrations			Foreign Investment Promotion Board
Rate of tax ¹¹⁵	Nil (since it is not permitted to carry out any revenue-generating activity)	Normal tax rate – 40% of net taxable income. Minimum Alternate Tax (MAT) ¹¹⁶ – 18.5% of adjusted book profits.	Normal tax rate – 30% of net taxable income. MAT – 18.5% of adjusted book profits.	Normal tax rate – 30% of net taxable income. Alternate Minimum Tax (AMT) ¹¹⁷ – 18.5% of adjusted book profits.
Long-term capital gain tax rate ¹¹⁸	Not applicable (since it is not permitted to carry out revenue-generating activity)	Nil ¹¹⁹ 10% ¹²⁰ 20% ¹²¹	Nil ¹²² 10% ¹²³ 20% ¹²⁴	Nil ¹²⁵ 10% ¹²⁶ 20% ¹²⁷
Advance tax payment	Not applicable (since it is not permitted to carry out revenue-generating activity)	To be paid in four instalments	To be paid in four instalments	To be paid in three instalments
Minimum capital norm	Not applicable (funded by Head Office)	Not applicable (funded by Head Office/internal accruals)	No minimum capital	No minimum capital
Repatriation of profits	Not applicable	No further tax on repatriation of profits	Subject to Dividend Distribution Tax of 20.36%. Exempt in the hands of shareholders.	No further tax on repatriation
Transfer pricing regulations	Not applicable	Applicable	Applicable	Applicable
Permanent establishment (PE)	Generally, do not constitute PE, but litigation exists	Constitutes PE and a taxable presence under a tax treaty or Income Tax provisions	An independent taxable entity and not a PE of foreign company. However, where working as a shell/conduit entity, it may constitute a PE.	Should not constitute PE. However, whether interest in LLP results in PE is still ambiguous.

¹¹⁵ Excluding surcharge and education cess

¹¹⁶ MAT is designed to ensure that no company with substantial accounting income can avoid tax liability by using exclusions, deductions and incentives available under the Income Tax Act

¹¹⁷ AMT is similar to MAT and is applicable to non-corporate bodies only if they are claiming incentive linked or profit linked deduction

¹¹⁸ Excluding surcharge and education cess

¹¹⁹ Transfer of equity shares/unit of an equity-oriented fund which attracts Securities Transaction Tax (STT)

¹²⁰ Transfer of unlisted securities (without benefit of indexation and foreign currency fluctuation)

¹²¹ Other cases

¹²² Transfer of equity shares/unit of an equity-oriented fund which attracts STT

¹²³ Transfer of listed securities (other than units) or zero-coupon bonds without indexation benefit

¹²⁴ Other cases

¹²⁵ Transfer of equity shares/unit of an equity-oriented fund which attracts STT

¹²⁶ Transfer of listed securities (other than units) or zero-coupon bonds without indexation benefit

¹²⁷ Other cases

Applicable surcharge and education cess	Not liable to tax	<p>Surcharge:</p> <p>Total income of:</p> <p>Up to INR 10 million – Nil</p> <p>Up to INR 100 million – 2%</p> <p>Above INR 100 million – 5%</p> <p>Education cess @ 3%</p>	<p>Surcharge:</p> <p>Total income of:</p> <p>Up to INR 10 million – Nil</p> <p>Up to INR 100 million – 7%</p> <p>Above INR 100 million – 12%</p> <p>Education cess @ 3%</p>	<p>Surcharge:</p> <p>Total income of:</p> <p>Up to INR 10 million – Nil</p> <p>Above INR 10 million – 12%</p> <p>Education cess @ 3%</p>
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Investment via shares or loans

A foreign corporation can fund its Indian subsidiary by infusing share capital (FDI) or by extending a loan (external commercial borrowing (ECB)). Both FDI and ECBs can be availed by the Indian subsidiary subject to fulfilment of prescribed exchange control regulations. Key tax implications of FDI/ECBs are:

- Repatriation of capital: Foreign capital invested in India is generally allowed to be repatriated along with capital appreciation, if any, after payment of taxes due on them, provided the investment was made on a repatriable basis. The repatriation is, however, subject to lock-in conditions in certain sectors.
- Repatriation of dividend: A company is liable to pay Dividend Distribution Tax (DDT) @ 20.36% (including surcharge and education cess) on the amounts declared or distributed as dividend. Such dividends are not taxed in the hands of the recipient.
- Payment of interest on ECBs: Subject to certain conditions, withholding tax on ECBs (wherever allowed) has been reduced from 20% to 5% (with applicable surcharge and cess) for ECBs availed between 1 July 2012 and 1 July 2017. Furthermore, the concessional rate of 5% would apply even in case the non-resident does not have a PAN in India.

Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs)

The Finance (No. 2) Act, 2014 introduced a taxation regime for business trusts – REITs and InvITs. These business trusts give small investors access to large-income-producing real estate and infrastructure assets, much like how mutual funds provide access to stocks. The Securities and Exchange Board of India (SEBI) issued guidelines for regulating such business trusts and an investor can enter the property market with as little as INR 200,000. Both these models have the following distinctive elements:

- The trust would raise capital by issuing units, which would be listed on recognised stock exchanges in India;
- The trust can raise debt from residents as well as non-residents;
- Income-bearing assets would be held by the trust by acquiring controlling or other specific interest in an Indian company (special purpose vehicle (SPV)) from the sponsor (promoters of the SPV).

Furthermore, the proposed taxation regime of such business trusts would, *inter alia*, include the following:

- No capital gains tax on the sponsor at the time of exchange of shares of the SPV with the units of the trust.
- The current beneficial regime of capital gains tax available on listed shares would also apply to such units for their holders, including the sponsor.
- Capital gains on the disposal of other assets by the trust shall be taxable in the hands of the trust. However, the same would not be taxable in the hands of the unit holders at the time of distribution.
- Dividend received by the trust from the SPV (which is subjected to DDT) would be exempt from tax at the time of receipt as well as distribution to unit holders by the trust.
- Interest and rental income received by the trust from the SPV is accorded pass-through status. Accordingly, this interest and rental income would not be chargeable to tax in the hands of the trust. However, at the time of distribution of this interest to investors of the business trust, taxes would be required to be withheld as per the ITA.

- Other income of the trust shall be taxable at the maximum marginal rate (i.e. 30%).

In addition, certain other reporting compliances like filing of tax returns, etc. would be required to be undertaken by business trusts.

Alternative Investment Funds (AIFs)¹²⁸

An AIF is any fund established or incorporated in India in the form of a trust, company, limited liability partnership or a body corporate that is a privately pooled investment vehicle, which collects funds from investors, whether Indian or foreign, for investing it in accordance with a defined investment policy for the benefit of its investors.

Category I AIFs are those that invest in start-up or early-stage ventures, social ventures, SMEs, infrastructure, other sectors or areas that the government or regulators consider as socially or economically desirable and shall include venture capital funds, SME funds, social venture funds, infrastructure funds and such other AIFs as may be specified. AIFs that are generally perceived to have positive spillover effects on the economy and for which the Board or government or other regulators in India might consider providing incentives or concessions shall be included, and such funds that are formed as trusts or companies shall be construed as 'venture capital company' or 'venture capital fund' as specified in the ITA.

Category II AIFs are those that do not fall in Category I and III and do not undertake leverage or borrowing other than to meet day-to-day operational requirements and as permitted in the regulations. AIFs such as private equity funds or debt funds for which no specific incentives or concessions are given by the government or any other regulator shall be included.

Category III AIFs are those that employ diverse or complex trading strategies and may employ leverage including through investment in listed or unlisted derivatives. AIFs such as hedge funds or funds which trade with a view to make short-term returns or such other funds which are open-ended and for which no specific incentives or concessions are given by the government or any other regulator shall be included.

From FY 2015-16 onwards, a special tax regime for Category I and II AIFs has been provided, irrespective of whether they are set up as a trust, company, LLP or as any other body corporate:

- Any income (other than income from profits and gains of business) of the investment fund will be taxable in the hands of the unit holders and not the investment fund;
- Income from profits and gains of business of the investment fund shall be taxable in the hands of the investment fund only;
- Any losses of the investment fund shall be subject to set-off and carried forward to the subsequent years only at the fund level (i.e. it will not be passed on to the unit holders);
- Any income that is not taxable at the fund level and paid to unit holders by the investment fund would be subject to withholding @ 10%;
- Provisions of DDT or Tax on Distributed Income shall not be applicable to income paid by the investment fund to its unit holders;
- Any income of the investment fund would be exempt from TDS requirement. This would be provided by issuing the appropriate notification;
- It is mandatory for the investment fund to file its Return of Income. The investment fund shall also be required to provide to the prescribed income tax authorities and the investors, the details of various components of income, etc. for the purpose of the scheme.

This tax 'pass through' will step up the ability of these funds to mobilise higher resources and make higher investments in small and medium enterprises, infrastructure and social projects and provide the much required private equity to new ventures and start-ups.

¹²⁸ Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1337601524196.pdf, accessed 19 May 2015

Tax incentives

The Indian government, in order to accelerate economic growth, extends various direct and indirect incentives to the business community. Some incentives available under the ITA are as follows:

- India has robust tax treaties with many countries. Taxpayers have the option of availing benefits under a tax treaty to the extent it is more beneficial vis-à-vis the provisions of the ITA (subject to certain documentation requirements).
- The rate of withholding tax on interest on ECBs has been reduced from 20% to 5% subject to certain conditions.
- Profit- and investment-linked incentives:
 - For units located in Special Economic Zones (SEZs): 100% income tax exemption on export income for the first five years, 50% for the next five years, and 50% on the re-invested export profit for the next five years.
 - For SEZ developers: income tax exemption on income for a block of 10 years in 15 years.
 - Investment-linked incentives for specified activities/sectors such as:
 - Infrastructure
 - Oil and gas
 - Research and development activities
 - Activities in specified geographical areas
 - Cold storage, warehousing facilities for agriculture produce and sugar
 - Hotel, hospital and slum redevelopment or rehabilitation with certain restrictions.

However, the company will be liable to pay tax under the provisions of MAT wherever profit-linked and investment-linked incentives are available.

- Accelerated depreciation @ 20% available on new plant or machinery acquired and installed by an undertaking engaged in the manufacture of any article.
- In addition, an investment allowance of 15% on the cost of machinery is allowed to a manufacturing company investing a minimum of INR 250 million within a specified time frame and subject to conditions.
- From FY 2015-16 onwards, if the industrial undertaking is set up in notified backward areas of Andhra Pradesh, Bihar, Telangana, or West Bengal, the taxpayer would be eligible for 35% of additional depreciation on assets acquired and installed in these notified areas for such industrial undertakings.

Transfer pricing

Transfer pricing refers to inter-company pricing arrangements between related business entities and commonly applies to inter-company transfers of services and tangible/intangible properties. In India, detailed provisions relating to transfer pricing were introduced by the Finance Act, 2001 in order to facilitate the computation of reasonable, fair and equitable profits and tax in India in the case of businesses carried on by multinational companies. Simply put, transfer pricing is the process of adjusting the prices of cross-border transactions between related/associated parties.

Section 92 of the ITA provides that the price of any transaction between associated enterprises (AE), either or both of whom are non-residents for tax purposes (international transaction), shall be computed having regard to the arm's length principle. Subsequently, the Finance Act, 2012 also brought 'specified domestic transactions' where transactions are carried out between two related Indian entities under the purview of transfer pricing.

Two enterprises are considered to be associated if there is direct/indirect participation in the management or control or capital of an enterprise by another enterprise or by the same persons in both the enterprises.

In determining whether there is participation in management or control, various factors are taken into consideration including:

- Direct/indirect shareholding having 26% or more voting power
- Advancing of loans of 51% or more of total assets
- Appointment of more than 50% of the board of directors
- Goods manufactured sold under influenced prices
- Dependence on intellectual property rights owned by either party, etc.

An additional clarification was issued highlighting the concept of a 'deemed international transaction', thereby widening the scope of transfer pricing in India. This provision considers a transaction between two residents in India as an international transaction subject to certain conditions.

Determination of 'arm's length price'

A crucial aspect of transfer pricing is the process of determining the arm's length price (ALP). The Central Board of Direct Taxes (CBDT) has prescribed six methods for determining the ALP:

- Comparable Uncontrolled Price Method
- Resale Price Method
- Cost Plus method
- Profit Split Method
- Transactional Net Margin Method
- Other Method (via Notification No. 18/2012 dated 23 May 2012)

The 'other method' has been prescribed to potentially cover transactions involving intangibles and business restructurings for which the above methods may not be the most appropriate.

The choice of the appropriate method is determined with respect to the nature and class of transaction, the classes of associated persons, the functions performed by them and other relevant factors.

Also, the Finance Act, 2014 had proposed to introduce the range concept for determination of ALP and use of multiple-year data for comparable analysis of transactions. Subsequently, the CBDT clarified this with a draft scheme of the proposed rules dated 21 May 2015, which is open to the public for comments. These rules mention the manner and scope of computation of ALP when adopting the range concept and use of multiple-year data.

International transactions

Apart from routine transactions relating to the purchase and sale of goods and services, the Finance Act, 2012 enhances the definition to include transactions involving business restructuring, intangibles, goodwill, corporate guarantees, overdue debtors, etc. There is no threshold exemption limit for this compliance.

Also, it is mandatory to obtain an accountant's certificate in the prescribed format for all international transactions between AEs. This report would have to contain prescribed particulars of the transaction, and would have to be filed with the tax authorities by 30 November of the relevant assessment year, along with the tax return.

Stringent penal provisions have been prescribed for non-compliance with the prescribed requirements under the new transfer pricing regime.

Advance Pricing Agreements

- The Finance Act, 2012 introduced Advance Pricing Agreements (APAs). An APA is an agreement between a taxpayer and the tax authorities for specifying the manner in which the ALP is to be determined with respect to an international transaction.
- The ALP shall be determined on the basis of the prescribed methods or any other method.
- An APA would be valid for a maximum of five consecutive years unless there is a change in the provisions or the facts having a bearing on the international transaction.
- In March 2015, the CBDT introduced roll-back provisions according to which, an APA would also be applicable to international transactions undertaken in the previous four financial years subject to certain conditions.
- On 19 December 2014, India signed the first bilateral APA with Japan which would be valid for five years. The APA has been finalised within a time span of 1.5 years, which is significantly shorter than the time normally taken to finalise APAs internationally.

Chapter 8

Personal taxation

While companies contribute a considerable amount to the tax collected each year by the Indian government, contributions from individuals also form a vital element of the revenue.

Taxes as per the Indian Income Tax Act (ITA) are levied on *persons*, which includes individuals. The rates of taxation differ in each financial year (from 1 April to 31 March), and are usually lower than the corporate rate of taxation.

Residential status

It is crucial for an individual to determine their correct residential status since, in India, taxation for a particular year is dependent on the residential status in India for that year. The Indian tax law categorises the residential status of an individual as 'resident' or 'non-resident' depending on the number of days of stay in India.

An individual is considered to be a resident if they satisfy any of the following conditions:

- a) Been in India for a period of 182 days or more during that financial year; or
- b) Been in India for a period of 60 days or more during that financial year and at least 365 days during the preceding four years.

Further, in condition (b) above, the period of 60 days would be extended to 182 days in the following cases:

- An Indian citizen who leaves India in any year for the purpose of employment; or
- An Indian citizen who leaves India as a member of the crew on an Indian ship; or
- An Indian citizen or a Person of Indian Origin, who has settled abroad, visits India.

In the case of an Indian citizen, being a member of the crew of a foreign bound ship leaving India, the period or periods of stay in India shall, in respect of such voyage, be determined in the manner and subject to such conditions as may be prescribed.

An individual is classified as a non-resident if they do not satisfy either of the above conditions.

The law has further categorised the residential status of a 'resident in India' into 'resident and ordinarily resident' and 'resident and not ordinarily resident'. A person is said to be 'resident and not ordinarily resident' in India in any year if the person has:

- been a non-resident in India in 9 out of the preceding 10 years; or
- been in India for a period of, or periods amounting in all to, 729 days or less during the preceding 7 years.

Thus, if an individual fulfils any one of the above conditions, he would be regarded as 'resident and not ordinarily resident' in India for that particular financial year.

The actual number of days an individual is present in India is generally determined on the basis of entries in the passport, taking into account the day of entry as well as exit.

An individual considered to be a resident of India as well as another country can determine his residential status as per the criteria specified under the tax treaty, if any, entered into by the Indian government with the government of that other country.

Scope of taxation

Once the residential status has been determined based on the above conditions, taxation of income would be determined as follows:

Particulars of income	Resident and ordinarily resident	Resident and not ordinarily resident	Non-resident
Income received or deemed to be received in India	Taxable	Taxable	Taxable
Income accrues or arises in or deemed to accrue or arise in India	Taxable	Taxable	Taxable
Income earned outside India	Taxable	Taxable (only if earned from a business/ profession controlled from India)	Not taxable

According to this table, once it is determined that the income of the individual is taxable in India, the computation mechanism would be more or less similar for all individuals irrespective of residential status. However, there could be a few exceptions that must be looked at on a case-by-case basis.

How to compute tax – a broad structure

For tax purposes, income is broadly divided into different heads of income and different computation mechanisms have been prescribed for each head. The heads are:

- Income from employment/salary
- Income from house property (rental income)
- Income from business and profession
- Income from capital gains
- Income from other sources (viz. dividend, winnings from lotteries, gifts, family pensions, etc.)

After aggregating income under the various heads, the taxpayer can then reduce taxable income with certain allowable deductions. For example, an individual could claim deductions with respect to investments made in the public provident fund or payment of life insurance premium, medical health policy premium, certain mutual funds, etc. After these deductions, the resultant taxable income is required to be offered to tax at the rates prescribed in the law.

Income tax rates

The tax rate applicable to an individual would depend on his income bracket. Various income slabs along with different tax rates are provided every year in the Union Budget, generally presented to the Parliament of India on the last day of February. The slab rates mentioned in the Budget are applicable for the following financial year (April–March). For instance, the Union Budget 2015-16 has prescribed the following rates for individual taxpayers (other than senior citizens):

Income	Tax rate
Up to INR 250,000	Exempt
INR 250,001 to 500,000	10%
INR 500,001 to 1 million	20%
Above INR 1 million	30%

Furthermore, the law also provides special exemptions to 'resident senior citizens' (individuals who are more than 60 years of age) and 'resident very senior citizens' (individuals who are more than 80 years of age), where the basic exemption limit is INR 300,000 and INR 500,000, respectively. In addition to the above, individuals with a total income of INR 10 million or more in a year are liable to pay a surcharge @ 12%.

All taxes in India are further increased by an education cess, which is 3% of the total tax payable (tax plus surcharge).

You can know more about individual tax liabilities on the Income Tax Department's website, www.incometaxindia.gov.in.

Ways to discharge income tax liability

An individual can discharge his income tax liability in either or all of the options mentioned below:

- Advance Tax
- Tax Deducted at Source (TDS)
- Self Assessment Tax

Advance Tax

Advance tax means the payment of tax before the end of the year. An individual has to estimate their total income for that year and discharge tax liability in three instalments during the year itself i.e. 30%, 60% and 100% of the tax liability, which is due by 15 September, 15 December and 15 March of that year. However, an individual is liable to pay advance tax only under the following conditions:

- The tax liability is more than INR 10,000; and
- The above liability of INR 10,000 is arrived at after considering TDS if any deducted by payers who have paid income to such person.

For individuals with salary as the sole source of income, advance tax would not be applicable as the entire tax liability would be taken care of by the employer by way of TDS. Furthermore, no advance tax is payable by a senior citizen if their total income does not include income from business or profession.

Tax Deducted at Source (TDS)

TDS refers to the portion of a payment that is deducted by the payer before making payment of the net amount to the payee. The TDS rate would depend on the nature of the income earned by the individual. For example, TDS from professional fees would be 10% while that from contractual payments would be 2%. The TDS collected by the payer is required to be deposited with the tax authorities within prescribed time limits.

It is crucial to keep in mind that TDS is only a part payment of tax. The final tax liability would be arrived at based on the slab rates applicable to the individual.

For non-residents, TDS is applicable on any sum paid to them. For example, if a foreign individual receives a certain sum from an Indian company and such amount is taxable in India, then the Indian company is liable to deduct tax at the applicable rates and deposit the same with the authorities within the prescribed time limits.

Self Assessment Tax

In case the advance tax paid by the individual and the TDS are not adequate to cover the entire gross tax liability for the year then the same can be discharged by the individual himself before the tax return is filed. Such tax paid would be regarded as Self Assessment Tax.

Tax treatment of Employee Stock Option Plans (ESOP)

An increasing number of multinational companies prefer granting Employee Stock Option Plans (ESOPs) to their employees wherein they are granted an option to buy the shares of the employer company at a discounted rate, lower than the market value.

The taxation of ESOPs as per Indian laws happens in two stages. In the first stage, it is taxable in the hands of the employee as salary (perquisite given by the employer), which is represented by the difference between the fair market value (FMV) of the shares and the actual price at which they are purchased by the employees. The law lays down the procedure for determining the FMV of the shares. The point of taxability is the date on which the option is exercised by the employee to subscribe to the shares. Employers are liable to deduct tax at source on this part of the income.

The second stage of taxability arises when the said shares are sold or transferred. The difference between the sale price and the FMV (calculated in the earlier phase of taxation) is taxable as capital gains. The tax treatment of such capital gains would be as prescribed in the section [Capital Gains Tax](#) in Chapter 7.

Wealth tax

Wealth tax legislation has been abolished from FY 2015-16 onwards.

Electronic filing of tax returns

The past few years have seen a sea change in the process of filing tax returns in India. Now, most taxpayers are expected to file their tax returns electronically instead of manually – a major paradigm shift in tax administration in India.

The Indian tax department has set up a Central Processing Centre (CPC) – a state-of-the-art facility in Bengaluru that processes all tax returns that have been filed electronically. The CPC has been responsible for drastically reducing the time taken to process tax returns and issue refunds. As a result, a large number of taxpayers, particularly individuals, have started receiving their refunds within a few months of filing returns.

To know more on e-filing of income tax returns, you can visit www.incometaxindiaefiling.gov.in.

Personal taxation in India is dynamic and complicated with several interpretational and other issues. However, the scheme of law provides for many relaxations with a view to avoid unnecessary hassles for individual taxpayers and has simplified the process to encourage timely and correct tax return filing and payment.

Chapter 9

Indirect taxes

In India, indirect taxes levied by the central government include customs duty, excise duty, service tax, Central Sales Tax, etc. and those by the state governments include sales tax or VAT, entry tax, etc. Since the power to levy state taxes lies with the respective state governments, the tax rate and compliances of state-level taxes vary across states. In addition, there are a few local taxes, duties, cess, etc. at the Municipal level such as octroi, local body tax, cess, profession tax, etc.

Indirect tax rates

Levy	Tax rates	Remarks
Value Added Tax	Ranges from 0% to 20%	As per the schedule prevalent in each state
Central Sales Tax	2%	Against declaration form
Service Tax	14%*	Composition scheme rates also available
Excise Duty	12.5%	Peak rate
Customs Duty	29.44%	

*Rate of service tax increased to 14% from 12.36% with effect from 1 June 2015; Furthermore, a Swachh Bharat (Clean India) cess at 2% is proposed on all or specified taxable services from a date to be notified subsequently.

Value Added Tax (VAT)

VAT is a multi-point, destination-based system of taxation, with tax being levied on value addition at each stage of the transaction in the production/distribution chain. It applies to the sale of goods *within* a state. The transfer of a right to use goods (a lease) is included in the definition of 'sale' for this purpose. VAT is a state-specific levy and varies from state to state within India.

VAT applies to the following transactions as well, in addition to the normal trading of goods:

- Transfer of goods during the execution of works contracts involving the supply of materials and services;
- Purchase of goods from unregistered vendors in specified situations;
- Delivery of goods on hire purchase or any system of payment by instalments;
- Supply of goods, being food, drink or any other article for human consumption.

All sellers with a turnover in excess of the registration threshold are liable to register for VAT. In most states, the threshold is sales of INR 1 million. An entity may register voluntarily for VAT (and CST also).

In most states, input tax credit/set-off is allowed for VAT paid with respect to goods acquired for resale or for use in the manufacture of taxable goods. Credit is obtained by offsetting the tax paid against VAT charged on sales (output tax). Export out of India is zero-rated (i.e. denoting goods or services that are taxable for VAT, but with a tax rate of zero). Also, there is a 'negative list' of goods for which credit is not admissible.

Central Sales Tax (CST)

CST applies to the movement of goods *from one state to another*, pursuant to a sale. Every person who sells goods to a buyer outside the state is required to be registered and pay CST.

VAT/CST is payable when the sale is complete (i.e. when the transfer of title to the goods takes place or, for leases, when the right to use the goods is transferred).

Service tax

Service tax applies to all services provided in India other than those mentioned in the negative list. Currently, there are 17 services on the negative list. No service tax would be applicable on those specified services and other exempted services. The rate of service tax in India has increased to 14% (education cesses being exempted) from 12.36% with effect from 1 June 2015. A Swachh Bharat (Clean India) cess is proposed at 2% on all or specified taxable services from the date to be notified subsequently.

Every person who provides taxable services in excess of the turnover threshold of INR 1 million is required to pay service tax.

In specified circumstances, a service recipient is also liable to pay service tax with respect to any taxable service received under the reverse charge mechanism; for example, import of services into India.

According to the Place of Provision of Services Rules, 2012, (PPOS), the taxability of a service will be determined based on its place of provision.

The Point of Taxation Rules state that service tax liability arises on the date of raising the invoice or the date of receipt of payment, whichever is earlier. Any advance received is also liable to service tax. Invoices should be raised within 30 days of completion of services.

The service provider can take credit for duties. Credit for service tax paid on the procurement of services (input tax) is allowed against the service tax due (output tax). Credit between excise duty and service tax is fungible. Under CENVAT Credit Rules, 2004, once the eligible credit is availed, it is available as a set-off against the output service tax or excise duty liability. The time limit to avail credit is one year from the date of invoice.

Excise duty

In addition to VAT, CST and service tax, excise duty is levied in the form of a value-added tax on the manufacture of goods in India. The rate of excise duty is 12.5%; education cesses are exempt.

Every person who undertakes manufacturing activity as per excise provisions is required to be registered with India's central excise authority, the Central Board of Excise and Customs. However, exemption from registration is granted to a few specified persons.

The taxable event (an event that causes the tax liability to arise) for levy of excise duty is the manufacture or production of goods. However, tax is payable at the time of removal of goods from the factory or warehouse.

Customs duty

As seen in many countries, India levies customs duty on the import of goods into India. Customs duty in India has the following components:

- Basic Customs Duty (with a peak rate of 10%)
- Additional Customs Duty (in lieu of excise duty)
- Education cess and Higher education cess
- Special Additional Duty of Customs (in lieu of domestic sales tax)

The effective rate of customs duty works out to 29.44%.

Import duty is payable on import of goods into India at the time of clearance of goods from the customs station.

Credit for the above duties/taxes is available subject to the fulfilment of certain conditions and documentation requirements.

Invoicing

A person registered under either VAT/service tax/excise legislations must issue an invoice for all sales made. A tax invoice is generally necessary to support claims for input tax credits. Contents of the tax invoice are prescribed under the respective laws. An adjustment note (or credit or debit note) may be issued to reduce or increase the amount of tax/duty payable on a supply/service.

A small business that pays tax under the Composition Scheme (an optional and simple scheme of taxation of a small percentage of gross turnover, designed for registered dealers whose turnover does not exceed a specified amount) is generally not entitled to input tax credit and not allowed to issue tax invoices.

Payment, returns and audit

VAT, CST, excise or service tax returns must be filed monthly/quarterly/half-yearly/yearly as per the period prescribed under the respective laws.

In certain cases, it is mandatory for a registered person to get the books of accounts audited by an independent auditor (e.g. a Chartered Accountant), provided the turnover exceeds the prescribed limit (typically INR 10 million). The audit report must be submitted to the tax authorities in the specified format.

Goods and Services Tax (GST)

In his Budget 2015-16 speech, India's Finance Minister, Arun Jaitley, reiterated the intention to introduce GST by 1 April 2016 and stated that the government is moving forward on various fronts towards that goal. GST will replace a majority of indirect taxes with a single unified tax, reducing the cascading effect of taxes on the cost of goods and services and paving the way for a common national market. It is expected to make Indian products competitive in domestic and international markets and spur economic growth.¹²⁹ The Finance Minister stated that this modernised indirect tax regime will bring greater transparency and be easier to administer. The introduction of GST has the potential to raise India's tax-GDP ratio from the current level of 17.5% to 20%.¹³⁰

With this imminent change, industry awaits a clear road map on the introduction of GST along with a draft GST law being made available in the public domain for discussion/comments. You can know more by following our [GST Updates](#) on our website.

¹²⁹ Economic Survey 2014-15, Vol. 2, <http://indiabudget.nic.in/es2014-15/echapter-vol2.pdf>, accessed 30 April 2015

¹³⁰ Economic Survey 2014-15, Vol. 1, <http://indiabudget.nic.in/es2014-15/echapter-vol1.pdf>, accessed 30 April 2015

Chapter 10

Labour regulations, welfare and social security

In this Chapter, we have provided an overview of Acts that are applicable across India. In addition, states also specify certain compliances, Acts, Rules and Regulations or extend the scope of certain central government Acts, which have not been included.

Employment and industrial relations

Under the Constitution of India, labour is a subject in the concurrent list¹³¹ where both the central and state governments are competent to enact legislations. As a result, India has a plethora of laws (over 50 Central Labour Acts alone) addressing various aspects such as industrial relations, safety and health, child and woman labour, social security, labour welfare, employment and training, wages, etc. India is a founder member of the International Labour Organisation (ILO) and has ratified 43 conventions and one protocol, of which 42 are in force, and two conventions have been denounced.¹³²

The Industrial Disputes Act, 1947 was enacted to make provisions for the prevention and settlement of industrial disputes and for providing certain safeguards to the workers. It contains the following:

- the procedure, power and duties of the authorities constituted under the Act
- provisions to prohibit strikes and lockouts, declaration of strikes and lockouts as illegal
- provisions relating to lay-off, retrenchment and closure
- provisions covering unfair labour practices
- provisions of various penalties

It applies to every industrial establishment carrying on any business, trade, manufacture or distribution of goods and services irrespective of the number of workmen employed. Every person employed in an establishment for hire or reward including contract labour, apprentices and part-time employees to do any manual, clerical, skilled, unskilled, technical, operational or supervisory work, is covered. It does not apply to persons mainly in managerial or administrative capacity, persons engaged in a supervisory capacity, etc.

The Industrial Employment (Standing Orders) Act, 1946 requires employers to clearly define and publish standing orders (service rules) and to make them known to the workmen employed by them. It applies to every industrial establishment where 100 or more workmen (50 or more in many states) are/were employed on any day of the preceding 12 months.

The Industrial Employment (Standing Orders) Central Rules, 1946 cover the classification of workmen, working hours, holidays, pay days, wage rates and payment, shifts, attendance, leave, termination of employment, disciplinary action for misconduct, complaints, etc.

The Plantations Labour Act, 1951 provides for the welfare of plantation labour and conditions of work in plantations. It applies to all tea, coffee, rubber and cinchona/cardamom plantations but state governments may extend it to other plantations. The Act is administered by the state governments and is applied to any land used as plantations, which measures five hectares or more in which 15 or more persons are working. The state governments are, however, free to declare any plantation land less than five hectares or less than 15 persons to be covered by the Act.

The Factories Act, 1948 provides for the health, safety, welfare, service conditions and other aspects of workers in factories. It applies to all factories employing more than 10 people and working with the aid of power or employing 20 people and working without the aid of power. The Act aims at protecting workers employed in factories from unfair exploitation by the employer. The Act also covers the following:

- industries involving hazardous processes
- permissible levels of certain chemical substances in the work environment
- facilities and conveniences

¹³¹ Ministry of Labour & Employment, <http://labour.gov.in/content/innerpage/constitutional-provision.php>, accessed 30 April 2015

¹³² Ratifications for India, International Labour Organization, http://www.ilo.org/dyn/normlex/en/f?p=1000:11200:0::NO:11200:P11200_COUNTRY_ID:102691, accessed 30 April 2015

- working hours
- overtime wages
- employment of women, night shifts
- leave
- notice of accidents, diseases, etc.
- obligation regarding hazardous processes/substances

Each state government is empowered to make rules for the purpose of this Act. The Factories Act, 1948 should be read with the respective state rules. State legislations such as the Shops and Establishments Act do not apply to workmen in a factory or in an establishment attached to a factory to whom the benefits of the Factories Act, 1948 are applicable.

The Contract Labour (Regulation and Abolition) Act, 1970 regulates the employment of contract labourers in establishments and by contractors. The Rules for implementing the provisions of the Act vary from state to state. This Act covers the following:

- registration of the principal employer
- licensing of contractors
- payment of wages
- facilities to be provided to contract labourers (canteens, restrooms, etc.)
- submission of returns
- maintenance of records (Register of Contractors)

Wages¹³³

The Payment of Wages Act, 1936 regulates the payment of wages¹³⁴ to workers employed in a factory, drawing wages up to INR 18,000 per month. This Act was enacted to ensure that wages payable to employed persons covered by the Act were disbursed by the employers within the prescribed time limit without any unauthorised deductions. It specifies the need for maintenance of registers, penalties, rights of employees, etc.

The Minimum Wages Act, 1948 provides for fixing minimum wages in certain scheduled employments and revising the rates at appropriate intervals. Certain employments are specified under the schedule to this Act which is referred to as 'scheduled employment', for which minimum rates of wages have been fixed. The Act covers norms for fixing minimum wages, cost of living allowance, variable dearness allowance, etc.

The Payment of Bonus Act, 1965 provides for the payment of bonus (linked with profit or productivity) to persons employed in certain establishments. It is applicable to every factory/establishment in which 10 or more workers are employed on any day during an accounting year and every other establishment in which 20 or more persons are employed on any day during an accounting year. Every employee receiving salary or wages up to INR 10,000 per month and engaged in any kind of work whether skilled, unskilled, managerial, supervisory, etc. is entitled to a bonus for every accounting year if he has worked for more than 30 working days in that year. This Act covers factors such as the *minimum* and maximum bonus payable, time limit for payment, calculation of bonus, etc.

Employment and training

The Employment Exchanges (Compulsory Notification of Vacancies) Act, 1959 provides for compulsory notification of vacancies to employment exchanges. It applies to all establishments in the public sector and to such establishments in the private sector as may be notified by the appropriate government from time to time.

The Apprentices Act, 1961 aims to provide practical training to technically qualified persons in various trades. The objective is promotion of new skilled manpower. The scheme is also extended to engineers and diploma

¹³³ Laws related to wages, <http://labour.gov.in/content/innerpage/wages.php>, accessed 30 April 2015

¹³⁴ Excludes bonus, pension fund, provident fund, travel allowance and gratuity

holders. The Act requires employers to hire apprentices in certain designated trades as notified by the government. The Act specifies the obligations of employers and apprentices, the standard of education/physical fitness, duration of training, terms and conditions of the contract, payment, health, safety, welfare, working hours, etc.

Maternity and paternity leave

With a view to regulate the employment of women in factories and establishments, the government introduced the Maternity Benefit Act, 1961, primarily to ensure the well being of women workers during the period before and after child birth and to provide for maternity benefits including maternity leave, wages, medical bonus, nursing breaks, etc. There is neither a wage ceiling for coverage under the Act nor is there any restriction as regards the type of work a woman is engaged in.

This Act applies to women who work in factories, mines, plantations, shops and establishments in which more than 10 employees are employed. It does not apply to employees covered by the Employees' State Insurance Act, 1948. It can be extended to other establishments by state governments.

While 15 days of paternity leave is authorised for the government's male employees, it is not obligatory for the private sector. Large private companies tend to have their own policies specifying the paternity benefits extended to their male employees.

Union representation

The Trade Unions Act, 1926 deals with the registration of trade unions (including associations of employers), their rights, liabilities and responsibilities as well as ensures that their funds are utilised properly. It gives legal and corporate status to registered trade unions. An employer cannot prevent workers from forming a union. They are formed to promote and protect the interest and welfare of workers by enabling collective bargaining.

Social security and pension plans

The Employees' Provident Fund and Miscellaneous Provisions Act, 1952 was enacted to provide social security to industrial workers. It provides for retirement/old-age benefits through the compulsory institution of contributory provident funds, pension funds and deposit-linked insurance funds for employees in factories and other establishments. Furthermore, the Act provides for payment of terminal benefits in various contingencies such as retrenchment, closure, and retirement on reaching the age of superannuation, voluntary retirement and retirement due to incapacity to work.

It applies to every factory and other establishments engaged in any industry employing 20 or more persons. This Act applies to all employees including contract labour and part-time labour drawing salaries up to INR 15,000 per month. However, an employee who draws salary beyond INR 15,000 can also become a member of the fund voluntarily upon fulfilment of certain formalities by the employer.

The minimum contribution would be the percentage of wages as given below:

Scheme	Employer's contribution	Employee's contribution
Provident fund	3.67%	12%
Pension fund	8.33% (Up to a maximum of INR 750)	Nil
Deposit-linked insurance fund	0.50%	Nil
Administration charges	1.16%	Nil
Total	13.67%	12%

Applicability for expatriates and international social security agreements

The Indian government vide Notifications GSR 705(E) and GSR 706(E) dated 1 October 2008 extended the Employees' Provident Fund (EPF) and Pension Scheme to all 'international workers'. Besides Indian employees working overseas, 'international worker' also includes an employee other than an Indian employee, holding other than an Indian passport, working for an establishment in India to which the EPF Act applies. The EPF contribution is to be calculated on the total salary earned by the employee, whether received in or outside India. The expatriate will be required to contribute 12% and the employer needs to contribute a similar amount.

An 'excluded employee' is an international worker, contributing to a social security programme of his/her country of origin, either as a citizen or resident, with whom India has entered into a social security agreement on a reciprocal basis, and enjoying the status of detached worker for the period and terms, as specified in the agreement.

Bilateral social security agreements are being negotiated with various countries to protect the interest of expatriate workers and companies on a reciprocal basis. India has already entered into agreements with Belgium, Czech Republic, Denmark, France, Germany, Hungary, Korea, Luxembourg, Netherlands, Norway and Switzerland. These agreements help workers by exempting them from social security contributions in case of short-term contracts and allowing them to export pension in case of relocation. Such agreements also prove beneficial for companies as exemption from social security contribution for their employees substantially reduces costs.¹³⁵ However, detailed analysis would be required before structuring the salary of expatriates from these countries.

If the employer is a company and an order for winding up has been made, the amount due from the employer whether in respect of employee's or employer's contribution must be included among the debts which are to be paid in priority to all other debts. This payment will be preferential payment provided the liability therefore has accrued before the order of winding up is made.

The Payment of Gratuity Act, 1972 enforces the payment of gratuity – a reward for long service – as a statutory retirement benefit to employees engaged in factories, mines, oilfields, plantations, ports, railway companies, shops or other establishments. Every employee irrespective of his wages is entitled to receive gratuity if he has rendered continuous service of five or more years except in case of death or disablement.

- Gratuity is payable to an employee on retirement or termination of service, resignation or on death or disablement due to accident or disease.
- This Act applies to every establishment employing 10 or more persons at any time during the year.
- In case of death or permanent disablement of an employee, nominees of the employee are entitled to gratuity even if the employee has worked for less than five years.
- The rate of gratuity payable to employees is 15 days' salary for every completed year of service or a part thereof exceeding six months, subject to a maximum amount prescribed under the Act from time to time, which is currently INR 1 million.
- Wages/salary would mean last drawn wages and include all payments earned by an employee while on duty or on leave in accordance with the terms and conditions of his employment excluding bonus, commission, house rent allowance, overtime wages, and any other allowance.

The formula to calculate gratuity is as follows:

$$\text{Gratuity} = \frac{\text{Monthly salary} \times 15 \text{ days} \times \text{Number of years of service}}{26}$$

¹³⁵ Bilateral Agreements, Ministry of Overseas Indian Affairs, <http://moia.gov.in/services.aspx?ID1=81&id=m4&idp=81&mainid=73>, accessed 30 April 2015

The Act provides only for the minimum gratuity payable. If an employee has been promised/provided higher gratuity under a contract or an award, he is entitled to higher gratuity.

Injury/disability/death/survivor benefits

The Employers' Liability Act, 1938 prohibits employers from raising certain defences in suits for damages in respect of personal injuries sustained by workmen due to negligence by the employer.

The Employees' Compensation Act, 1923 earlier known as the Workmen's Compensation Act, provides for payment of compensation to workmen for injury by accident arising out of and in the course of his employment. The amount of compensation varies depending on the age of the employee, whether the injury results in death or permanent disablement, nature of disablement, etc. This Act is not applicable to workers covered under the Employees' State Insurance Act.

Employment insurance

The Employees' State Insurance Act, 1948 provides benefits to employees in case of sickness, maternity, disablement and death due to an employment injury or occupational hazard, and to provide medical care to the insured employees and their families. It covers all employees including casual, temporary or contract employees. It is wider than the Factories Act as the benefits of this Act extend to employees whether working inside the factory or establishment or elsewhere, directly employed by the principal employee or through an intermediate agency, and whether the employment is incidental or in connection with the factory or establishment. The contribution payable to the Employees' State Insurance Corporation in respect of an employee comprises of the employer's contribution and employee's contribution at a specified rate. The rates are revised from time to time. Currently, the employer is required to contribute 4.75% of wages and the employees' contribution is 1.75% of wages.

Profession tax

As profession tax varies from state to state (it is not imposed by all state governments), in order to get an overview, we will discuss the Maharashtra State Tax on Profession, Trades, Callings, and Employment Act, 1975. An employer must get registered under the Act and obtain a Registration/Enrolment Certificate under which the payment in respect of taxes can be deducted from employees' salaries (currently up to a maximum of INR 2,500 per year). In Maharashtra, profession tax is applicable to both, individuals and organisations (company, firm, proprietary concern, Hindu Undivided Family (HUF), society, club, association of persons, corporation or any other corporate body in Maharashtra).

Commercial establishments

Shops and Establishments Act

States have their own acts with regard to shops and commercial establishments. These Acts regulate the conditions of work and employment in shops, commercial establishments, residential hotels, restaurants, eating houses, theatres, and other places of public amusement or entertainment. The Shops and Establishments Act is applicable to all persons employed in a shop or commercial establishment with or without wages, except members of the employers' family. It does not apply to workmen in a factory or in an establishment attached to a factory to whom benefits under the Factories Act, 1948 are applicable.

This Act lays down the following rules:

- registration of establishments
- working hours per day and week
- guidelines for rest, opening and closing hours, closed days, national and religious holidays, overtime work
- ban on employment of children (under 15 years)
- employment of young persons and women
- annual leave, maternity leave, sickness and casual leave, etc.

- notice of termination of service
- maintenance of registers

The rules regarding registration of shops and establishment vary from state to state. For example, the Bombay Shops and Establishments Act, 1948 is applicable to shops and commercial establishments in Maharashtra.

Recent developments¹³⁶

In a major initiative for reducing the multiplicity of labour laws, ensuring compliance and promoting ease of doing business, the government initiated a number of labour reform measures.

- The Apprentice Act, 1961 has been amended to make it more responsive to industry and youth. An Apprentice Protsahan Yojana was also launched to support micro and small and medium enterprises (MSMEs) in the manufacturing sector in engaging apprentices. This scheme aims to support 100,000 enterprises by providing 50% stipend for 2.5 years. The government is also working towards bringing a single uniform law for the MSME sector to ensure operational efficiency and improve productivity while ensuring job creation on a large scale.
- The Ministry of Labour & Employment has drafted the Small Factory Bill for regulating factories employing less than 40 workers. The Bill combines the provisions of multiple labour laws applicable to small factories, thus facilitating compliance and reporting. The Bill envisages rules for wages, overtime hours, social security and appointment of factory inspectors in units employing fewer than 40 workers.
- A unified labour portal scheme, Shram Suvidha portal, has been launched for timely redressal of grievances and creating a conducive environment for industrial development. Its main features are: (i) a unique Labour Identification Number (LIN) facilitating online registration; (ii) filing a self-certified, simplified, single online return instead of 16 separate returns; and (iii) a transparent, computerised labour inspection scheme with labour inspectors uploading inspection reports within 72 hours.
- After the setting up of a new Ministry of Skill Development and Entrepreneurship to promote skill and entrepreneurial activities, common norms for skill training are being set up across central ministries/ departments. 31 industry/employer-led Sector Skill Councils (SSCs) are now operational and these have been aligned with the 25 sectors of the 'Make in India' campaign.
- The processes of the Employees' State Insurance Corporation (ESIC) have been digitised to ensure efficiency. The online portal enables employers to file monthly contributions, generate temporary identity cards, create monthly contribution challans online and issue 'pehchan cards' for insured persons for fast and convenient delivery of services.
- The database of 42.3 million subscribers of the Employees' Provident Fund (EPF) scheme has also been digitised. A Universal Account Number has been launched facilitating portable, hassle-free, and universally accessible provident fund accounts for employees. The statutory wage ceiling under the Employees' Provident Fund and Miscellaneous Provisions Act has been enhanced to INR 15,000 per month with effect from 1 September 2014. A minimum pension of INR 1,000 has been introduced for pensioners under the Employees' Pension Scheme, 1995 with effect from 1 September 2014.
- The National Career Service (NCS) is being implemented as a project to transform the National Employment Service and provide various job-related services such as online registration of job seekers and job vacancies, career counselling, vocational guidance, etc.

¹³⁶ Economic Survey 2014-15, Vol.2, <http://indiabudget.nic.in/es2014-15/echapter-vol2.pdf>, accessed 30 April 2015

Appendices

Appendix 1

TDS rates on some of the common payments made to residents:

Nature of payment	Rate of TDS in case of payment to		Threshold limit for total payment
	Individual or HUF	Others, including corporate assessees	
TDS on salaries paid	According to the slab rates applicable to respective employees		NA
TDS on interest on securities	10%	10%	INR 5,000
TDS on deemed dividends*	10%	10%	NA
TDS on interest other than 'Interest on Securities'			
By banks	10%	10%	INR 10,000
By others	10%	10%	INR 5,000
TDS on winnings from lottery or crossword puzzle	30%	30%	INR 10,000
TDS on winnings from horse races	30%	30%	INR 5,000
TDS on payments to contractors	1%	2%	INR 30,000 for a single transaction and INR 75,000 for the year
TDS on payment of insurance commission	10%	10%	INR 20,000
TDS on commission or brokerage	10%	10%	INR 5,000
TDS on rent			
Land, building, furniture and fittings	10%	10%	INR 180,000
Plant and machinery, equipment	2%	2%	INR 180,000
TDS on transfer of immovable property other than agricultural land	1%	1%	INR 5,000,000
TDS on fees for professional or technical services, royalty and non-compete fees	10%	10%	INR 30,000
TDS on remuneration/commission paid to Director, other than salary	10%	10%	NA
TDS on payment of compensation on compulsory acquisition of immovable property other than agricultural land	10%	10%	INR 200,000

*Regular dividend paid by the company is out of the purview of withholding taxes as the company is required to pay Dividend Distribution Tax @ 20.36%, the credit of which is not given to the recipients of the dividend.

Appendix 2

TDS rates on payments made to non-residents and foreign companies:

Nature of payment	Rate of tax*
TDS on interest on infrastructure debt fund, on foreign currency loans (under a loan agreement or by way of issue of long term bonds), on rupee denominated bonds of any Indian company or government security	5%
TDS on interest other than mentioned above in foreign currency	20%
TDS on long-term capital gains on unlisted securities	10%
TDS on long-term capital gains on other than specified assets	20%
TDS on short-term capital gains on listed shares and units of equity-oriented mutual funds	15%
TDS on short-term capital gains other than mentioned above and any other income	40%
Royalty and fees for technical services	10%
*applicable surcharge and education cess @ 3% shall also be levied	

Useful Links

Business Portal of India www.archive.india.gov.in/business

Bureau of Indian Standards - www.bis.org.in

Central Board of Excise and Customs - www.cbec.gov.in

Central Pollution Control Board - cpcb.nic.in

Competition Commission of India - www.cci.gov.in

Controller General of Patents, Designs and Trademarks - www.ipindia.nic.in

Copyright Office - copyright.gov.in

Department of Consumer Affairs - consumeraffairs.nic.in

Department of Electronics and Information Technology (DeitY) - deity.gov.in

Department of Financial Services - financialservices.gov.in

Department of Industrial Policy and Promotion - dipp.nic.in

Director General of Foreign Trade - www.dgft.gov.in

eBiz, India's G2B portal - www.ebiz.gov.in

Export Promotion Council for EOUs and SEZs - www.eouindia.gov.in

Income Tax Department - www.incometaxindia.gov.in

India Brand Equity Foundation - www.ibef.org

Indian Trade Portal – www.indiantradeportal.in

International Labour Organization - www.ilo.org

International Monetary Fund - www.imf.org

Invest India - investindia.gov.in

Ministry of Commerce and Industry - commerce.nic.in

Ministry of Corporate Affairs - www.mca.gov.in

Ministry of Environment, Forests and Climate Change - envfor.nic.in

Ministry of Finance - finmin.nic.in

Ministry of Labour and Employment - labour.gov.in

Doing business in India

Ministry of Overseas Indian Affairs - moia.gov.in

National Consumer Disputes Redressal Commission - ncdrc.nic.in

National Portal of India - india.gov.in

Office of the Economic Advisor - www.eaindustry.nic.in

Reserve Bank of India - www.rbi.org.in

Special Economic Zones in India - www.sezindia.nic.in

Supreme Court of India - supremecourtfindia.nic.in

Union Budget - indiabudget.nic.in

United Nations Conference on Trade and Development - unctad.org

World Bank - www.worldbank.org

World Trade Organisation - www.wto.org

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