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Making the most of it

Destination India 2011

Overview of Tax and Regulatory framework in India

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Foreword

In the recent past, when some of the strongest economies of the world were struggling to deal with the global recession, India not only exhibited its economic resilience, but also consolidated the recovery process.

It built upon the foundation of a remarkable 8% GDP growth rate in 2009-10 in the wake of the global financial crisis, further re-emphasising its position as an emerging market during 2010-11 with a stronger GDP growth rate of 8.6%.

With greater emphasis on rapid urbanisation, poverty alleviation and infrastructural development, unprecedented investment opportunities have been created for foreign investors. These have been part of the government of India's initiative to represent India as a forerunner for novel opportunities in the eyes of investors. Also, with a median age of 25 years and with 31% of the population under the age of 15 years, India's advantage in terms of the quality and potential of labour is unmatched by any of its Asian competitors as also other BRIC economies.

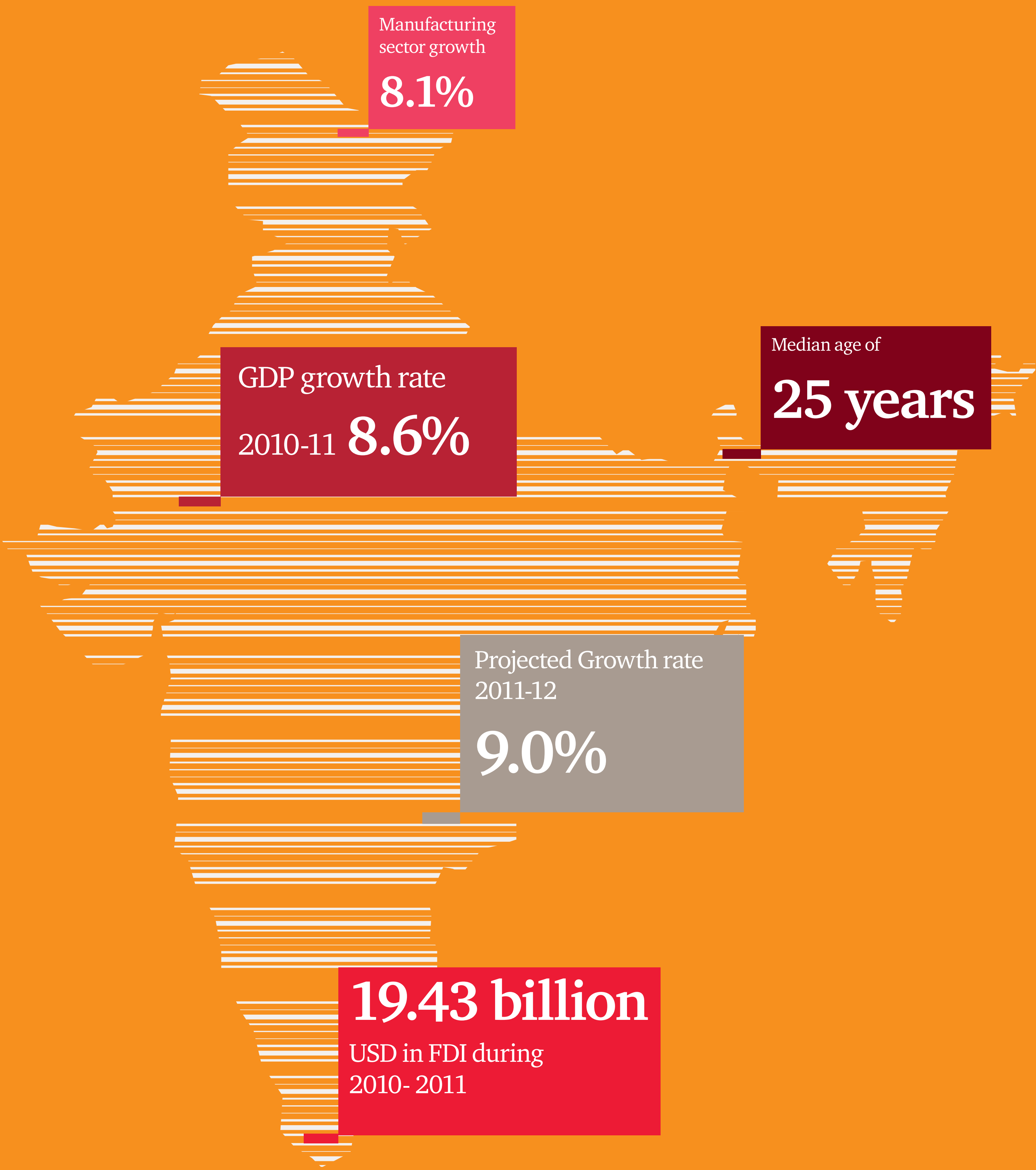
India has consistently provided lucrative investment avenues for foreign investors– both first-time and incumbent.

Despite a marginal dip in foreign direct investment (FDI) in 2010-11 (which recorded FDI inflows of USD 19.4 billion, as against FDI of USD 25.88 billion in 2009-10), India has been ranked second in global FDI in 2010. It will continue to remain among the top five attractive destinations for international investors during 2010-12, according to the United Nations Conference on Trade and Development (UNCTAD) in a report on world investment prospects **World Investment Prospects Survey 2009-2012**.

Destination India provides potential investors with the nuances of doing business in India. Its focus is on tax policy, tax incentives, exchange control and FDI policy. The publication has been compiled by a team of Pricewaterhouse Coopers' inbound investment advisory specialists in India, drawing on their extensive knowledge and experience of the typical issues faced by first-time investors in India.

Our specialists will be happy to advise and assist you on your specific requirements. We invite you to contact us for further details.

July 2011


Manufacturing sector growth
8.1%
GDP growth rate
2010-11 8.6%
Median age of
25 years
Projected Growth rate 2011-12
9.0%
19.43 billion
USD in FDI during 2010- 2011

Content

Chapter 1

Overview

Vital facts

Size	3.3 million sq. kms, the world's seventh largest nation
Population	Over 1.2 billion people, the world's second most populous nation
Political setup	Parliamentary democracy
Constitution	Written constitution with the Preamble "Justice -social, economic and political; Liberty of thought, expression, belief, faith and worship; Equality of status and opportunity; Fraternity assuring the dignity of the individual and the unity and integrity of the Nation."
Fundamental rights	Guaranteed by the Constitution
State religion	Secular state -there is no state religion
Directive principles of state policy	Promotion of the people's welfare in a social order
Union of India	Twenty-eight federal states and seven union territories
Parliament	Two houses: Lok Sabha (Lower House) and Rajya Sabha (Upper House)
Head of State	President
Head of Government	Prime minister
Independent judiciary	Supreme court as highest judicial authority in India. High court ashead of judicial hierarchy in the individual states
Language	The official language is Hindi, but English is the preferred language for conducting business and is widely read and spoken

Governing laws

India has an exhaustive legal framework governing all aspects of business. The following list sets out the key regulations and provides a brief description for each:

Arbitration & Reconciliation Act, 1996	Relates to alternate redressal of disputes
Central Excise Act, 1944	Governs duty levied on the manufacture or production of goods in India
Central Sales Tax, 1956	Governs the levy of tax on all inter-state sales in India Act
Companies Act, 1956	Governs all corporate bodies in India
Competition Act, 2002	Ensures free and fair competition in the Indian market
Consumer Protection Act, 1986	Protects consumers from unscrupulous traders/manufacturers
Customs Act, 1962	Deals with import and export regulations
Customs Tariff Act, 1975	Creates a uniform commodity classification code based on the globally adopted Harmonised System of Nomenclature for use in all international trade - related transactions
Direct Taxes Code Bill, 2010	Aims to moderate tax rates and simplify tax laws. All direct taxes including wealth tax and income tax will be brought under one bill.
Environment Protection Act, 1986	Provides a framework for obtaining environmental clearances Act, 1986
Factories Act, 1948	Regulates labour in factories
Foreign Exchange Management Act, 1999	Regulates foreign exchange transactions including foreign investment
Indian Contract Act, 1872	Codifies the way contracts are entered into, executed and implemented. It also codifies the effects of breach of contract
Income Tax Act, 1961	Governs direct taxes on the income of all persons, both corporate and non-corporate, as well as residents and non-residents

Industrial Disputes Act & Workmen Compensation Act, 1951	Covers labour laws relating to disputes
Industrial (Development Regulation) Act,1951	Provides for the development and regulation of certain industries
Information Technology Act,1999	Governs e-commerce transactions
Limited Liability Partnership Act, 2008	Establishes a new form of entity which combines the organisational flexibility of partnership with the advantages of limited liability. It provides operational flexibility for such enterprises by sparing them detailed legal and procedural requirements intended for large companies
Prevention of Money Laundering Act, 2002	Prevents money laundering and provides for the confiscation of property derived from, or involved in, money laundering
Patents Act, Copyright Act, Trade Marks Act, Design Act	Protects intellectual property rights
Right to Information Act, 2005	Sets out the right of every citizen to access information under the control of public Act, the authorities and promotes transparency and accountability in the work of public authorities
Securities and Exchange Board of India Act, 1992	Relates to the protection of investor interest in securities and regulation of the securities market. It puts in place securitisation and asset foreclosure laws, creating a legal framework for establishment of asset reconstruction companies.
Special Economic Zones Act, 2005	Governs the establishment, development and management of the Special Economic Zones (SEZs) for the promotion of exports. It provides for fiscal and economic incentives for developers of SEZ units.

If you look at the world, it would inevitably appear that India's growth is pre-ordained. The world needs working hands. The world needs back offices. India seems to be a natural fit. We are producing a global workforce, which is not only for India.

Sunil Bharti Mittal, founder and chairman of Bharti Enterprises

"….India has been a 'stand-out performer' in the global economy. The nation has benefited from reforms"

General Angel Gurria, OECD secretary

Economic Growth

Having asserted its resilience during the turbulent global financial crisis, Indian industry and economic growth have showcased progressive buoyancy. The ministry of finance has indicated an annual growth rate of 9% in GDP through FY 2011-2012, and is taking careful measures to counter the loss of industrial momentum.

Growth has been driven by performance in all three sectors--a rebound in agriculture, continued momentum in industry and a slightly below-par performance in services. Inflation remains an area of concern as risks remain from domestic demand and high global commodity prices, in the wake of the West Asia crude shock.

India has emerged as Asia's largest buying economy. Since 2001, its middle-class has seen even further increases in its disposable income, and consequently, consumption and savings. Analysts predict that by 2025–with current growth rates–India will become the fifth largest consumer goods market in the world. The Asian Development Bank has estimated that over the next two decades, the middle-class population in the country will reach 1 billion. The middle-class is set to assume the traditional role of the American and European middle-classes. Global industry is acknowledging this.

Particularly, the consumer durables segment has furthered growth. An enhanced consumer segment, positive outlook on employment and rising incomes have precipitated growing consumption.

Prime Minister Manmohan Singh is confident of achieving the projected GDP growth based on the performance of the Indian economy over the last few years. This shows confidence in the inherent strength and resilience of the Indian economy–the fastest-growing free economy in the world.

During his visit to India, US President Barack Obama mentioned that the sheer volume and pace of India's progress in just two decades was one of the most stunning achievements in human history.

Integration with the global economy

These are exciting times on the foreign trade front for India with several simultaneous dialogues underway with various countries and regions over free trade agreements. The India-ASEAN trade in goods agreement has already been signed and has propelled trade in many industries. Also, trade agreements with Korea, Japan, the European Union, Australia, Thailand, Bangladesh, India, Myanmar and Srilanka have the potential to catapult India to the forefront of international trade and preferential treatment. The prospects for international growth of Indian businesses are both promising and unprecedented.

Demographic advantage

India is today one of the three largest Asian economies in terms of purchasing power parity. The median age of the country's population is 25, which in comparison to other Asian countries, puts India in a very favourable demographic position. The United Nations predicts that India's working age population (15 to 64 years) will increase by 135 million in one decade, that is, by 2020. So while most countries, such as those in Europe, China and the US, will witness a reduction in workforce in the coming decades, India's position is strengthening. This is a product of its high birth rate, which will last till about 2050. A young, eager and well-educated workforce is the key to the country's future prosperity. In the modern knowledge economy, this favourable demographic phase provides India with a significant competitive advantage and has important implications for the country's economic growth trajectory and social stability.

Chapter 2

Foreign Investment in India

Foreign Collaboration in India

The Indian government embarked on liberalising the Indian regulatory framework, with specific reference to foreign investment, through the Statement on Industrial Policy of 1991. Since then the Indian regulatory environment for foreign investment has been consistently eased to make it increasingly investor-friendly.

Under the current FDI framework, foreign investment is permitted by all categories of investors (other than citizens or entities of Pakistan) and in all sectors, except:

- Sectors not open to the private sector, namely atomic energy and railways;
- Lotteries, gambling and betting;
- Agriculture (excluding floriculture, horticulture, seed development, animal husbandry, pisciculture, aquaculture and cultivation of vegetables, mushrooms, etc. under controlled conditions and services related to agro and allied sectors);
- Plantations (excluding tea plantations);
- Retail trading (other than single brand retail);
- Real estate (except construction development projects);
- Chit funds, nidhi companies, or trading in Transferable Development Rights; and
- Manufacturing of cigars, cheroots, cigarillos and cigarettes, and tobacco and tobacco substitutes.

For other sectors, there are two routes for obtaining approval for foreign investment in India:

- Automatic route (i.e. no prior approvals) under delegated powers exercised by the Reserve Bank of India (RBI); and
- Approval by the government through the Foreign Investment Promotion Board (FIPB) under the Ministry of Finance.

These are discussed in brief below:

Automatic Route

The automatic route is available to all Foreign Investment cases, other than:

- Specified sectors which require FIPB approval for FDI or for FDI beyond a prescribed cap;
- Investments other than equity shares and compulsorily and mandatorily convertible debentures/ preference shares;
- Investment for considerations other than cash (except for capitalisation of an External Commercial Borrowing (ECB) due for repayment and interest on such ECB, as well as technology royalties due for payment);
- Investments by citizens and companies of Bangladesh;
- Investments in warrants and partly paid shares;
- Investment in entities other than companies.

The above cases would require prior Government approval.

The FDI policy has been relaxed recently to remove the requirement of obtaining prior approval in cases of fresh investment by a foreign investor having an existing venture or tie-up in India.

FIPB Route

In cases of foreign investment where the project does not qualify for automatic approval, prior approval is required from the FIPB. The decision of the FIPB is normally conveyed within 30 days of submitting an application.

A proposal for foreign investment is decided on a case-to-case basis on the merits of the case and in accordance with the prescribed sectoral policy. Generally, preference is given to projects in high priority industries and the infrastructure sector, those with export potential,large-scale employment opportunities,links with the agro sector, social relevance, or those relating to the infusion of capital and induction of technology.

A recent policy liberalisation has allowed, under the approval route, FDI byway of non-cash contributions to capital, in cases of import of capital goods/equipment and pre-operative or pre-incorporation expenses incurred by the foreign promoter.

Foreign investment proposals under the FIPB route that involve a total foreign equity inflow of more than INR 12 billion must be placed before the Cabinet Committee of External Affairs (CCEA) for its further consideration.

Fresh prior approval from the FIPB/CCEA is not required for bringing in additional investment into the same entity in the following cases:

- Entities which earlier obtained FIPB/ CCEA approval and subsequently either the activity/sector has been placed under automatic route or sectoral caps have been removed or increased (provided that such additional investment along with initial/original investment is within the current sectoral caps).

FIPB approval is required to be obtained by Indian company which is engaged only in downstream investment activities for holding purposes or which does not have any operations nor any downstream investments.

Further, downstream investments is also permitted through use of internal accruals, subject to such investments complying with sectoral caps / policy.

The downstream investment, whether made under the automatic route or the approval route by a foreign owned or controlled Indian company is required –

- To be reported within 30 days to the DIPP/ FIPB;
- To adhere to prescribed valuation norms and
- Not to be funded through leveraging from the domestic market.

For sectors where the FDI cap is less than 49% (e.g. media and defence) there are additional conditions that are required to be met in relation to the single largest

Indian shareholder. Insurance sector is not subject to these guidelines.

For the purpose of computing indirect FDI, foreign investment in the Indian investing company includes all types of foreign investment, namely FDI, investments by Non-Resident Indians, portfolio investment by FIIs and NRIs), ADRs/GDRs, FCCBs, Convertible Preference Shares/ Convertible Debentures, and Foreign Venture Capital Investors (FVCIs). However, NRI investments made on a non-repatriation basis will not be counted as FDI for this purpose.

FDI in Limited Liability Partnerships

Very recently in May 2011, the Government notified the FDI policy allowing foreign investment in LLPs. Key features of the FDI policy for LLPs, are as below:

- FDI in LLPs allowed upto 100% in sectors/activities that are currently eligible for 100% FDI under automatic route and which do not have any sectoral or other FDI-linked conditionalities;
- Prior approval from the FIPB will be required for FDI in LLP;
- Downstream investment by LLPs with FDI will not be allowed. However, an Indian company (ICo) with foreign investment can make downstream investment into a LLP with prior FIPB approval, provided both the ICo and LLP are engaged in activities eligible for 100 % FDI under automatic route;
- Only cash contribution will be permissible for FDI in LLPs;
- FIIs and FVCIs cannot invest into LLPs. Further LLP cannot raise foreign currency loans.

Investment through Share Acquisition

Acquisitions may be made of shares and convertible debentures of an existing Indian company which is either a privately held company or a company in which the public is interested, i.e. a company listed on a stock exchange, provided that a resolution to this effect has been passed by the Board of Directors of the Indian company whose shares are being acquired. Such acquisitions need to comply with FDI guidelines.

Prior FIPB approval is required in all cases where either the “control” or “ownership” of the Indian company, engaged in a sector where FDI caps apply, is transferred to or acquired by a non-resident entity. Acquisition by way of share swap is also permitted with prior FIPB approval and subject to valuation guidelines.

Prior approval of RBI is required in cases of share acquisition that entail deferment of the acquisition consideration, such as those that are based on performance milestones.

Foreign investors looking at acquiring equity in an existing Indian company engaged in defined financial services activities would require prior approval of the RBI.

Acquisition of a publicly listed company is subject to the guidelines of the Securities Exchange Board of India (SEBI), Take-Over Regulations which require that any person acquiring 15% or more of the voting capital or control in a publicly listed company should make a public offer to acquire a minimum 20% stake from the public.

Valuation Norms

The price of shares proposed to be issued/transferred from a resident to a non-resident must be determined in accordance with the following guidelines:

- In the case of a listed company, the price may not be less than the price at which a preferential allotment of shares can be made under the SEBI Guidelines. Further, in a rights issue, the prices are to be determined by the company;
- In the case of an unlisted company, the issue/transfer of shares is to be at a price not less than fair value to be determined by a SEBI registered Category - I - Merchant Banker or a Chartered Accountant as per the discounted free cash flow method. Further, in the case of a rights issue, the price may not be less than the price at which an offer on a right basis is made to resident shareholders.

In relation to a transfer of shares from a non-resident to resident, the pricing of shares is to be determined as follows:

- In the case of a listed company, the price may not be more than the minimum price at which the transfer of shares can be made from a resident to a non- resident;
- In the case of an unlisted company, the price of shares may not be more than the minimum price at which the transfer of shares can be made from a resident to a non-resident.

Investment by Foreign Institutional Investors

A registered Foreign Institutional Investor (FII) may, through the SEBI, apply to the RBI for permission to purchase the shares and convertible debentures of an Indian company under the Portfolio Investment Scheme.

FIIs are permitted by RBI to purchase the shares/convertible debentures of an Indian company through registered brokers on recognised stock exchanges in India. They are also permitted to purchase the shares/convertible debentures of an Indian company through private placement/arrangement.

The total holding by each FII/SEBI approved sub-account of FII cannot exceed 10% of the total paid-up equity capital or 10% of the paid-up value of each series of convertible debentures issued by an Indian company. Further, the total holdings of all FIIs/sub-accounts of FIIs added together cannot exceed 24% of the paid-up equity capital or the paid-up value of each seriesof convertible debentures. This limit of 24% may be increased to the specified sectoral cap or statutory ceiling, as applicable, by the Indian company concerned by passing a Board of Directors resolution followed by the permission of the shareholders through a special resolution to that effect.

Technology Transfer

Payments of royalties, lump sum fees for the transfer of technology and payments for use of trademark/brand names can be made under the automatic route, i.e., without any approval from the Indian Government.

Summary of Foreign Direct Investment in India

India ranks among the most attractive destinations for FDI in the world. Indian markets have significant potential and offer prospects of high profitability and a favourable regulatory regime to entice investors. A summary of FDI for key sectors is as follows:

Advertising Industry

100% FDI is permitted under the automatic route.

Film Industry

100% FDI is permitted under the automatic route in the film industry, including film financing, production, distribution, exhibition, marketing and associated activities related to the film industry.

Agriculture & Allied Activities

FDI/NRI investment is not permitted in agriculture sector, except under the following activities:

- FDI up to 100% on the automatic route is permitted in floriculture,horticulture,the development of seeds,animal husbandry,pisciculture, aquaculture,cultivation of vegetables and mushrooms under controlled conditions and services related to agro and allied sectors.Certain conditions apply for companies dealing with development of transgenic seeds/ vegetables;
- In the tea sector (including tea plantations), FDI up to 100% is allowed with the prior approval of the FIPB and subject to the following conditions:
  - Compulsory disinvestment of 26% equity in favour of an Indian partner/ the Indian public within a period of five years;
  - Prior approval of the state government is required for any change in land use.
- 100% FDI under automatic route is permitted for coffee and rubber processing and warehousing.

Alcohol – Distillation and Brewing

FDI is permitted up to 100% under the automatic route, subject to obtaining an industrial licence.

Asset Reconstruction Companies

FDI up to 49% is permitted with prior FIPB approval in an Asset Reconstruction Company (ARC) registered with RBI. Where any individual investment exceeds 10% of the equity, such an investor may not hold any controlling interest in the ARC. Investments by FIIs are not allowed. However, SEBI registered FIIs can invest in Security Receipts (SRs) issued by RBI registered ARCs.

Banking

- Public Sector Banks – FDI and portfolio investment allowed up to 20% under the approval route;

- Private Sector Banks – FDI (from all sources) up to 74% is allowed (up to 49% under the automatic route, and beyond that up to 74% under the approval route). Voting rights per shareholder are restricted to 10%. While the Cabinet has approved an amendment to the Banking Regulation Act linking voting rights to shareholding, a notification by RBI giving effect to the amendment is still awaited. Please note that within the permissible FDI ceiling, there are separate limits for FII/NRI investment under the portfolio investment scheme;
- A foreign bank may operate in India through only one of three channels, viz.: (i) a branch or branches; (ii) a wholly-owned subsidiary; and (iii) a subsidiary with aggregate foreign investment of up to a maximum of 74% in a private bank.

Broadcasting

- Terrestrial Broadcasting FM (FM Radio) - Foreign investment, including NRI, Person of Indian origin (PIO) and portfolio investments, is permitted up to 20% under the approval route;
- Cable Network - Foreign investment, including FDI NRI, PIO and portfolio investments, is permitted up to 49% under the approval route. Companies with minimum of 51% of paid-up share capital held by Indian citizens are eligible to provide cable TV services under the Cable Television Network Rules (1994);
- Direct-To-Home - Foreign investment, including FDI, NRI, PIO and portfolio investments, is permitted up to 49% under the approval route. Within the 49% foreign equity, the FDI component should not exceed 20%;
- Broadcasting Services - The total direct and indirect foreign investment, including FDI and portfolio investments, is permitted up to 74%. FDI up to 49% is under automatic route and beyond 49%, FIPB approval is required;
- Setting up Hardware Facilities such as Uplinking Hubs - Foreign investment, including FDI and FII, is permitted up to 49% under the approval route;
- Up-linking TV Channels - Foreign investment, including FDI and FII, up to 26% is permitted under the approval route for up-linking a news and current affairs TV channel; 100% FDI is permitted under the approval route for up- linking a non-news and current affairs TV channel.

The above sub-sectors would also be subject to compliance with terms and conditions as may be prescribed by the Ministry of Information & Broadcasting.

Cigarettes

FDI is prohibited in the manufacture of cigars, cheroots, cigarillos and cigarettes, and tobacco and tobacco substitutes.

Civil Aviation and Airports

- FDI up to 49% is permitted for scheduled air transport services/domestic scheduled passenger airlines under the automatic route. NRI investment is permitted up to 100% under the automatic route. However, no direct or indirect equity participation by foreign airlines is allowed;
- For non-scheduled air transport services, non-scheduled airlines and cargo airlines, FDI up to 74% is permitted (up to 49% under the automatic route and beyond that with FIPB approval). NRI investment is permitted up to 100% under the automatic route;
- 100% FDI is permitted under the automatic route for Maintenance and Repair Organisations, flying training institutes and technical training institutions;
- FDI up to 74% and NRI investment up to 100% is permitted under the automatic route for ground-handling services subject to sectoral regulations and security clearances. FDI up to 49% is permitted under the automatic route and between 49% and 74% is permitted under the approval route;

- FDI up to 100% is permitted under the automatic route for helicopter services/ sea plane services. However approval from Directorate General of Civil Aviation will be required;
- Foreign airlines can participate in the equity of companies operating cargo airlines, helicopter services and seaplane services.

Coal and Lignite

- FDI is permitted up to 100% under the automatic route in coal and lignite mining for captive consumption by power projects, iron & steel and cement units and other eligible activities, subject to the provisions of the Coal Mines (Nationalisation Act), 1973;
- A company setting up coal processing plants is allowed FDI up to 100% subject to the condition that it will not perform coal mining and will supply the washed or sized coal to parties supplying raw coal / coal processing plants instead of selling it on the open market.

Commodity Exchanges

Composite foreign investment (FDI + FII) up to 49% is permitted with prior FIPB approval. FII investment is capped at 23% and restricted to secondary market purchases while FDI investment is capped at 26%. No foreign investor/entity including persons acting in concert may hold more than 5% equity.

Credit Information Companies (CICs)

Foreign investment (FDI + FII) in CICs is permitted up to 49%, subject to:

- Prior approval of the Indian Government and regulatory clearance from RBI is required;
- Investment by registered FIIs is permitted up to 24% (within the overall limit of 49%) only in listed CICs, subject to conditions;
- Foreign investment is subject to the Credit Information Companies (Regulation) Act, 2005.

Courier Services

FDI up to 100% is permitted under the approval route for courier services excluding the distribution of letters.

Defence

FDI, including NRI investments, in this sector is permitted up to 26% subject to prior approval of the government and compliance with the security and licensing requirements and guidelines issued by the Ministry of Defence.

The single largest Indian shareholder is to hold at least 51%.

According to the guidelines for the production of arms and ammunitions, the management of the applicant company/ partnership should be in Indian hands, and the majority of the Board as well as the Chief Executive should be resident Indians. Further, there is a three year lock-in period for the transfer of equity from one foreign investor to another.

Hazardous Chemicals

100% FDI is allowed under the automatic route and subject to obtaining an industrial licence under the Industries (Development & Regulation) Act 1951.

Hotels and Tourism Related Industry

100% foreign investment is allowed under the automatic route.

Industrial Explosives

100% FDI is allowed under the automatic route subject to obtaining the industrial licence under the Industries (Development & Regulation) Act 1951 and regulations under the Explosives Act 1898.

Insurance

FDI in the insurance sector is permitted up to 26% under the automatic route subject to obtaining a licence from the Insurance Regulatory & Development Authority.

Lottery Business, Gambling and Betting

FDI/foreign technical collaboration in any form is prohibited in Lottery Business, Gambling and Betting.

Micro and Small Enterprises (MSE)

100% FDI is permitted in a MSE for the manufacture of items reserved under the small scale sector, subject to compliance with the appropriate sectoral policy.

However, any industrial undertaking, with or without FDI, which is not a MSE and is engaged in manufacturing items reserved for the MSE sector (presently 204 items), would require FIPB approval where foreign investment is more than 24%. Such an undertaking would also require an industrial licence under the Industries (Development & Regulation) Act 1951, which prescribes an export of minimum of 50% of the new or additional annual production of the MSE reserved items to be achieved within a maximum period of three years.

Mass Rapid Transport System

FDI up to 100% is allowed under the automatic route in mass rapid transport systems, including associated commercial development of real estate, in all metropolitan cities.

Mining

- FDI is allowed up to 100% under the automatic route for activities such as exploration and mining of metals and non-metal ores, including gold and silver, minerals, diamonds and precious stones;
- FDI up to 100% is permitted with prior government approval for mining and mineral separation of titanium-bearing minerals and ores, it value addition and integrated activities, subject to sectoral regulations and the conditions of the Mines and Minerals (Development & Regulation) Act, 1957.

Non-Banking Financial Services

FDI in this sector is permitted under the automatic route, subject to compliance with the guidelines issued by RBI.

100% foreign investment is only allowed in the following 18 activities under the automatic route subject to the minimum capitalisation norms indicated below:

i. Merchant Banking;
ii. Underwriting;
iii. Portfolio Management services;
iv. Investment Advisory Services;
v. Financial Consultancy;
vi. Stock Broking;
vii. Asset Management;
viii. Venture Capital;
ix. Custodial Services;
x. Factoring;
xi. Credit Rating Agencies;
xii. Leasing and Finance;
xiii. Housing Finance;
xiv. Forex Broking;
xv. Credit Card Business;
xvi. Money Changing Business;
xvii. Micro Credit;
xviii. Rural Credit.

Minimum Capitalisation Norms (Foreign Equity): Fund-Based Activities

% FDI	Minimum capitalisation
Foreign capital up to 51%	USD 0.5 million to be bought upfront
Foreign capital > 51% and up to 75%	USD 5 million to be bought upfront
Foreign capital > 75%	USD 7.5 million to be bought upfront and the balance of USD 42.5 million in 24 months

Minimum Capitalisation Norms (Foreign Equity): Non-Fund Based Activities

Non-Banking Financial Companies (NBFCs), the minimum capitalisation norm has been fixed at USD 0.5 million.

The following activities would be classified as non-fund-based activities:

i. Investment Advisory Services;

ii. Financial Consultancy;

iii. Forex Broking;

iv. Money Changing;

v. Credit Rating.

100% foreign owned NBFCs with a minimum capitalisation of USD 50 million are permitted to set up step down subsidiaries for specific NBFC activities without restriction on the number of operating subsidiaries and without bringing in additional capital.

JV operating NBFCs with FDI up to 75% are permitted to set up subsidiaries for undertaking other NBFC activities, subject to the compliance with applicable minimum capitalisation norms by the subsidiaries.

Further, share premium received along with face value of the shares upon issue of the shares to non-resident investors would be counted as part of minimum capitalization requirement.

A non-fund based NBFC is prohibited to set up subsidiary for any other activity., and neither can it participate in the equity of an NBFC holding/operating company.

Petroleum

Other than Refining

100% FDI is permitted under the automatic route for the following, subject to the existing policy and regulatory framework in the petroleum sector:

- Oil exploration;
- Petroleum product pipelines;
- Petroleum products marketing;
- Laying of natural gas/LNG pipelines;
- LNG regassification infrastructure;
- Market studies and formulation and investment financing in the petroleum sector.

Refining

In the case of public sector units, FDI is permitted to 49% with prior FIPB approval. In the case of private Indian companies, FDI up to 100% is permitted under the automatic route.

Ports and Harbours

Up to 100% FDI is allowed through the automatic route for leasing of existing assets of ports, construction and maintenance of assets, leasing of equipment for port handling and leasing of floating crafts and captive facilities for port based industries.

Power

FDI up to 100% is permitted in the power sector under the automatic route for projects relating to the generation, transmission, distribution and trading of power, other than the generation, transmission and distribution of electricity in atomic reactor power plants.

Print Media

Publication of Newspapers, Periodicals and Indian Editions of Foreign Magazines Dealing in News and Current Affairs

Foreign investment, including FDI, NRI, PIO and FII investment, is permitted up to 26%.

Publishing/ Printing of Scientific and Technical Magazines/ Specialty Journals/ Periodicals

FDI is permitted up to 100%.

Publication of Facsimile Editions of Foreign Newspapers

FDI up to 100% is permitted provided the FDI is by the owner of the original newspapers whose facsimile edition is proposed to be brought out in India.

These sub-sectors would need to comply with terms and conditions as may be prescribed by Ministry of Information & Broadcasting.

Construction Development Projects

FDI up to 100% under the automatic route is permitted in:

- Construction-development projects (including but not restricted to housing, commercial premises, resorts, educational institutions, recreational facilities, city and regional level infrastructure, and townships) subject to certain conditions such as:
  - Minimum area to be developed;
  - Minimum capitalization of USD 10 million for a wholly-owned subsidiary and USD 5 million for a JV with an Indian partner;
  - Original investment i.e. the entire amount brought in as FDI has a minimum three-year lock-in from the date of receipt of each installment of FDI or from the date of completion of minimum capitalization, whichever is later.

Investment by NRIs is not subject to these conditions for construction development projects.

Investment in SEZs, hotels, hospitals and industrial parks (satisfying prescribed conditions) are exempted from the above requirement.

Industrial Parks

FDI up to 100% is permitted under the automatic route subject to fulfilment of prescribed conditions.

Satellites - Establishment Operations

FDI up to 74% is permitted with prior FIPB approval subject to the sectoral guidelines of the Department of Space - Indian Space Research Organisation.

Security Agencies in Private Sector

Under the Private Security Agencies (Regulation) Act, 2005, a security agency licensee:

- Should be a firm registered in India;
- Should not have a foreign director/partner;
- Foreign shareholding would be restricted to a maximum of 49% under the approval route.

Stock Exchanges, Depositories Corporations

Foreign investment up to 49% (FDI cap at 26% and FII at 23%) is permitted with prior approval from FIPB. FII are allowed only through purchases in the secondary market.

Telecommunications

FDI up to 74% is allowed for the following activities (subjected to prescribed conditions):

- Basic, Cellular, Unified Access Services, Long Distance, V-Sat, Public Mobile, Radio Trunk Services, Global Mobile Personal Communication Services;
- Internet Service Providers with gateways;
- ISPs not providing gateways;
- Radio paging;
- End-to-end bandwidth.

FDI up to 100% is allowed for the following activities:

- Infrastructure provider providing dark fibre, right of way, duct space, power (IP Category 1);
- Electronic mail;
- Voice mail.

This will be subject to the condition that such companies will divest 26% of their equity in favour of the Indian public in five years, if these companies are listed in other parts of the world.

FDI up to 49% is under the automatic route and above that under the government route.

The above services would be subject to licensing and security requirements irrespective of the quantum of foreign investment.

Trading

100% FDI is permitted under the automatic route for trading companies engaged in the following activities:

- Cash and Carry Wholesale Trading / Wholesale Trading subject to the Operational Guidelines;
- Trading for exports;
- E-commerce activities: E-commerce activities refer to the activity of buying and selling by a company through the e-commerce platform. Such companies would engage only in Business to Business (B2B) e-commerce and not in retail trading, implying that the existing restrictions on FDI in domestic trading would be applicable to e-commerce as well
- Sourcing from MSEs.

100% FDI is permitted with FIPB approval for:

- Trading of items sourced from small scale sector;
- Test marketing of items for which a company has industrial licence for manufacture.

51% FDI is permitted with FIPB approval for Single Brand product retailing, subject to the following conditions:

- Products to be sold should be of a "single brand" only;
- Products should be sold under the same brand internationally;
- "Single Brand" product retailing covers only products which are branded during manufacturing;
- Eligible customers:
  - Entities holding sales tax/Value Added Tax (VAT) registration/ service tax/ excise duty registration;
  - Entities holding trade licenses;
  - Entities holding permits licences etc. for undertaking retail trade from Government Authorities/Local Self Government Bodies;
  - Institutions with certificates of incorporation or registration as a society or registration as public trust for their own consumption.
- Wholesale trading to group companies may not exceed 25% of the total turnover of the wholesale venture.

Venture Capital Fund and Venture Capital Company

Foreign Venture Capital Investors are permitted to invest upto 100% under the automatic route in an Indian Venture Capital Undertaking and may also set up a domestic asset management company to manage the fund.

A SEBI registered FVCI can also invest in a domestic venture capital fund registered under the SEBI (Venture Capital Fund) Regulations, 1996.

However, if the entity undertaking venture capital fund activity is a trust registered under the Indian Trust Act, 1882, foreign investment would be permitted under the approval route.

FVCIs are permitted to invest in other companies subject to FDI regulations.

Entry Options

A foreign company looking to set up operations in India, can consider the following options:

Entry Strategy i : Operating as an Indian Company

Option 1: Wholly-Owned Subsidiary Company

A foreign company can set up a wholly owned subsidiary company in India to carry out its activities. Such a subsidiary is treated as an Indian resident and an Indian company for all Indian regulations (including Income Tax, Foreign Exchange Management Act,1999 and the Companies Act), despite being 100% foreign-owned. At least two members, for a private limited company, and seven members, for a public limited company, are mandatory.

Option 2: Joint Venture with an Indian Partner (Equity Participation)

Although a wholly owned subsidiary has proved to be the preferred option, foreign companies have also begun operations in India by forging strategic alliances with Indian partners. The trend is to choose a partner who is in the same field/area of activity or who brings synergy to the foreign investor's plans for India. Sometimes joint ventures are also necessitated due to restrictions on foreign ownership in certain sectors.

The foreign investment guidelines for investment in an Indian company have already been discussed above.

Option 3: Limited Liability Partnership (LLP)

LLP is a new form of business structure in India. It combines the advantages of a company, such as being a separate legal entity having perpetual succession, with the benefits of organisational flexibility associated with a partnership. At least two partners are required to form a LLP and they have limited liability.

LLP is comparatively easier to manage with less compliance levels as compared to a company form of organisation. Further, a LLP is not subject to mandatory requirements applicable to a company with regard to provision of depreciation and transfer to reserves prior to distribution of profits (this requirement is discussed in Chapter 3 dealing with Funding Options). As mentioned earlier, the FDI policy for LLPs has been notified recently making this a possible viable entity form for Indian business operations of foreign investors.

Entry Strategy ii: Operating as a Foreign Company

Option 1: Liaison Office

Setting up a Liaison or Representative Office is a common practice for foreign companies seeking to enter the Indian market. The role of such offices is limited to collecting information about the possible market and to providing information about the company and its products to prospective Indian customers. Such offices act as listening and transmission posts and provide a two-way information flow between the foreign company and the Indian customers. A Liaison Office is not allowed to undertake any business activities other than liaison activities in India and cannot, therefore, earn any income in India, under the terms of approval granted by the RBI.

Option 2: Project Office

Foreign companies planning to execute specific projects in India can set up temporary project/site offices in India for this purpose. The RBI has granted general permission to a foreign entity for setting up a project office in India, subject to the fulfilment of certain conditions. The foreign entity needs only to provide a report to the jurisdictional Regional Office of the RBI giving the particulars of the project/contract.

Option 3: Branch Office

Foreign companies engaged in manufacturing and trading activities abroad can set up Branch Offices in India for the following purposes, with the prior approval of RBI:

- Export/import of goods;
- Rendering professional or consultancy services;
- Carrying out research work in which the parent company is engaged that promotes technical or financial collaborations between Indian companies and a parent or overseas group company;
- Representing the parent company in India and acting as a buying/selling agent in India;
- Rendering services in information technology and development of software in India;
- Rendering technical support for the products supplied by parent/ group companies;
- Acting as a foreign airline/shipping company.

In general, manufacturing activity cannot be undertaken through a Branch Office. However, foreign companies can establish a Branch Office/unit for manufacturing in a SEZ subject to the fulfilment of certain conditions.

Citizens of specified countries are prohibited from establishing a project office or any other place of business in India without the prior permission of the RBI.

Chapter 3

Funding Options in India

A foreign company which sets up a subsidiary in India can fund its Indian subsidiary through alternative options, which primarily consist of the following:

Equity Capital

Regulatory Approvals

In accordance with FDI guidelines which have been discussed in Chapter 2.

Transfer to Reserve Rules

Corporate laws in India provide for a mandatory transfer of distributable profits to free reserves of the Indian company in the event of a dividend declaration. In the event that the Indian company declares dividends in excess of 20% of the paid-up capital, a minimum of 10% of distributable profits would need to be transferred to statutory free reserves.

Amounts transferred to statutory reserves can be ploughed back into the business of the company. These can be distributed to equity shareholders only on the liquidation or in the case of inadequate profits (under the prescribed conditions).

Repatriation of Capital

Equity funds can be repatriated only on the liquidation or the transfer of shares. Limited buy-back provisions are available under corporate laws. Capital reduction can be undertaken in certain circumstances with court approval. Certain sectors (like defence, construction and development of real estate) are subject to a minimum lock-in period before the capital can be repatriated.

External Commercial Borrowings (ECBs)

Indian companies (other than financial intermediaries) are allowed to raise ECBs from any internationally recognised source such as banks, financial institutions, capital markets, export credit agencies, suppliers of equipment, foreign collaborators, and foreign equity holders.

ECBs can be raised from foreign equity holders holding the prescribed minimum level of equity in the Indian borrower company:

- ECB up to USD 5 million – minimum equity of 25% held directly by the lender;
- ECB more than USD 5 million – minimum equity of 25% held directly by the lender and a debt-equity ratio not exceeding 4:1 (i.e. the proposed ECB should not exceed four times the direct foreign equity holding).

The prevailing ECB policy stipulates certain end-uses; for instance ECBs can be availed only for:

- Import of capital goods, new projects, modernisation and expansion. This window can be availed only for projects in the real estate sector - industrial sector and infrastructure sector ((i) power, (ii) telecommunication, (iii) railways, (iv) road including bridges, (v) sea port and airport, (vi) industrial parks, (vii) urban infrastructure (water supply, sanitation and sewage projects), (viii) mining, exploration and refining and (ix) cold storage or cold room facility, including for farm level pre-cooling, for preservation or storage of agricultural and allied produce, marine products and meat). Rupee/ foreign currency expenditure is permitted up to:
  - USD 500 million for borrowers in the infrastructure and industrial sectors under the automatic route;
  - USD 100 million for borrowers in the service sector (IT, hotels and hospitals) under the automatic route.
- Overseas acquisition by Indian companies;
- First stage acquisition of shares in the disinvestment process and in the public

offer stage under the government's disinvestment programme;

- Lending to self help groups or for micro credit or for bonafide micro finance activity including capacity building by Non-Governmental Organisations engaged in micro finance activities;
- Payment for obtaining a licence/permit for 3G Spectrum is an eligible end - use under the automatic route;
- NBFCs exclusively involved in financing infrastructure projects can avail ECB subject to complying with the prudential standards prescribed by the RBI and the borrowing entities fully hedging their currency risk;
- On-lending by Infrastructure Finance Companies (IFCs) to the infrastructure sector is allowed under the approval route, provided that the IFCs comply with prescribed conditions.

ECBs are not permitted for working capital, on-lending or investment in capital market or real estate.

ECBs are required to have the following prescribed minimum average maturities.

The approval requirements for ECBs have been significantly liberalised. No prior approvals are required for ECBs complying with the prescribed minimum maturities, "all-in-cost" ceilings and end-user requirements. All other ECBs require prior approval from the appropriate RBI committee.

Indian corporate bodies raising ECBs have to retain the funds abroad until the time of their utilisation. Prepayments of up to USD 500 million can be made without approvals, subject to compliance with the minimum average maturity of the loan and in any case three years.

It is permissible for an Indian company to issue equity shares against ECBs in convertible foreign exchange already due for payments or repayment, subject to meeting all applicable tax liabilities and procedures.

Preference Shares

Indian companies can mobilise foreign investments through the issue of preference shares. All preference shares (other than compulsorily convertible preference shares) have to be redeemed out of accumulated profits or proceeds of fresh capital within a period of 20 years under Indian Company Law. The conversion formula and conversion time needs to be determined upfront . The

proposals are processed either through the automatic route or the FIPB route, as the case may be. The following guidelines apply:

- Issue of preference shares is permissible only for a rupee-denominated instrument in accordance with the Indian Companies Act;
- Only compulsorily and fully convertible preference shares are considered foreign direct equity for the purposes of sectoral caps on foreign equity. All other kinds of preference shares, optionally convertible or redeemable, fall outside the FDI cap and would have to comply with ECB norms;
- The dividend rate should not exceed the limit prescribed by the Ministry of Finance (currently fixed at 300 Basis Points above the State Bank of India's Prime Lending Rate).

Debentures

Debentures can be issued by Indian companies to raise funds. The debentures can carry an interest coupon rate. Such interest should typically be tax deductible expense for the Indian company. Where debentures are issued to a foreign investor, they should comply with the FDI policy in case of compulsorily convertible debentures, and with the ECB guidelines where the debentures are non-convertible or optionally convertible. In case of compulsorily convertible debentures (CCDs), conversion terms have to be determined upfront and in any case the conversion price cannot be less than the price arrived at as per pricing norms prescribed by RBI.

Global Depository Receipts (GDR)/ American Depository Receipts (ADRs)/ Foreign Currency Convertible Bonds (FCCBs)

Foreign investment through GDRs/ADRs/ FCCBs is also treated as FDI. Indian companies are permitted to raise capital in the international market through the issue of GDRs/ADRs/FCCBs, subject to certain restrictions.

The issue of ADRs or GDRs does not require any prior approval (either from the Ministry of Finance, FIPB or RBI), except where the FDI after such issue would exceed the sectoral caps or policy requirements, in which case prior approval from FIPB would be required. The issue of FCCBs up to USD 500 million also does not require any prior approvals. Only companies listed on the stock exchange are allowed to raise capital through GDRs/ADRs/FCCBs. The end-use of FCCB proceeds has to comply with ECB norms. Any convertible instrument issued by a listed company has to be mandatorily convertible or redeemable within 18 months.

Foreign Currency Exchangeable Bonds (FCEBs)

In FY 2007-08, the Indian government notified the Foreign Currency Exchangeable Bonds Scheme for the issue of FCEBs. The salient features of the scheme are:

- FCEBs are bonds expressed in foreign currency, the principal and interest of which is payable in foreign currency;
- An FCEB is issued by an issuing company which is part of the promoter group of a listed company whose equity is offered and which is engaged in a sector eligible to receive FDI (offered company) and which holds shares in the offered company. The FCEB is subscribed to by a person resident outside India and is exchangeable into an equity share of the offered company on the basis of any equity related warrants attached to debt instruments;
- The investment under the scheme is required to comply with the FDI policy as well as the ECB Policy requirements. The proceeds of FCEB:
  - are to be used in accordance with end uses prescribed under the ECB policy;
  - are not permitted to be utilised for investments in the capital market or in real estate in India;
  - can be invested by the issuing company overseas by way of direct investment, including in a JV or Wholly Owned Subsidiary (WOS), subject to the existing guidelines on Indian direct investment in a JV or WOS abroad.

Chapter 4

Significant Exchange Control Regulations

Exchange control is regulated under the Foreign Exchange Management Act, 1999 (FEMA). Under the FEMA, foreign exchange transactions are divided into two broad categories: current account transactions and capital account transactions. Transactions that alter the assets or liabilities outside India of a person resident in India or, in India, of a person resident outside India, are classified as capital account transactions. All other transactions are considered current account transactions.

The Indian rupee is fully convertible for current account transactions, subject to a negative list of transactions which are either prohibited or which require prior approval.

An Indian company with foreign investment is treated equally with other locally incorporated companies. Similarly, a foreign-invested Indian company is also treated equally with other locally incorporated companies. Accordingly, the exchange control laws and regulations for residents apply to Indian companies with foreign investment.

Current Account Transactions

Foreign nationals or Indian citizens who are not permanently resident in India and have been deputed by a foreign company to its office/branch/subsidiary/ JV in India are allowed to make recurring remittances abroad for family maintenance of up to 100% of their net salary. Further, up to 100% of the salary of a foreign national or Indian citizen deputed by a foreign company to its Indian office/branch/ subsidiary/JV can be paid abroad by the foreign company subject to the foreign national or Indian citizen paying applicable taxes in India.

Prior approval of the RBI is required for acquiring foreign currency for the following purposes:

- Holiday travel over USD 10,000 per person p.a.;
- Gift over USD 5,000 or donation over USD 10,000 per remitter/donor p.a.;
- Business travel over USD 25,000 per person per visit;
- Foreign studies as per the estimate of the institution or USD 100,000 per academic year, whichever is higher;
- Consultancy services procured from abroad of over USD 1,000,000 per project (USD 10,000,000 in case of infrastructure projects);
- Reimbursement of pre-incorporation expenses over the higher of USD 100,000 and 5% of investment brought into India.

Certain specified remittances are prohibited:

- Remittances out of lottery winnings;
- Remittance of income from racing, riding, etc. or any other hobby;
- Remittance for the purchase of lottery tickets, banned or prescribed magazines, football pools, sweepstakes, etc.;
- Payment of commission on exports made towards equity investments injoint ventures/wholly owned subsidiaries abroad of Indian companies;
- Payment of commission on exports under the rupee state credit route;
- Payment related to “Call Back Services” of telephones;
- Remittance of dividend by any company to which the requirement of dividend balancing is applicable;
- Remittances of interest income of funds held in a non-resident special rupee (account) scheme.

Capital Account Transactions

Capital account transactions can be undertaken only to the extent permitted. The RBI has prescribed a list of capital account transactions, which include the following:

- Investments overseas by residents;
- Borrowing or lending in foreign exchange;
- Export or import of currency;
- Transfer or acquisition of immovable property in or outside India.

Liberalised Remittance Scheme for Resident Individuals

Under the regulations of the Foreign Exchange Management Act, 1999, resident individuals are permitted to remit up to USD 200,000 per FY (Apr-Mar) for any permitted current or capital account transaction, or a combination of both, subject to specified terms and conditions. This is in addition to a facility of foreign travel of up to USD 25,000 per annum. All other transactions which are otherwise not permissible under FEMA and those in the nature of remittances for margins or margin calls to overseas exchanges or overseas counterparties are not allowed under the scheme.

Miscellaneous

Repatriation of Capital

Foreign capital invested in India is generally repatriable, along with capital appreciation, if any, after the payment of taxes due, provided the investment was on a repatriation basis.

Acquisition of immovable property in India

Generally foreigners are not permitted to acquire immovable property except in certain cases, where the property is required for the business of the Indian branch/office/subsidiary of the foreign entity. NRIs or PIOs are permitted to acquire immovable properties (except agricultural land).

Royalties and Technical Know- How Fees

As of 16 December 2009, payments of trademark/ technology royalties have been freed from limits. For any payment relating to a period after 16 December 2009, Indian companies can make payment for trademark/technology royalties without any restrictions under the automatic route.

Dividends

Dividends are freely repatriable after the payment of Dividend Distribution Tax by the Indian company declaring the dividend. No permission of RBI is necessary for a dividend affecting a remittance, subject to specified compliance requirements.

Remittances by Branch/Project Office

No prior approval is required for remitting profits earned by Indian branches of foreign companies (other than banks) to their Head Offices outside India. Remittances of winding-up proceeds of a branch/liaison office of a foreign company in India are permitted subject to the authorised dealer's approval. Remittances of winding-up proceeds of a project office of a foreign company in India are permitted under the automatic route subject to the fulfilment of the compliance requirements.

Chapter 5

Taxation in India

Corporate Tax Rates

Corporate tax rates are as follows:

For a company	*Where taxable income exceeds INR 10 million*	*Other cases*
Domestic company	32.45%	30.9%
	(30% plus surcharge of 5% plus education cess of 3%)	(30% plus education cess of 3%)
Foreign company	42.02%	41.2%
	(40% plus surcharge of 2% and education cess of 3%)	(40% plus education cess of 3%)

Dividend Distribution Tax (DDT)

Dividend income is exempt in the hands of the shareholders. However, a DDT is levied on companies declaring dividends. The effective DDT rate is 16.22% (15% plus 5% surcharge and education cess of 3%). Exemption from DDT to SEZ developers has been withdrawn from 1 June,2011. In order to mitigate the cascading effect of DDT, it is also provided that any dividend received by a domestic company during any financial year from its subsidiary shall be allowed to be reduced from the dividend to be paid/distributed/declared by such a domestic company for the purpose of computation of DDT, provided the following conditions are fulfilled:

- The dividend so received by the domestic company had been subject to DDT;
- The domestic company is not the subsidiary of any other company.

Minimum Alternate Tax (MAT)

With the object of bringing zero tax companies under the tax net, MAT at 18.5%, plus applicable surcharge and education cess, of book profits is levied on companies whose tax payable under normal income tax provisions is less than 18.5% of book profits. Further, MAT will become applicable to SEZ developers/units with effect from FY 2011-12. The current effective MAT rates are as follows:

Company	*Where taxable income exceeds INR 10 million*	*Other cases*
Domestic company	20.01%	19.05%
Foreign company	19.44%	19.05%

A credit of such tax paid under MAT provisions is allowed against the tax liability which arises in the subsequent ten years under the normal provisions of the Income Tax Act. Unadjusted MAT credit can be carried forward till the tenth year following the year in which the credit arises.

Alternate Minimum Tax on Limited Liability Partnerships

MAT provisions which were currently applicable only to companies have now been extended to Limited Liability Partnerships (LLPs) in modified form of Alternate Minimum Tax(AMT) effective FY 2011-12. AMT will be applicable to LLPs at a rate of 18.5%. However in the case of LLPs, AMT will apply to the adjusted total income (as per the Income Tax provisions) rather than the adjusted book profits, as in the case for companies. AMT credit is available to a LLP for 10 years.

Capital Gains

Particulars	*Tax Rates**	
	Resident	*Non-resident*
a. Short-term capital assets[1] (other than (b) below)	Normal corporate/ individual tax rates	Normal corporate/ individual tax rates
b. Short-term capital assets-listed equity shares and units of equity oriented funds which have been charged to Securities Transaction Tax (STT)	15%	15%
c. Long-term capital assets-listed equity shares in a company or unit of an equity oriented fund which have been charged to STT	Exempt	Exempt
d. Long-term capital assets- listed securities (other than (c) above)	10%	10%
e. Other long-term capital assets[2]	20%	20%

* *An applicable surcharge and education cess would also be levied on the above tax rates.*

1 *A short-term capital asset is one which is held for a period of not more than 36 months (not more than 12 months in the case of shares, listed securities, units of mutual funds and zero coupon bonds).*

2 *Indexation of cost of acquisition and improvement of a long-term capital asset of any nature (other than debentures) is available to residents. However, the benefit of indexation is available to non-residents only on long-term capital assets other than shares/ debentures of an Indian company acquired in foreign currency. Securities, including equity shares in a company or unit of an equity oriented fund, which have not been charged to STT, may be taxed @ 10%(plus applicable surcharge and education cess) without giving any indexation benefit at the option of the taxpayer.*

Computation of Total Income - General

- All incomes accruing or arising in India are taxable in India to a non- resident taxpayer subject to the Double Taxation Avoidance Agreement (DTAA) with the country of residence of the taxpayer;
- Taxable income is computed for a uniform accounting year, i.e. the fiscal year from 1 April to 31 March;
- The taxable income is called “Total Income”, which is computed after adding certain disallowances, such as loss on sale of assets and miscellaneous expenditure written off and the reduction of certain allowances/benefits from the book profits.

Depreciation

Depreciation is allowed separately at the following rates for computing taxable income:

Factory Building	10%
Furniture and fittings	10%
Plant and machinery (general)	15%
Computers (including software)	60%
Motorcars, other than those used in a business of running them on hire	15%
Intangible assets (such as know-how, patents, copyrights, trademarks, licences, franchises or any other business or commercial rights of a similar nature)	25%

For certain priority items, such as energy saving devices and pollution control equipment, depreciation is allowed at higher rates. Undertakings engaged in the business of generation or generation and distribution of power have the option of claiming tax depreciation at the above rates or on a straight-line basis at rates prescribed in the Income-tax Rules, 1962. The rates vary from 1.95% to 33.40%.

In the case of a new asset, depreciation for the full year is allowed only if the asset is put to use for 180 days or more during the fiscal year; otherwise depreciation is allowed at only half the prescribed rate.

In addition, depreciation of 20% of the actual cost of a new plant or machinery acquired and installed after 31 March 2005 is allowed to a taxpayer engaged in the business of manufacture or production of any article or product in the year in which such a new plant or machinery is acquired and installed.

Taxation of Know-how Fee in the Hands of Foreign Companies

Under domestic tax law, the royalties/technical fees payable to non-residents with a permanent establishment in India are taxed on a net basis. In contrast, the royalties/technical fees payable to non-residents without a permanent establishment in India are taxed on a gross basis. Concessional tax rates, as given below, apply if the agreement relates to a matter included in industrial policy or if the agreement has been approved by the government of India:

For contracts entered on or after 1 June 2005	10%
For contracts entered into after 31 May 1997 but before 1 June 2005	20%
For contracts entered into on or before 31 May 1997 (Surcharge and education cess, as applicable, would also be levied.)	30%

Taxation of dividends received from overseas group companies

From FY 2011-12 dividends received by Indian companies from specified foreign companies will be taxed at a concessional rate of 15%. However no expenditure would be deductible while computing this dividend income."Specified foreign company"means a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital.

Double Tax Avoidance Agreements

Double Tax Avoidance Agreements override the Indian Income-tax Act provisions to the extent that they are more beneficial to the assessee (concessional tax rates applicable under certain double tax avoidance conventions that India has signed with various countries are provided in tabular form under Annexure 2).

Relief is granted in respect of income chargeable to tax, both under the Income-tax Act of India and the domestic tax laws in that other country, in order to promote mutual economic relations, trade and investment.

Tax Information Exchange Agreements(TIEA)

Recently, India has entered into TIEAs with Bermuda, Isle of Man, British Virgin Islands, Bahamas and Cayman Islands. The objective of the TIEA is to promote international cooperation in tax matters through exchange of information. These agreements provide for sharing information including exchange of banking and ownership information. However, the nature of tax related information that could be shared under a TIEA varies from agreement to agreement.

Transactions with persons located in Notified Territories

In order to discourage transactions with persons located in a country which does not effectively exchange information with India, certain anti-avoidance measures have been introduced from 1 June, 2011. These measures would enable the Government to designate any Country/jurisdiction not exchanging information with India as a 'notified jurisdictional area'. Transactions between any taxpayer and a party located in a notified jurisdictional area would be deemed to be a transaction between "associated enterprises" and transfer pricing regulations will apply accordingly. Transactions with persons located in these jurisdictions would have the following additional implications:

- No deduction would be allowed in respect of payments made to any financial institution unless an authorisation is issued to the income tax authorities to seek relevant information from this financial institution;
- No deduction would be allowed for any expenditure or allowance unless the taxpayer maintains the prescribed documents or provides the prescribed information to the tax authorities;
- Receipts from a person located in the notified jurisdictions, shall become taxable income for the taxpayer unless he is able to explain the source of such money in the hands of the payer or in the hands of the beneficial owner;
- Payments made to a person located in a notified jurisdictional area shall be liable for higher withholding tax.

Advance Rulings

To facilitate full planning and to avoid any future disputes under the Income-tax Act, a non-resident can approach the Authority for Advance Rulings to determine the income tax aspects of any proposed or current transaction.

An advance ruling can also be sought by a resident to determine the tax liability of a non-resident with whom a transaction has been undertaken or is proposed to be undertaken.

Certain notified residents may also apply to the Authority for Advance Rulings to seek a ruling concerning the computation of total income.

Such an advance ruling would be binding on the person seeking it in relation to the transaction and the income tax department cannot disregard the ruling unless there is some change in the facts or law affecting it.

Wealth Tax

Wealth tax is charged on net wealth as on 31 March every year (referred to as the valuation date). Wealth tax is charged both on individuals and companies at the rate of 1% of the amount by which the "net wealth" exceeds INR 3 million. The term "net wealth" broadly represents the value of the excess of certain assets over the debts concerned. Assets include guest houses and residential houses, motorcars, jewellery / bullion / utensils of gold and silver, yachts, boats, aircraft, urban land and cash in hand. A debt is an obligation to pay a certain sum of money incurred in relation to those assets which are included in the "net wealth".

Transfer Pricing

Provisions relating to transfer pricing facilitate the computation of reasonable, fair and equitable profits and tax in India in the case of businesses carried on by multinational companies. Essentially, transfer pricing is the process of adjusting the prices of cross-border transactions between related or associated parties. The transfer pricing provisions generally follow the relevant Organisation for Economic Co-operation and Development (OECD) guidelines. However, there are certain fundamental differences. The Indian provisions require the computation of an "arm's length price" compared to the internationally accepted norm of an arm's length range. Further, the arm's length price is to be computed as the "arithmetic mean" of comparable results. A variance of around 5% of the mean may be chosen. However w.e.f 1 April, 2012, the Central Government would notify the variance percentage.

Section 92 of the Income-tax Act provides that the price of any transaction between associated enterprises, either or both of whom are non-resident for tax purposes (international transaction), is to be computed with regard to the arm's length principle.

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 enterprises.

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

- Direct/indirect shareholding having 26% or more of voting power;
- Advancing of loans of 51% or more of total assets;

- Appointment of more than 50% of the Board of Directors;
- Sale of manufactured goods under influenced prices;
- Dependence on Intellectual Property Rights owned by either party.

Determination of the "arms length price"

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

- Comparable Uncontrolled Price Method;
- Resale Price Method;
- Cost Plus method;
- Profit Split Method;
- Transactional Net Margin Method.

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

Burden of Proof and Assessment

The burden of proving that the international transactions are in accordance with the arm's length principle lies with the taxpayer. For this purpose, the Income-tax Act requires the maintenance of prescribed information and documents relating to international transactions undertaken between associated enterprises. Failure to do so attracts very significant penalties. Also, it is mandatory to obtain an accountant's certificate in a prescribed format in respect of all international transactions between associated enterprises. Such a report would have to contain prescribed particulars of the transaction and would have to be filed with the tax authorities by 30 November(in the case of companies) of the relevant assessment year.

Once the accountant's certificate has been filed, the concerned tax officer may call for the prescribed documentation in the assessment proceedings. Based on available information, the tax officer may adjust or recompute the prices used in international transactions. Such an adjustment would attract tax and interest on the additional amount. Potentially, a penalty of 100% to 300% of the tax on the adjusted amount could also be levied.

With the approval of the Commissioner of Income-tax(CIT), the Assessing Officer may refer the case to specially appointed Transfer Pricing Officers (TPO) for a detailed review. Effective 1 June 2011, this review would cover determination of ALP in respect of transactions noted by him subsequently during the course of proceedings before him. The order of such a TPO would have to be considered by the Assessing Officer when finalising the assessment.

Dispute Resolution

To expedite the resolution of disputes, Dispute Resolution Panels (DRP) comprising three CITs have been constituted.

Such an alternate scheme of dispute resolution shall apply in respect of foreign companies /transfer pricing orders to be passed on or after 1 October 2009 which are prejudicial to the assessee. In such cases, the Assessing Officer is required to forward a draft order to the assessee. The assessee can file objections against the draft order before the DRP. After considering all evidence/objections and further enquiries, the DRP is to issue binding directions to the Assessing Officer within nine months. The Assessing Officer passes an order within one month in conformity with the directions of the DRP.

Direct Tax Code (DTC)

On 30 August 2010 the government placed before the Parliament the Direct Taxes Code Bill, 2010. The Bill is modelled on the draft Direct Taxes Code that was originally released in August 2009, changes proposed in the Revised Discussion Paper released in June 2010 and further suggestions and comments made on this by stakeholders. The salient features of the Bill are summarised in Annexure 3. The Bill has now been referred to the Standing/Select Committee of the Indian Parliament for further deliberation. Comments and suggestions have been invited by the Government on the same.

Individual Tax

General

A foreign national seconded to work in India, in general, becomes liable to Indian income tax. Other taxes to which an individual may become liable are capital gains tax levied on disposal of assets in India and wealth tax levied on possession of taxable wealth. Taxation in India is based on the residential status of a person and not on citizenship. The residential status of a person under Income-tax Act is determined solely based on his or her physical presence in India regardless of purpose of the stay. A person may qualify to be a Resident and Ordinarily Resident (ROR), Resident but not Ordinarily Resident (RNOR) or a Non-Resident (NR) in India.

Scope of Taxation

Salary income is subject to income tax in India if services are rendered in India, irrespective of whether salary is received in India or not. Other incomes are subject to income tax if received or are deemed to be received in India, or accrue or arise or are deemed to accrue or arise in India. However, ROR income that accrues or arises outside India will also be subject to tax in India. In other words, an expatriate who is ROR is taxed on his/her worldwide income.

Double Taxation Avoidance Agreement

Where an individual is treated as a tax resident of another country, that individual qualifies for relief from Indian tax under a double taxation agreement between that country and India. Most Agreements set various tests to determine in which of the two countries an individual is resident for taxation purposes. Most agreements contain clauses which exempt a resident of one country from tax on employment income in India if he is present in India for less than 183 days in a tax year, and fulfil some other conditions. Where an individual is doubly taxed in India, credit of taxes paid overseas on such doubly taxed income is available in accordance with the relevant Agreement.

Indian Social Security (Provident Fund)

The Government has introduced compulsory social security regulations for employees holding foreign passports and working for an entity in India to which the Provident Fund (PF) Rules apply. India has, principally, two types of Social Security schemes, namely, an Employees Provident Fund and an Employee Pension Scheme.

Under the scheme an international worker is required to contribute 12% of his salary every month towards the PF. The employer is required to make a matching contribution. A part of the employer's contribution (at the rate of 8.33%) is allocated to the Employee Pension Fund.

The accumulated balance in PF is refundable along with interest on fulfilment of specified conditions. However, pension contributions are treated on the principles of reciprocity with the home country of foreign nationals. The employer is required to deposit the contributions (both employer and employee) with the Authorities by the designated dates.

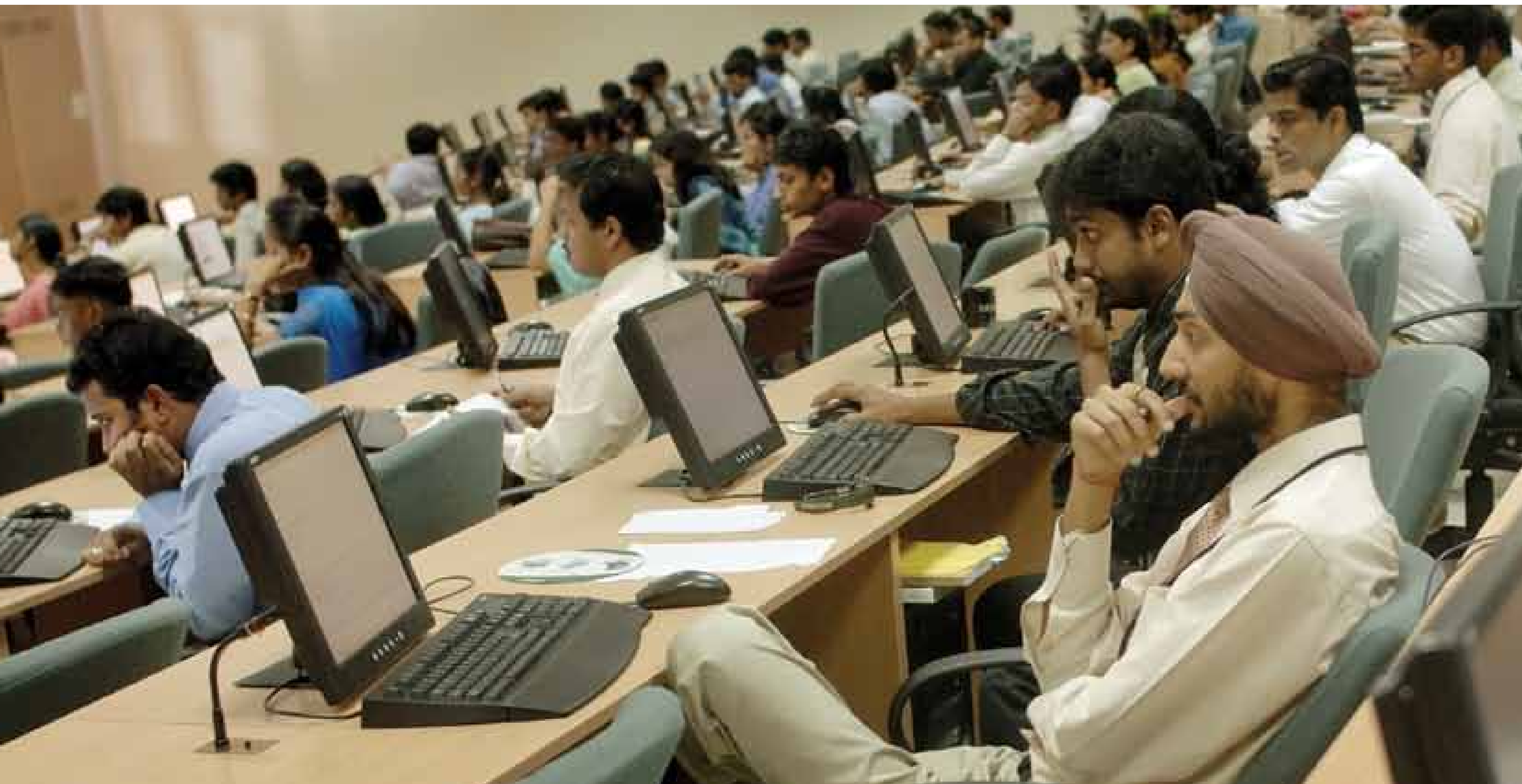
In the case where an individual comes from a country with which India has a Social Security Agreement (SSA) then he or she may claim exemption from India social security subject to the relevant conditions being fulfilled. India has so far signed SSAs with Belgium, France, Germany Luxembourg, Netherlands, Switzerland, Hungary, Denmark, the Czech Republic, Norway and the Republic of Korea. Out of above agreements, only the agreement with Belgium, Germany and Switzerland have so far been notified and made operational. At the end of each year, a tax return has to be filed with the income tax authorities in the prescribed form. The return is to be filed at the latest by July 31 of the relevant assessment year

Personal income tax rates

Taxable Income Over (INR.)	*Not Over (Rs.)*	*Tax on Column 1 (INR.)*	*Percentage on excess (%)*
0	180,000	-	0%
180,000	500,000	-	10%
500,000	800,000	32,000	20%
800,000	And above	92,000	30%

A resident woman(below 60 years of age) and a resident senior citizen(aged above 60 but below 80 years), with income upto INR 190,000 and INR 250,000 respectively do not have to pay tax. Very senior citizens (aged 80 years and above) do not have to pay tax upto income of INR 500,000.

Further, an education cess @ 3% of the tax is levied (irrespective of the level of income).



Immigration (Work permit / Visa)

An individual visiting India must have a valid passport. According to the provisions of The Foreigners Act 1946 and The Foreigners Order 1948, a valid visa is required for any "foreigner" intending to visit India. However, a foreigner who is Person of Indian Origin (PIO) or Overseas Citizen of India (OCI) card holder is exempted from visa requirements. There have been significant developments in the visa regime in terms of the nature of visa needed, the limit on hiring foreign nationals, etc. Seeking professional advice prior to applying for visa is strongly recommended.

Under the provisions of the Registration of Foreigners Rules 1939, any foreign national visiting India who either has valid visa or is intending to stay for more than 180 days, must register within 14 days of arrival with the "Foreigners Regional Registration Officer" (FRRO). OCI card holders are exempted from registration with FRRO. PIO card holders are required to register only when their continuous stay in India exceeds 180 days.

Gift Tax

There is no gift tax liability in India. Any sum of money exceeding INR 50,000 or immovable property whose stamp duty value exceeds INR 50,000 or any immovable property whose fair market value exceeds INR 50,000 received without consideration by an individual from any person would be subject to tax as "Income from other sources". This would not apply to any sum of money received:

- from any relative (spouse, brother, sister, brother or sister of the spouse or any lineal ascendants or descendants);
- on the occasion of the marriage of the individual;
- under a will or by way of inheritance;
- in the expectation of the death of the donor.

Indirect Taxes

Customs Duty

Customs duty is levied by the Central Government on the import of goods into, and export from India. The rate of customs duty applicable to a product to be imported/ exported depends upon on its classification under the Customs Tariff Act. With regard to exports from India, duty is levied only on a very limited list of goods.

The Customs Tariff is aligned with the internationally recognised Harmonised Commodity Description and Coding System of Tariff Nomenclature (HSN) provided by the World Customs Organization.

The peak rate of Basic Customer Duty (BCD) is currently set at 10% for all goods other than agricultural and other specified products. However, the Indian central government has the power to exempt goods of any specified description from the whole or any part of custom duties. In addition, preferential/concessional rates of duty are available under the various bilateral and multilateral trade agreements entered into by India with other parties.

Customs duty is levied on the transaction value of the imported or exported goods. Under Section 14 of the Customs Act 1962, the concept of transaction value is the sole basis of valuation for purposes of import and export. While the general principles adopted for valuation of the goods in India are in conformity with the World Trade Organisation agreement on customs valuation, the central government has established independent Customs Valuation Rules applicable to the export and import of goods.

India does not have one uniform rate of customs duty and the customs duty applicable to any product is composed of a number of components. The types of customs duties applicable are as follows:

- BCD is the basic component of customs duty levied at the effective rate notified under the First Schedule to the Customs Tariff Act, 1985 (CTA) and applied to the landed value of the goods (i.e. the Cost CIF value of the goods plus landing charges at 1%);
- The Countervailing Duty (CVD) is equivalent to, and is charged in lieu of, the excise duty applicable on like goods manufactured in India. CVD is calculated on the landed value of the goods and the applicable BCD. However, the CVD on specific consumer goods intended for retail sale is calculated on the basis of the maximum retail price (MRP) printed on their packs after allowing specified abatements. The general rate of excise duty is currently at 10% and consequently the rate of CVD is also 10%. In addition, Education Cess (EC) at 2% and Secondary & Higher Education Cess (SHEC) at 1% are also levied on the CVD;
- Further, EC at 2% and SHEC at 1% are also levied on the aggregate customs duties (except safeguard duty, countervailing duty and anti-dumping duty). Goods attracting customs duties at bound rates under international commitments (for example, the IT Agreement and Indo-US Textile Agreement) have been exempted from these cesses;
- Addition Duty of Customs (ADC) at 4% is charged in addition to the above duties on all imports subject to a few exceptions. The exemptions include:
  - Goods which are fully exempt from BCD and CVD;
  - Goods for export promotion schemes under which imports are allowed at zero duty;
  - Imports by 100% EOUs and units in EHTPs/STPs or SEZs;
  - Domestic Tariff Area (DTA) clearance of 100% EOUs/EHTPs/STPs/SEZ units, provided such goods are not exempt from sales tax/VAT;
  - Pre-packed goods intended for retail sale in India and having a requirement to declare MRP either under the Standards of Weight and Measures Act or any other law for the time being in force;
  - Mobile phones, watches and readymade garments.

ADC is calculated on the aggregate of the assessable value of the imported goods, the total customs duties (i.e. BCD and CVD) and the applicable EC and SHEC.

BCD, EC and SHEC levied on the aggregate customs duties are a cost on any import transaction. The duty incidence arising on account of all other components may be set off/refunded subject to prescribed conditions. Where goods are imported for the purposes of manufacture, the Indian manufacturer may take a credit of the CVD and ADC paid at the time of import for setting off against the output excise duty. In the case of service providers, CVD credit is available. Similarly, the central government allows a refund of the mechanism in relation to the ADC paid on goods imported for the purpose of trading in India, subject to fulfilment of the conditions prescribed under the governing notifications and circulars issued in this regard.

CENVAT (Excise Duty)

Central Value Added Tax (CENVAT) is a tax levied by the central government on the manufacture or production of movable and marketable goods in India.

The rate at which excise duty is leviable on the goods depends on the classification of the goods under the Excise Tariff. The Excise Tariff is primarily based on the eight digit HSN classification adopted so as to achieve conformity with the Customs Tariff.

The excise duty on most consumer goods which are intended for retail sale is chargeable on the basis of the MRP printed on the goods packaging. However, abatements are admissible at rates ranging from 20% to 50% of the MRP for the purposes of charging Basic Excise Duty (BED). Goods other than those covered by a MRP based assessment are generally chargeable to duty on the "transaction value" of the goods sold to an independent buyer. In addition, the central government has the power to fix tariff values for charging ad valorem duties on the goods.

Under the rationalised structure, the standard rate of BED is 10%. There is concessional rate of excise duty of 5% on 76 items. Further, 130 items attracts excise duty at 1% ad valorem. In addition, some goods, such as specified motor vehicles, attract higher CENVAT rates of 22%.

Notifications granting partial or complete exemption to specified goods from payment of excise duties are also available. EC at 2% and SHEC at 1% are applicable on the aggregate excise duties.

The central excise duty is a modified form of Value Added Tax (VAT) where a manufacturer is allowed credit on the excise duty paid on locally sourced goods and the CVD and ADC paid on imported goods. The CENVAT credit can be utilised for payment of excise duty on the clearance of dutiable final products manufactured in India. In the light of the integration of goods and services tax initiated in 2004, manufacturers of dutiable final products are also eligible to avail CENVAT credit of the service taxes paid on input services used in or in relation to the manufacture of final products and clearances of final products upto to the place of removal. In addition, CENVAT credit is admissible on the following input services:

- Services used in relation to setting up, modernisation, renovation or repairs of a factory, a premises of a service provider or an office relating to such a factory or premises;
- Advertisement or sales promotion services;
- Services in relation to procurement of inputs;
- Activities relating to business such as accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry

and security, inward transportation of inputs or capital goods and outward transportation.

The Finance Act 2011 has introduced some specific exclusions from the definition of Inputs and input services eligible for claiming for credit, such as:

- Specified input services and inputs used for construction of buildings or civil work;
- Specified input services which are primarily for personal use and consumption of any employee

A manufacturer of dutiable and exempt goods, using common inputs or input services and opting not to maintain separate accounts, may choose between the following options:

- Reverse the credit attributable to the inputs and input services used for manufacture of the exempted goods, to be worked out in a manner prescribed in the rules; or
- Pay a percentage of the value of the exempted goods.

Service Tax

Service tax is levied on specified taxable services identified under Chapter V of the Finance Act, 1994 (the Act). At present approximately 120 services are classified as taxable under the Act. The existing rate of service tax is 10%. In addition, EC of 2% and SHEC of 1% of the service tax is levied on taxable services. Thus the effective rate of service tax is 10.30%.

The Finance Act, 2011 has amended the scope of various categories of taxable services such authorized service station, life insurance service, clubs, business support services, legal professional services and clinical establishment services.

- Services by air-conditioned restaurants having license to serve liquor;
- Short-term accommodation in hotels / inns / clubs / guest houses etc;

The onus of payment of service tax lies on the provider of the services. However, for specified services, such as transport of goods by road and sponsorship services, the service tax liability rests with the recipient of the services.

Taxable services provided by service providers located outside India to a recipient in India are subject to service tax in terms of the Services (Provided from Outside India and Received in India) Rules, 2006. Under these rules, where the taxable services are provided from outside India and received in India, the service recipient is required to register and pay the tax in accordance with the relevant provisions of law.

The current threshold limit for service tax exemption for small service providers is INR 10 lakhs. The threshold limit for obtaining service tax registration is INR 9 lakhs. All persons liable to pay service tax on eligible taxable services received or provided by them are required to obtain service tax registration from the jurisdictional Service Tax Commissioner. In this connection, the Service Tax Rules, 2004 provide that service recipients liable to pay service tax who receive services in more than one premises or office, and who have a centralised billing or accounting system, can opt for centralised registration by making an application to the Commissioner of Central Excise within whose jurisdiction the premises or office from where the centralised billing or accounting is located.

Service tax was earlier charged on the gross value of the services which have been rendered. The Central Government has introduced the Service Tax (Determination of Value) Rules, 2006. The main features of these rules are detailed below:

- Where the consideration received for taxable service is not wholly or partly in money, the value of the taxable service would be equal to the gross amount charged by the service provider for a similar service as the sole consideration to any other person;
- Where such a value of a similar service is not available, the value of the taxable service shall be determined by the service provider and shall not be less than the cost of provision of such services;
- Any expenditure or costs incurred in providing taxable services shall be included in the value of such services;
- Only such expenditure as is incurred as a pure agent of the service receiver shall be excluded from the value of taxable services;
- In the case of services imported into India, the value of taxable services will be equal to the actual consideration charged;
- The Proper Officer has powers to question the valuation of such services and to re-determine the value after giving the assessee reasonable opportunities to be heard.

In the light of the integration of goods and services tax, a service provider can avail CENVAT credit of excise duties paid on capital goods and inputs used for providing output services, along with the service taxes paid on input services subject to fulfilment of certain prescribed conditions.

Also, the central government has, under the Export of Service Rules, 2005 (Export Rules), provided that no service tax is chargeable on the export of services. The benefit of exemption from service tax would be available on exported services, subject to the fulfilment of the conditions prescribed under the Export Rules.

As an alternative, the service provider can also discharge the service tax on exports and claim a rebate of the service tax paid. In addition to the rebate of tax paid on the exported services, rebate/refund provisions have been

established with regard to the service tax paid on input services and excise duty paid on input goods used in providing the exported services.

The Finance Act 2011 has introduced Points of Taxation rules, which provides guidelines for determination of point of time as to when the service could be said to have been provided or received for the purpose of collection and payment of Service Tax. These rules prescribe accounting of services tax on accrual basis as against the earlier system of cash basis.

E-payment of service tax has been made mandatory for certain categories of large assessees with effect from 1 October 2006.

Sales Tax

The sale of movable goods in India is chargeable to tax at the central or state level. The Indian regulatory framework has granted power to state legislatures to levy tax on goods sold within that state. Such sales are, therefore, chargeable to VAT at the rates notified under the VAT laws of the relevant state.

All goods sold in the course of interstate trade are subject to Central Sales Tax (CST).

Where goods are bought and sold by registered dealers for trading or for use as inputs in the manufacture of other goods or specified activities (such as mining or telecommunications networks), the rate of sales tax is 2%, provided Form C is issued by the purchasing dealer. In the absence of that Form C, the applicable rate would be the rate of VAT on such goods in the originating state.

CST is sought to be phased out before introduction of Goods and Services Tax (GST) in India, which is presently expected to be introduced by during the year 2012 - 2013. In the interim, CST will continue to coexist with state VAT.

Inter-state procurement on which CST is charged in the originating state is not eligible for input tax credit in the destination state.

VAT

State level sales tax was replaced by VAT with effect from 1 April 2005 in the majority of Indian states. The states of Tamil Nadu, Pondicherry and Uttar Pradesh replaced the state sales tax regime with VAT from 1 January 2007, 1 June 2007 and 1 January 2008 respectively. With the introduction of VAT in the state of Uttar Pradesh, the process of replacing state level sales tax with VAT was completed.

Under the VAT regime, the VAT paid on goods purchased from within the state is eligible for VAT credit. The input VAT credit can be utilised against the VAT/ Central Sales Tax payable on the sale of goods. This ensures that the cascading effect of taxes is avoided and that only the value addition is taxed.

Currently, there is no VAT on imports into India. Exports are zero rated. This means that while exports are not charged to VAT, VAT charged on inputs purchased and used in the manufacture of export goods or goods purchased for exports is available to the purchaser as a refund.

State VAT is charged at varying rates of 1%, 4%, 5% and 20%. Goods other than those notified to be covered under the above rates are charged at a general rate ranging from 12.5% to 15%. Some of the states have varied these tax rates.

Turnover thresholds have been prescribed so as to keep small traders out of the ambit of the VAT. A tax under a composition scheme, at a lower rate, may be levied on such small traders in lieu of the VAT.

The following conditions also apply to VAT:

- VAT registered dealers need to issue serially numbered invoices with prescribed particulars;
- The periodicity of filing of VAT returns, in most states, is the same as that prescribed in the previous sales tax regime;
- A comprehensive self-assessment of VAT has been introduced;
- Turnover taxes, surcharges, additional surcharges and the special additional tax have been abolished, excepting certain states such as Gujarat and Kerala;
- Entry taxes continue, but have been made VATable, except where they are in lieu of Octroi.

The Central Government took a major step towards the transition to a national integrated GST in 2006. Implementation of GST will be a historical reform in the history of India as it will subsume majority of taxes such as CVD, Excise, Service Tax, CST, State VAT and some other state levy.

At present a dual rate GST model is envisaged whereby the convergence of rate of tax to one standardised rate of 16% on across goods and services is expected to happen in three years of implementation.

Under the proposed dual GST model, a central GST as well as a state GST will be levied on the taxable value of a transaction of supply of goods and services and both the centre and the state will legislate, levy and administer the central GST and the state GST respectively.

A reform like GST is obvious to attract lot of deliberation and discussion at all stages of planning and implementation and as such is time intense effort. Implementation of GST also entails Constitutional amendments as to the rights and powers of State and Central government to levy different taxes. Still with regards to the concentrated efforts of political bureau it is expected to be rolled out during the year 2012 - 2013.

Octroi Duty / Entry Tax

"Entry Tax" is a tax on entry of goods into the state from outside the state for use, consumption or sale therein. Entry tax continues to exist under the VAT regime, though in certain states it has been made VATable and can be set off against the output VAT liability in the state.

Entry tax is leviable on purchase value, which is defined to mean the amount of the valuable consideration paid or payable by a person for the purchase of any goods. The value of the specified goods can be ascertained from the original invoice for purchase of such goods.

Octroi is a municipal levy which is levied at the time of entry of specified goods into the limits of the relevant municipal corporation. Thus, Octroi can be leviable, if there is movement of goods from one city to another in the same state, in the event the cities fall under the jurisdiction of two different municipal corporations.

Stamp Duty

Stamp duty is levied at various rates on documents such as bills of exchange, promissory notes, insurance policies, contracts effecting transfer of shares, debentures, and conveyances for transfer of immovable property.

Research and Development Cess

Research and Development Cess of 5% is levied on all payments made for the import of technology. The term "technology" includes import of designs, drawings, publications and services of technical personnel (the amount leviable to cess includes the living costs of technical personnel in India).

Tax Incentive Scheme

100% Export Oriented Units (100% EOU) Scheme

The 100% EOU Scheme was introduced by the Government in 1980 with a view to promoting exports by creating additional production capacities.

- 100%EOUs are extended a host of incentives and facilities, including duty free imports of capital goods, raw material, and consumables as well as tax deductions against export income;
- These units are permitted to be set up for a varied range of business activities including manufacture, services, software development, agriculture, aquaculture, animal husbandry, floriculture, horticulture and sericulture, without any restrictions of location;
- Trading activities are not covered for the purpose of the benefits extended to these units.

Undertakings set up in EOUs are eligible for a deduction of 100% of the derived export profits for 10 years up to 31 March 2011.

The exemption from MAT enjoyed by these units was withdrawn with effect from 1 April 2007.

Special Economic Zone Scheme

The SEZ Policy was introduced by the Government in 2000 with a view to providing an internationally competitive and unproblematic environment for exports. The SEZ Act, 2005 along with the associated Rules, provides the umbrella legal framework for all important legal and regulatory aspects of SEZ development as well as for units operating in SEZs.

SEZs are duty-free enclaves considered to be outside the customs territory of India for the purposes of carrying out their authorised activities.

SEZ developers are entitled to 100% tax holidays (of profits and gains derived from the business of developing the SEZ) for ten consecutive years out of 15 years beginning from the year in which the SEZ is notified by the government. Exemption from DDT has been discontinued with effect from 1 June, 2011 and exemption from MAT has been discontinued from FY 2011-12.. Expenditure undertaken by a developer on account of the development of SEZ is also exempt from duties of customs, excise and central sales tax.

A unit set up in an approved SEZ enjoys a 100% tax holiday for five years and 50% for the next ten years (during the last five years subject to certain additional conditions) out of profits derived from actual exports of goods and services. The tax holiday period commences from the year in which the SEZ unit begins to manufacture or produce or provide services.

Annexure 1 sets out the salient features and benefits of the SEZ.

Electronic Hardware Technology Park (EHTP) Scheme and Software Technology Parks of India (STPI) Scheme

In a bid to enhance the export potential of the electronics industry and develop an efficient electronic component and information technology industry, the EHTP and STP schemes have been announced. These offer a package of incentives and facilities like duty free imports in line with the 100% EOU scheme, as well as deemed export benefits and tax holidays. Export-oriented IT enabled services like call centre services, data processing, medical transcriptions, etc. are also eligible to be registered under the STP scheme.

The Directors of STPs in respect of STP proposals and the Designated Officers in respect of EHTP proposals accord approval to such units subject to compliance with the set of conditions applicable to units set up under the 100% EOU Scheme.

Undertakings set up in EHTPs or STPs are eligible for a deduction of 100% of export profits for ten years up to 31 March 2011.

The exemption from MAT enjoyed by these units was withdrawn from 1 April 2007.

Setting up of Industrial Parks

Under the Industrial Park Scheme 2008 notified by the Central Board of Direct Taxes, the industrial park developers are eligible for 100% tax deduction to be provided for ten consecutive assessment years out of 15 years after the commencement of operations of such units.

Some of the conditions to be fulfilled to avail the benefit of an industrial park are;

- The date of commencement of the industrial park should be before 31 March 2011;
- The area allocated or to be allocated to industrial units shall not be less than 90% of the allocable area;
- There should be a minimum of thirty industrial units located in an industrial park;
- For the purpose of computing the minimum number of industrial units; all units of a person and his/her associated enterprises to be treated as a single unit;
- The minimum constructed floor area should not be less than 50,000 square metres;
- No industrial unit, along with the units of an associated enterprise, should occupy more than 25% of the allocable area;
- The industrial park should be owned by only one undertaking; and
- Industrial units should undertake only manufacturing activity as defined in National Classification, 2004, Code issued by the Central Statistical Organisation, Department of Statistics.

100% tax deduction is available to the developers of industrial parks for any ten consecutive assessment years out of 15 years beginning from the year in which the undertaking or the enterprise develops and begins to operate an industrial park.

Enterprises / Undertakings in Industrial Parks in Specified States

Income tax holidays and exemptions from CENVAT are available for units set up in industrial parks in the states of Uttranchal, Himachal Pradesh and the North East states, subject to certain conditions. These have been summarised below:

State	*Incentives*	*Validity Period*	*Eligible Units*
Uttaranchal/ Himachal Pradesh	100% income tax holiday for first 5 years, next five years - 30% (25% if the assessee is not a company) 100% exemption from CENVAT	Ten years	Units engaged in specified activities that (a) begin manufacturing/ commence operations; or (b) undertake substantial expansion from 7 January 2003 up to 31 March 2012 New units commencing commercial production or existing units undertaking more than 25% expansion in installed capacity on or after 7 January 2003 but before 31 March 2010
North-Eastern States (including Sikkim)	100% income tax holiday Concessional rate of duty payable on ten years, value addition during manufacture or refund of duty in cash, subject to conditions	Ten years	Units that (a) begin manufacturing any eligible article or thing; (b) undertake substantial expansion; or (c) carry out prescribed eligible business, from 1 April 2007 to 31 March 2017 New industrial units and units existing before 1 April which have undertaken substantial expansion by refund of duty paid in cash, subject to increase in investment by 25% or more commencement of production between 1 April 2007 and 31 March 2017

Tax Holiday in Respect of Infrastructure / Power / Natural Gas Network

Undertakings engaged in prescribed infrastructure projects are eligible for tax deduction of profits from the following business:

- 100% tax deduction for ten consecutive years in a block of 20 years for undertakings engaged in developing, operating and maintaining infrastructure facilities like roads, bridges, rail systems, highway projects, water supply projects, water treatment systems, irrigation projects, sanitation and sewerage systems or solid waste management systems systems;
- 100% tax deduction for ten years in a block of 15 years for undertakings involved in developing, operating and maintaining ports, airports, inland waterways or inland ports;
- 100% tax deduction for ten years in a block of 15 years to undertakings which:
  - are set up in any part of India for the generation or generation and distribution of power and begin to generate power before 31 March 2012; or
  - start transmission or distribution by laying a network of new transmission or distribution lines before 31 March 2012; or
  - undertake substantial renovation and modernisation of the existing network of transmission or distribution lines before 31 March 2012.
- Seven year tax holiday available to entities engaged in the production of mineral oil would not be available for blocks licensed under contracts awarded after 31 March, 2011.

Investment linked deduction in respect of specified businesses

Investment linked tax incentive provided by way of allowing 100% deduction in respect of any expenditure of capital nature (other than on land, goodwill and financial instrument) is available to six specified types of businesses, viz.

- Setting up and operating a cold chain facility on or after 1 April, 2009;
- Setting up and operating a warehousing facility for storage of agricultural produce on or after 1 April 2009;
- Laying and operating a cross-country natural gas or crude or petroleum oil pipeline for distribution, including storage facilities being an integral part of such network commencing operations on or after 1 April, 2007;
- Building and operating, anywhere in India, a hotel of two-star or above category commencing operations on or after 1 April 2010;
- Building and operating, anywhere in India, a hospital with at least one hundred beds for patients commencing operations on or after 1 April 2010;
- Developing and building a housing project under a scheme for slum redevelopment or rehabilitation commencing operations on or after 1 April, 2010;
- Recently, two new businesses have been included as “specified business” i.e.
- Developing and building a housing project under a notified scheme of affordable housing framed by the Central Government or a State Government commencing operations on or after 1 April, 2011; and

- Production of fertiliser in India in a new plant or in a newly installed capacity in an existing plant commencing operations on or after 1 April, 2011.

Tax Holiday in Respect of Other Facilities

Food Processing Units

A 100% tax holiday for the first five years and a deduction of 30% (25% if the assessee is not a company) of profits for the next five years are available to undertakings engaged in the business of processing, preservation and packaging of fruits and vegetables or in the integrated business of handling storage and transportation of food grains, starting operations on or after 1 April 2001.

Further this tax holidays is extended to additional industries such as processing, preserving and packaging of meat and meat products or poultry, marine and dairy products, if they begin to operate on or before 1 April 2009.

Scientific Research and Development

If certain conditions are met, a deduction is available of twice the amount of scientific research expenditure incurred on an approved in-house research and development facility by a company engaged in the business of bio-technology or any business of manufacture or production of any article or thing except specified articles. Currently, this weighted deduction is available until FY 2011-12.

Further, from FY 2011-12, any sum paid to a National Laboratory or a university or an Indian Institute of Technology or an approved scientific research programme also qualifies for a weighted deduction of 200% as against 175% earlier.

A weighted deduction is available of one and one-fourth times any sum paid for scientific research to a domestic company, if such company:

- Has as its main object the scientific research and development;

- Is approved by the prescribed authority, in the prescribed manner; and
- Fulfils such other conditions as may be prescribed.

Hotels and Convention Centres

A five-year 100% tax holiday commencing from the initial year (subject to certain conditions) is provided in respect of profit derived from the business of hotels (two, three and four stars) and convention centres located in specified areas. This tax holiday would be available provided the construction is completed and operations are started during the period 1 April 2007 to 31 July 2010.

A five-year tax holiday is available in respect of profits derived from the business of new two star, three star and four starcategory hotels located in specified districts having a World Heritage Site. The hotel should start functioning between 1 April 2008 and 31 March 2013.

Hospitals

A five-year tax holiday is available in respect of profits derived from the business of operating and maintaining hospitals located anywhere in India (other than the excluded area), subject to the fulfilment of certain conditions. The hospital should start functioning between 1 April 2008 and 31 March 2013.

Chapter 6

Mergers and Acquisitions

Mergers and Acquisition (M&A)

India has experienced a sharp rise in M&A and outbound activity in recent years, owing to its dominant participation in the global economy. M&A activity in India is subject to the interplay of various tax and regulatory legislations, ranging from direct and indirect taxation, securities laws, company law, foreign exchange control regulations, competition law and stamp duty law.

Part I: Indian M&A

The Indian regulatory framework broadly facilitates the following modes of acquisition / reorganisation:

1. Share acquisition
2. Asset acquisition – assets (itemized sale) or business (slump sale)
3. Merger or amalgamation
4. Demerger or hive-off

1 Share Acquisition

1.1 Seller's Perspective

- Profit on Sale of Shares
  - Transfer of shares in Indian companies is taxable in India as capital gains;
  - The Indian tax authorities are currently seeking to tax the "indirect transfer" of underlying shares of an Indian company, through the transfer of shares of the overseas holding company, – the matter is pending before the courts in India.
- Repatriation of Profits
  - Repatriation can be made through dividend, repurchase (buy-back) of shares or capital reduction by the company;
  - Distribution of dividends attracts dividend distribution tax at 16.61% and is payable by the company paying the dividend. The dividend is not taxable in the hands of shareholders there is no withholding tax on dividend payments;
  - Companies distributing dividend are also required to comply with the transfer to reserve rules;
  - Repurchase (buy-back) of shares by a company is taxable as capital gains, subject to benefits under applicable Double Tax Avoidance Agreements (Treaty), if any;
  - Capital reduction – this requires the approval of the High Court.
- Taxable as deemed dividend to the extent of accumulated profits;
- Balance amount taxable as capital gains (similar to repurchase of shares).

1.2 Buyer's Perspective

- Acquisition Structure
  - Acquisition of a listed company's shares has to be compliant with the Takeover Code and Open Offer conditions to be considered, where the buyer proposes to acquire 15% or more in the target company;
  - Transfer of shares attracts stamp duty at 0.25% of the value of shares transferred and is generally borne by the buyer. However, no stamp duty is payable if the shares sought to be transferred are held in electronic or demat form.
- Funding Costs
  - Interest costs are generally not tax deductible in India, given that dividend income is exempt in the hands of the shareholders.
- Withholding Tax
  - Acquisition of shares of an Indian company from a non-resident attracts withholding tax provisions;

- Buyer (including non-residents) is required to withhold tax at applicable rates on payment / accrual of consideration payable to a non-resident;
- No withholding of tax is required for acquisition of shares from Indian residents;
- As mentioned above, in certain cases "indirect transfers" are also sought to be taxed in India by the Indian tax authorities – Indian withholding tax provisions are sought to be applied in such cases.

- Debt/ Equity Requirements
  - No prescribed debt-equity ratios / thin capitalisation rules under taxation law;
  - Debt / equity amounts are generally driven by commercial considerations.
- Preservation of Tax Losses
  - No impact on carry forward of tax losses on transfer of shares of a listed company;
  - In the case of other companies, transfer of shares / change in ownership beyond 49% disentitles the company from carrying forward prior years' tax losses from business;
  - No impact of transfer of shares on carry forward of unabsorbed depreciation allowance.

2 Asset / Business Acquisition

2.1 Seller's Perspective

- Sale of Assets (Itemised Sale)
  - Generally, the consideration for the transfer of assets is assigned either asset wise or for a class of assets and such transactions are classified as "Itemised Sales";
  - Computation of gains is made in respect of each asset and the same is taxable as short-term or long-term capital gains, depending on the period of holding:
    i. Self-generated intangible assets
    ii. Cost of acquisition of such intangible assets is generally taken as "Nil"
  - Entire amount of consideration would be taxable in the hands of the Seller;
  - Immovable assets – valuation adopted for stamp duty purposes to form taxable base, if such amount exceeds the consideration for the transfer;
  - Non-compete fees are deemed to be business income and are chargeable to tax at normal rates applicable to business income in the year of accrual.
- Slump Sale
  - Defined to mean transfer of undertaking for a lump-sum consideration, without values being assigned to individual assets and liabilities;
  - Capital gains = Consideration less "net worth";
  - Capital gains taxable as short-term or long-term capital gains, depending on period of holding/ existence of the undertaking;
  - No indexation benefit available in case of slump sale of undertaking;
  - Net worth = Book value of assets (Tax Written Down Value for tax depreciable assets to be considered) less liabilities transferred.

2.2 Buyer's Perspective

- Acquisition Structure
  - Generally, in an asset acquisition (not qualifying as a slump sale), the consideration for assets is generally mentioned in the transaction documents;
  - In case of slump sale, the lump sum consideration generally to be allocated to assets based on a valuation report. Buyer can claim depreciation on such value provided the assets qualify for depreciation;
  - The buyer is liable for stamp duty on the transfer of immovable property at a rate which varies from State to State;
  - Seller is liable to charge VAT/ sales tax on movable property at appropriate rates. Slump sale however, is typically not subject to VAT/ sales tax.

- Funding Costs
  - Interest on loan taken for the acquisition of assets is generally tax deductible. There are some exceptions to this rule.
- Acquisition Expenses
  - Acquisition expenses related to the purchase will be added to cost of assets;
  - Consequently, they would be eligible for depreciation allowance in the case of depreciable assets.
- Treatment of Goodwill and Intangibles
  - Goodwill arising from an asset acquisition is not allowed as a tax deduction, either through amortisation or depreciation;
  - Cost/ value of intangible assets (such as know-how, patents, copyrights, trademarks, franchises or any other business/ commercial rights of a similar nature) can be depreciated for tax purposes.

3. Amalgamations and De-mergers

- Transfer of capital assets attract capital gains tax, unless they are specifically exempt;
- However, certain specified reorganisation schemes, such as amalgamations or de-mergers, are exempt from levy of capital gains tax in the hands of the company as well as shareholders, subject to conditions.

3.1 Amalgamations

- Amalgamation refers to the merger of one or more companies into another company;
- Conditions required to be satisfied to claim tax exemption:
  - Transfer of all assets and liabilities
  - Shareholders holding at least 75% of shares (value) in amalgamating/ transferor companies to become shareholders in the amalgamated/ transferee company
- From a tax perspective, amalgamation is considered to be operative from the "Appointed Date" mentioned in the Scheme, though actual approval is obtained on an earlier or later date.

3.2 De-mergers

- De-merger refers to the transfer of an undertaking or a part thereof, through a scheme of arrangement;
- Conditions required to be satisfied to claim tax exemption:
  - All assets and liabilities pertaining to such undertaking are to be transferred
  - Consideration for demerger is settled though issue of shares to the shareholders of the de-merged company on a proportionate basis
  - Shareholders holding at least 75% of shares (value) in demerged companies become shareholders in the resulting company
- From a tax perspective, demerger is considered to be operative from the "Appointed Date" mentioned in the Scheme, though actual approval is obtained on an earlier or later date.

3.3 Amortisation of Amalgamation/ De-merger Expenses

- Amalgamation/ de-merger expenses are allowed to be amortised at 20% per annum over a five year period.

3.4 Carry Forward of Accumulated Loss and Unabsorbed Depreciation

- Amalgamation
  - Subject to certain conditions, accumulated tax loss or unabsorbed depreciation of an amalgamating company owning engaged in an industrial undertaking, ship, hotel, banking, operation of an aircraft business (restricted to public sector company) is eligible to be carried forward by the amalgamated company;
  - Specified conditions are laid down in relation to continuance of business, holding of assets, etc.;
  - Industrial undertakings include entities engaged in manufacture or processing of goods, manufacture of computer software, generation or distribution of electricity, telecommunications services, etc.

- De-merger
  - Accumulated loss or unabsorbed depreciation directly related to the undertaking demerged is transferrable;
  - If they are not directly relatable to the undertaking, then proportionate amounts are transferrable based on the ratio in which assets have been transferred;
  - There is no need to own an industrial undertaking, ship, hotel, etc. and no additional conditions imposed.

3.5 Other Matters

- Amalgamations and de-mergers normally attract stamp duty (potentially significant) at rates varying from State to State;
- Stock exchange (for listed companies), High Court and other regulatory clearances are required for amalgamations or de-mergers.

Part II: Outbound Investments

1. Regulation of Overseas Direct Investment

- Outbound investment from India for investing in a joint venture or wholly owned subsidiary abroad is allowed under automatic route for bonafide business purposes;
- Investment of an amount upto 400% of the net worth of the Indian investor can be made.

2. Tax on Overseas Investments

- Considering the high tax regime of dividend and capital gains in India coupled with nascent foreign tax credit regulations, it becomes imperative that investments are structured to optimize tax efficiencies;
- Essential tax considerations for the Indian outbound investor are capital gains mitigation, foreign tax reduction and reduction of Indian tax on repatriation of funds to India;
- India currently has no controlled foreign corporation (CFC) rules, so there will be no India tax on foreign profits that remain unremitted from offshore subsidiaries;
- However, the Government has proposed to introduce the CFC Regulations in the proposed Direct Tax Code.

3. Outbound Structuring

- It is important to have a robust Outbound structure which is flexible, optimises global tax cost, has ability to bring in new investors and repatriate/ deploy funds in a tax efficient way.

Annexure 1

Special Economic Zones in India

"The objectives of SEZs include making available goods and services free of taxes and duties supported by integrated infrastructure for export production, quick approval mechanisms, and a package of incentives to attract foreign & domestic investments for promoting exports."

Ministry of Commerce & Industry, Government of India

An SEZ is a specifically delineated, duty-free area notified as such by the Ministry of Commerce under the Special Economic Zones Act, 2005 (SEZ Act); the zone is considered to be outside the customs territory of India for the purposes of carrying out authorised activities.

The SEZ Act, 2005 and SEZ Rules, 2006, which came into force with effect from 10 February 2006, govern the development of SEZs. The Act provides the umbrella legal framework for all important legal and regulatory aspects of SEZ development as well as for units operating in these SEZs.

Scope of SEZ Act

- Establishment of SEZs and units;
- Fiscal regime for developers and units;
- Requirements, obligations, entitlements;
- Single window clearance mechanism;
- Establishment of administrative authority for SEZ set up by the government of India;
- Special courts and single enforcement agency to ensure speedy trials.

Development of SEZs

SEZs are notified by the Ministry of Commerce and can be set up by private developers, by central/state governments, or jointly by any two or more of the above on contiguous, vacant land.

Fiscal Benefits to the Developer

Income Tax Incentives

- 100% tax deduction for ten years out of 15 years beginning with the year in which the SEZ is notified by the government;
- Exemption from Dividend Distribution Tax has been discontinued with effect from 1 June 2011;
- Exemption from Minimum Alternate Tax has been discontinued from FY 2011-12; accordingly, SEZ developers will henceforth be required to pay MAT.

Indirect Tax Incentives

- Exemption from customs duty on import of capital goods/raw material into the SEZ for authorized operations;
- Exemption from excise duty on local procurement of capital goods/raw materials;
- Exemption from CST on inter-state purchases subject to submission of statutory declaration Form I;
- Exemption from payment of service tax on the input services wholly consumed in the SEZ unit for authorised operations and refund mechanism for service tax paid wholly or partially consumed outside the SEZ for authorised operations.

In addition, goods sold from DTA units to the SEZ unit would attain the status of physical exports. In light of this, the sale of goods to a SEZ unit will be regarded as exports and the DTA unit will be eligible for export benefits;

- Exemption from ADC in lieu of sales tax/VAT on goods manufactured within the SEZ unit and sold to a DTA on the condition that such goods are subject to sales tax/VAT;
- Exemption from VAT as per VAT legislation;
- Exemption from payment of stamp duty as per state government policy.

Who Should Set up a Unit in SEZ?

Export oriented manufacturers and service providers (including Information Technology (IT) and Information Technology Enabled Services (ITES) providers, BPOs, contract manufacturers, etc.) have huge growth potential in Indian SEZs. IT hardware and software and telecom equipment suppliers can also set up units in SEZs for supply to the domestic market.

FDI Policy

100% FDI is permitted under the automatic route for SEZ development. For units in SEZs, the FDI Policy of the government of India will apply.

No Minimum Export Obligation

- SEZ units to be net foreign exchange earners at the end of five years calculated cumulatively;
- No limit on DTA sales provided full import duty is paid;
- Supply of IT hardware and software and telecom equipment to domestic markets, as well as supply of goods and services to other SEZ/EOU/STPI units, are counted towards calculation of foreign exchange earnings.

Fiscal Benefits to a SEZ Unit

- 15 year income-tax deduction on export profits beginning with the year in which the unit begins to manufacture, produce or provide services – 100% for the initial five years, 50% for the next five years and up to 50% for the remaining five years, equivalent to profits ploughed back for re-investment;
- Tax deduction only for physical export;
- Exemption from MAT has been discontinued with effect from FY 2011-12;accordingly, SEZ units will henceforth be required to pay MAT;
- Same indirect tax benefits as the SEZ developer;
- Exemption from electricity duty;
- Exemption from payment of stamp duty as per state government policy.

Liberal Exchange Controls

- 100% 100% export earnings maintainable in foreign exchange in Special Foreign Currency Account – minimal restrictions on business payments outside India;
- Unlimited credit period for export realisation;
- Branches of foreign companies in SEZ are eligible to undertake manufacturing activities.

Offshore Banking Units

An Offshore Banking Unit is a branch of a bank in India located in the SEZ with the permission of RBI. Offshore Banking Units provide cheaper finance at international rates to units in SEZs. Banks setting up Offshore Banking Units in SEZs are entitled to tax deduction (beginning with the year in which they obtain requisite approvals) of 100% for the first five years and 50% for the next five years. A similar deduction is available to units of an International Financial Services Centre.

Annexure 2

Tax Rates under Double Taxation Avoidance Agreements

Name of the Country	Interest	Dividend (Refer to note a)	Royalty (Refer to note m)	Fee for Technical Services (Refer to note m)
Austria	10%	10%	10%	10%
Armenia	10%	10%	10%	10%
Australia	15%	15%	10% (b); 15% in other cases	No specific provision (e). However, it can be covered under Royalty
Bangladesh	10%	10% (c); 15% in other cases	10%	No specific provision (e)
Belarus	10%	10% (i); 15% in other cases	15%	15%
Belgium	10%(k); 15% in other cases	15%	10%(f)	10%(f)
Botswana	10%	7.5% (i); in other cases 10%	10%	10%
Brazil	15%	15%	25% if royalty arises from trademarks; 15% in other cases	No specific provision (e)
Bulgaria	15%	15%	15% if it relates to copyrights of literary, artistic or scientific work; 20% in other cases	20%

Name of the Country	Interest	Dividend (Refer to note a)	Royalty (Refer to note m)	Fee for Technical Services (Refer to note m)
Canada	15%	15% (c); in other cases 25%]	10% (b); in other cases 15%	10% (b); in other cases 15%
China	10%	10%	10%	10%
Czech Republic	10%	10%	10%	10%
Cyprus	10%	10% (c); in other cases 15%	15% (including fee for included services)	10% (for technical fees)
Denmark	10% (k); 15% in other cases	15% (i); 25% in other cases	20%	20%
Ethiopia (refer note u)	10%	7.5%	10%	10%
Finland Refer to note (p)	10%	15% (p)	10% (b); in other cases 15%	10% (b); in other cases 15%
France	10%(f)	10% (f)	10% (f)	10% (f)
Germany	10%	10%	10%	10%
Greece	21.115% (i)	Exempt	10.558% (m)	No specific provision (e)
Hungary	10% (f)	10% (f)	10% (f)	10% (f)
Iceland	10%	10%	10%	10%
Indonesia	10%	10% (i); 15% in other cases	15%	No specific provision (e)
Ireland	10%	10%	10%	10%
Israel	10%	10%	10%	10%
Italy Refer to note (o)	15%	15% (c); in other cases 25%	20%	20%
Japan	10%	10%	10%	10%
Jordan	10%	10%	20%	20%
Kazakhstan	10%	10%	10%	10%

Name of the Country	Interest	Dividend (Refer to note a)	Royalty (Refer to note m)	Fee for Technical Services (Refer to note m)
Kenya	15%	15%	20%	17.5% (for managerial, technical, professional or consultancy fees)
Kuwait	10%	10%	10%	10%
Republic of Korea	10% (n); 15% in other cases	15% (d); 20% in other cases	15%	15%
Kyrgyz Republic	10%	10%	15%	15%
Libya Arab Jamahriya	21.115% (i)	Exempt	10.558% (m)	No specific provision (e)
Grand Duchy of Luxembourg	10%	10%	10%	10%
Malaysia	10%	10%	10%	10%
Malta	10%	10% (i); in other cases 15%	15% including fee for included services	10% on fee for technical, managerial and consultancy services
Mauritius	21.115% (i)	5% (c); in other cases 15%	15%	No specific provision (e)
Mongolia	15%	15%	15%	15%
Montenegro	10%	5% (i); in other cases 15%	10%	10%
Morocco	10%	10%	10%	10%
Mozambique (refer note t)	10%	7.5%	10%	10%

Name of the Country	Interest	Dividend (Refer to note a)	Royalty (Refer to note m)	Fee for Technical Services (Refer to note m)
Myanmar	10%	5%	10%	No specific provision (e)
Namibia	10%	10%	10%	10%
Nepal	10% (n); in other cases 15%	10% (c); in other cases 15%	15%	No specific provision (e)
Netherlands	10% (f)	10% (f)	10% (f)	10% (f)
New Zealand	10%	15%	10%	10%
Norway	15%	15% (i); in other cases 25%	10% (f)	10% (f)
Oman	10%	10% (c); in other cases 12.5%	15%	15%
Philippines	10% (n); in other cases 15%	15% (c); in other cases 20%	15%	No specific provision (e)
Poland	15%	15%	22.50%	22.50%
Qatar	10%	5% (c); in other cases 10%	10%	10%
Portugal	10%	10% (i); 15% in other cases	10% including fee for included services	No specific provision. However it can be covered under Royalty
Romania	15%	15% (i); in other cases 20%	22.50%	22.50%
Russian Federation	10%	10%	10%	10%
Saudi Arabia	10%	5%	10%	No specific provision (e)
Serbia	10%	5% (i), in other cases 15%	10%	10%

Name of the Country	Interest	Dividend (Refer to note a)	Royalty (Refer to note m)	Fee for Technical Services (Refer to note m)
Singapore	10%(k);in other cases 15%	10%(i); in other cases 15%	10%	10%
South Africa	10%	10%	10%	10%
Spain	15%	15%	20%(f), 10% (f)(b)	20%(f)
Sri Lanka	10%	15%	10%	No specific provision (e)
Sweden	10%(f)	10%(f)	10%(f)	10%(f)
Sudan	10%	10%	10%	10%
Slovenia	10%	5%(c); in other cases 15%	10%	10%
Switzerland	10%	10%	10%	10%
Syrian Arab Republic	10%	5% (c), in other cases 10%	10%	No specific provision, (e)
Tajikistan	10%	5% (i), in other cases 10%	10%	No specific provision, (e)
Tanzania (refer note q)	12.5%	10%(c); in other cases 15%	20%	20% On management & professional fees
Thailand	10%(n),in other cases 25%	15%(c)(h); 20%(i) or (h)	15%	No specific provision (e)
Trinidad and Tobago	10%	10%	10%	10%
Turkey	10%(k); in other cases 15%	15%	15%	15%
Turkmenistan	10%	10%	10%	10%
Uganda	10%	10%	10%	10%
Ukraine	10%	10%(i); in other cases 15%	10%	10%

Name of the Country	Interest	Dividend (Refer to note a)	Royalty (Refer to note m)	Fee for Technical Services (Refer to note m)
United Arab Emirates	5%(k); in other cases 12.5%	10%	10%	No specific provision (e)
United Arab Republic	21.115%(l)	Exempt	10.558% (m)	No specific provision (e)
United Kingdom	10%(n); in other cases 15%	15%	10%(b); in other cases 15%	10%(b); in other cases 15%
United States of America	10%(k); in other cases 15%	15%(c); in other cases 25%	10%(b); in other cases 15%	10%(b); in other cases 15%
United Mexican States (refer note r)	10%	10%	10%	10%
Uzbekistan	15%	15%	15%	15%
Vietnam	10%	10%	10%	10%
Zambia	10%	5% j); in other cases 15%	10%	10% on managerial & Consultancy fees

Notes:

a. The treaty tax rates on dividends are not relevant in case of payment of a dividend by an Indian company since under the current Indian tax legislation, dividend distribution by such companies is exempt from income tax in the hands of recipient

b. For use of industrial, scientific or commercial equipment

c. If the beneficial owner is a company which holds at least 10% of the capital of the company paying the dividend

d. If the beneficial owner is a company which owns 20% of capital of the company paying the dividend

e. In the absence of a specific provision, it may be treated as business profits under respective treaties

f. The "Most Favoured Nation" clause is applicable. The Protocol to the Treaty limits the scope and rate of taxation to that specified in similar articles in Treaties signed subsequently by India with other OECD nations

g. In most of the treaties the interest attributable to financing of exports and imports and loans granted by specified institutions is subject to Nil or lower withholding tax rates

h. The company paying the dividend is engaged in an industrial undertaking

i. If the beneficial owner is a company which holds at least 25% of the shares of the company paying the dividend

j. If the recipient is a company owning at least 25% of capital during the period of six months before date of payment

k. If paid on a loan granted by a bank / financial institution

l. The tax rate under domestic tax laws is 20%, plus surcharge @ 2.5%; education cess of 3% is levied, the effective tax rate being 21.115%

m.The prescribed tax rate for Royalty and Fees for Technical Services, under domestic tax laws is 10% (plus surcharge @ 2.5% and education cess of 3%, the effective tax rate being 10.558%). The rate would apply for payments under the agreement entered on or after 1 June 2005

n. If interest is received by a bank or financial institution

o. The protocol amending the DTAA with Italy (January 2006) stipulates the rate of 10% for Dividend, Interest, Royalty and Fee for Technical Services

p. Revised DTAA with Finland (January 2010) stipulates the rate of 10% for Dividend, Royalty and Fees for Technical Services. The Revised DTAA comes into force on 1 April 2011

q. As per a Government Press Release, under an agreement signed on 27 May, 2011 the maximum rate of tax to be charged in the country of source will not exceed a two-tier 5% or 10% in the case of dividends and 10% in the case of interest and royalties. This is yet to be notified

r. The agreement comes into force with effect from 1 April, 2011

s. The South Asian Association for Regional Cooperation ("SAARC") Member States comprising Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka had entered into a SAARC agreement for the avoidance of double taxation and mutual administrative assistance in tax matters which was signed in Dhaka, Bangladesh on 13 November, 2005. The CBDT has issued a Notification No. 3/2011-FTD-II [F. NO.500/96/97-FTD-II], dated 10 January, 2011, which directs that all the provisions of the SAARC limited multilateral agreements on avoidance of double taxation and mutual administrative assistance in tax matters ("SAARC Agreement") shall be effective in India with effect from the 1 April, 2011

t. The agreement was notified on 31 May, 2011

u. As per a government Press Release an agreement was signed on 25 May, 2011, but it is yet to be notified.

Annexure 3

Direct Tax Code

On 12 August 2009, the Indian Government released the draft DTC for public debate. The objective is to moderate the tax rates and simplify tax laws; all direct taxes including wealth tax and income tax will be brought under one code. Public and stakeholder feedback on the proposals outlined in those documents were analysed by the Government and suggestions for amendments received from public, business associations and other bodies were taken into account. A Revised Discussion Paper addressing the major issues was released in June 2010. Further feedbacks was received on the Revised Discussion Paper. The Direct Taxes Code Bill, 2010 tabled in the Parliament on 30 August 2010 is an outcome of this process.

A summary of significant proposals of the DTC follows:

Commencement

The DTC is proposed to be effective from 1 April 2012 and not from 1 April 2011, as had been intended earlier. This gives time to companies to understand the provisions, engage in a dialogue with the Indian government and, more importantly, restructure their operations as they switch over to taxation under the DTC. Also, this gives time to the government to adapt its systems to accept and audit additional new compliance requirements imposed on the tax payers.

Tax Rates

- Tax rates for individuals are proposed to be revised as follows :

Income slab (INR)	New Income slab (INR)	Tax Rate
Upto 180,000*	Upto 200,000**	Nil
180,001 – 500,000	200,001– 500,000	10%
500,001 – 800,000	500,001 – 1,000,000	20%
Above 800,000	Above 1,000,000	30%

**The tax slabs are with reference to the Income – taxAct, 1961 forAY 2012-13*

*** In the case of resident senior citizens Rs 200,000 may be read as Rs 250,000 and Rs 200,001 as Rs 250,001. It is proposed to eliminate a separate range for female taxpayers*

- Partnership firms, associations of persons and bodies of individuals will be taxed separately as an “unincorporated body” at a maximum marginal rate of 30% without any threshold exemption limit;
- Tax rate for companies (both domestic and foreign) is proposed at 30%;
- Domestic companies will continue to be liable to dividend distribution tax at 15%;
- Foreign companies will be subject to branch profits tax of 15%.

Minimum Alternative Tax (MAT)

- MAT is proposed to be levied on book profits at 20%;
- Further, MAT credit will be available for set-off against normal tax liability up to 15 consecutive financial years immediately succeeding the year in which the credit becomes available.

Wealth Tax

- The DTC proposes to levy wealth tax at 1% of net wealth over INR 10 million. All taxpayers except non-profit organizations are liable to wealth tax. New categories of assets introduced for levying wealth tax are archaeological collections, drawings, paintings, sculptures or any other work of art, watch having value in excess of INR 50,000 and equity or preference shares held in Controlled Foreign Companies(CFC).

International Taxation

- Transportation charges paid to a non-resident by a resident are taxable as also transportation charges paid by non-residents to non-residents if they are in respect of carriage to or from a place in India;
- Income arising from transfer of shares of a foreign company sought to be taxed in India if assets in India (held directly or indirectly by the company) represent atleast 50% of the fair market value of all the assets owned by the foreign company. The 50% test is to be applied at any time during the 12 months prior to transfer;
- Presumptive taxation scheme continued with no change in the rates except in the case of non- residents engaged (a) in the business of providing services / supplying plant and machinery in connection with prospecting for, or extraction or production of, mineral oil or natural gas which has been increased from 10% to 14%, (b) in the case of business of operation of ships, the rate has been increased from 7.5% to 10% and (c) in case of business of operation of aircrafts, the rate has been increased from 5% to 7%;
- Definition of royalty is expanded and withholding tax rate is increased from 10% to 20%, both for royalty and fees for technical services;
- Head Office Expense - Head office expenditure would be allowable to the extent of 0.5% of total turnover or gross receipts of business in India.

Residency rules

Companies having a place of effective management in India at any time in the year will be considered as resident in India

The Place of effective management is defined to mean:

- place where Board of Directors (BoD) or Executive Directors, as the case may be make their decisions, or
- in a case where the BoD routinely approve commercial and strategic decisions made by the executive directors or officers, the place where such executive directors or officers perform their functions.

Separately, CFC provisions are proposed to be introduced as an anti-avoidance measure, providing the following:

- CFC provisions attracted when a foreign company is controlled by resident tax payers. Control has been defined where one or more persons resident in India, individually or collectively, directly or indirectly, hold shares carrying not less than 50% of the voting power or capital of the company. An additional condition is that the entity is a resident of a country with lower level of taxation, i.e. the amount of tax payable in foreign country is less than 50% of the corresponding tax payable under the DTC;
- The net profit earned by the CFC will be attributed (and not only the passive income) to the resident tax payer based on the percentage holding and for the period such percentages are held;

- CFC provisions not triggered in case the foreign company is listed on a stock exchange or is engaged in "active trade or business" (subject to certain conditions) or specified income does not exceed INR 2.5 million;
- Where 50% or more income of an offshore entity is derived from sale of goods/services to controlled corporations, it will not be considered as having engaged in active trade or business;
- Underlying foreign tax credit mechanism not provided.

Treaty provisions vis-à-vis domestic tax law

The provisions of the DTC or the Double Tax Avoidance Agreement, whichever is more beneficial to the taxpayer shall apply, except in the following circumstances:

- When General Anti - Avoidance (GAAR) provisions are invoked;
- When CFC provisions are invoked;
- When branch profit tax is levied.

Branch Profit Tax

The concept of branch profits tax introduced. Profits of Indian branches of foreign companies would be additionally subjected to branch profits tax at 15%. Branch profits tax to be levied on income attributable directly or indirectly to a Permanent Establishment (PE) or immovable property situated in India. PE is defined in the same way as in the treaties and includes one day Service PE, (substantial) equipment PE and insurance agent PE.

Applicable Tax rates for non-residents

- Royalty and Fee for technical services rates proposed to be increased to 20% on gross basis;
- Capital gains taxable at 30%;
- Corporate tax rate at 30%.

Definitions of key terms to be enlarged

- Fees for Technical Services to include consideration fordevelopment and transfer of design, drawing, plan or software or similar services;
- Royalty to include the consideration for use / right to use of transmission by satellite, cable, optic fibre, use or right to use ship or aircraft and live coverage of any event;

- Income would be deemed to accrue in India regardless of whether payments are made outside India, or the services are being rendered outside India, or income has otherwise not accrued in India.

General Anti-Avoidance Rule

- The DTC contains the provisions of GAAR wherein CIT has been empowered to declare an arrangement as impermissible if it has been entered into with the objective of obtaining a tax benefit and lacks commercial substance. The arrangement would be presumed to be for the purpose of availing tax benefits even if the main purpose of a part or step of the arrangement was to avail tax benefits;
- Any arrangement would be presumed to be for availing tax benefits unless the tax payer demonstrates that availing tax benefits was not the main objective of the arrangement;
- CIT to determine the tax consequences on invoking GAAR. Order of CIT will be forwarded to the tax payer and to the CIT of the other party to the arrangement; such CIT to proceed against other party to apply GAAR;
- The provisions of GAAR to apply subject to such conditions and manner as may be prescribed;
- The forum of DRP available in cases where in GAAR provisions are invoked;
- GAAR to override provisions of Double Taxation Avoidance Agreements.

Domestic Taxation

Corporate Tax

DTC proposes the corporate tax rate to be 30% and also provides for unlimited carry forward of business losses. In an attempt to rationalise and simplify tax computation, the DTC proposes amendment in the basis of computation of business income from the current "business profits with specified adjustments" to an "income expense model" prevalent in certain developed and other Asean countries. Largely, DTC also provides a status quo on DDT levy at 15% on the dividend declared or distributed.

Computation

- Business income computed based on the income-expense model:

Gross Earnings XXX

Less: Business Expenditure

Operating Expenditure (includes all expenditure laid out for the purposes of the business) XXX

Permitted Finance Charges (includes interest charges, finance charges, etc.) XXX

Capital Allowances (includes depreciation, deferred revenue expenditure, etc.) XXX

Taxable Income from Business XXX

- Business Assets to be distinguished from Investment Assets; Business Assets further classified as Business Trading Assets and Business Capital Assets;
- 200% Weighted deduction for in-house scientific R&D expenditure extended to all industries;
- Remaining value of block of business capital assets where all assets cease to exist will continue to be eligible for depreciation;
- In the case of a finance lease, the lessee would be eligible to claim capital allowance.

Dividend Distribution Tax

- Status quo on DDT rate at 15%;
- DDT exemption not available for SEZ developer.

Exemptions, Deductions and New Schemes

- Profit-based tax incentives are sought to be discontinued and expenditure/ investment-based incentive scheme introduced and will apply to the following businesses:
  - Generation, transmission or distribution of power;
  - Developing or operating and maintaining Infrastructure facility (as defined);
  - Operating and maintaining a hospital in specified areas;
  - Processing, preservation and packaging of fruits and vegetables;
  - Laying and operating cross country natural gas or crude or petroleum, pipeline distribution network including storage facilities;
  - Setting-up and operating a cold chain facility;
  - Setting-up and operating agricultural warehouse facility;
  - Operating anywhere in India new hotel of two star or above category on or after 1 April 2010;
  - Operating anywhere in India new hospital with at least hundred beds on or after 1 April 2010;
  - Developing and building a housing project under notified schemes of slum re- development or rehabilitation commencing on or after 1 April 2010;
  - Exploration and production of mineral oil or natural gas;
  - Developing a SEZ and to a unit established in a SEZ.
- Export based incentives such as section 10A, 10AA, 10B, 10BA to be eliminated
  - Area / profit-based incentives to be discontinued without affecting the tax payers currently enjoying such incentives, which will be grandfathered;
  - Tax holiday for infrastructure companies grandfathered for projects eligible until 31 March, 2012;
  - Tax holiday for SEZ developers grandfathered for projects notified until 31 March, 2012;
  - Tax benefits allowed to SEZ units starting operations before 31 March, 2014.

Capital Gains

- Paradigm shift in taxation of capital gains is proposed under the DTC. All capital gains would be considered as income from ordinary sources and be taxable at normal rates of tax, removing the benefits of lower rates. However, fair market value substitution date is shifted to 1 April, 2000. Cost of acquisition is deemed to be nil for all self generated assets and where cost of assets cannot be determined;
- Transfer of business capital assets will be taxed under the head business income;
- STT to continue;
- No capital gains tax on sale of equity shares of a company or unit of an equity oriented fund held for more than one year if STT is paid on the transfer;
- Capital gains tax payable only on 50% of the gains in case equity shares of a company or unit of an equity oriented fund is held upto one year if STT is paid on the transfer;
- Cost of acquisition of assets acquired on retirement from unincorporated body prescribed.

Mergers and Acquisitions

- Full value of consideration in case of transfer of land and building has been specified to be the stamp duty value in all cases, as against the Income-tax Act where a revenue officer could refer the matter to a Valuation Officer to determine the value of the land and building;
- Under the Income-tax Act, it is provided that exemption on holding – subsidiary transfers shall be withdrawn and exempted gain would be taxed in the year of transfer of original asset if the conditions of exemption were violated. The DTC seeks to tax such exempted gain in the year in which the conditions are violated. Hence, the rigors of revising past years returns has been done away with;
- The DTC narrows the definition of business reorganisation to include only reorganisation between "residents";
- Pursuant to the demerger, the DTC specifically provides for issue of equity shares to shareholders of the demerged company, as against the Income-tax Act where the nature of shares was not provided;
- The DTC provides for a liberalized regime for carry forward of loss, as compared to the Income-tax Act ;
- The DTC provides for carry forward of losses of the demerged unit upon satisfaction of the business continuity test. The Income-tax Act does not contain such a condition;
- In case of succession of a sole proprietorship, or a partnership firm, by a company, the DTC provides for carry forward of losses, subject to fulfilment of prescribed conditions. This was not facilitated under the Income-tax Act;
- New provisions have been introduced in the DTC which expressly provide for taxation of income for payments received in case of retirement of a participant, being a member of an unincorporated body.

Slump sale

- Profit on slump sale will be liable to tax under the head Capital Gains.

Transfer Pricing

- Introduction of Advance Pricing Arrangements (APA)to provide certainty of tax liability with regard to international transactions;
- Safe Harbour provisions have been introduced. However, detailed rules are yet to be prescribed;
- Definition of Associated Enterprise broadened to include enterprises based on any specific or distinct location.

Advance Pricing Agreement (APA)

- The DTC seeks to introduce the concept of APA;
- APA is an agreement between the taxpayer and the tax authorities for the upfront determination of the arm's length pricing / pricing methodology of an international transaction;
- The features of an APA will be as follows
  - The methodologies for the determination of the arm's length price under an APA may involve the use of any transfer pricing methods(including the specified methods), subject to necessary / expedient adjustments made by the Board;
  - APA validity shall not exceed five consecutive years; and
  - APA not to be binding in case of change in the law on the basis of which it was entered into.

Individual tax - Residency rules and taxability

The separate category of resident but not ordinarily resident is proposed to be done away with. Resident individuals would enjoy exemption on income sourced outside India for 2 consecutive financial years i.e. in the financial year the individual becomes a resident and in the immediately succeeding financial year if the individual was a non resident for nine years immediately preceding the financial year in which he becomes a resident.

FIIs

- Income earned by FIIs to be taxed as capital gains;
- Payments made to FIIs as a consideration for sale of listed securities shall not be subject to withholding tax.

Mutual Funds

- Distribution Tax of 5% to be levied on distribution of income by an Equity Oriented Mutual Fund. Such income shall be exempt in the hands of the investors;
- Income distributed by funds other than Equity Oriented Mutual Fund will be taxable in the hands of the investors and not subject to levy of distribution tax.

Banking companies

- The deduction for amounts credited to provision for bad and doubtful debts account shall be restricted to 1% of aggregate average advances computed in the prescribed manner, subject to fulfilment of prescribed conditions.

Insurance companies

- Profits of life insurance business shall be the profits determined in shareholders' account (subject to certain specified adjustments) and taxable at 30% (as against 12.5% earlier);
- Profits of other insurance business shall be the profits disclosed in annual accounts, subject to certain prescribed adjustments;
- Insurance/reinsurance premium received by a non-resident entity for covering risk in India shall be taxable at the rate of 20%;
- 5% tax rate has been proposed on the amount of income distributed by life insurance company to the policyholders of an 'approved equity oriented life insurance scheme'. This tax seems to be targeted towards ULIP products.

Trust Taxation

- Trust taxation provisions have been simplified. Differential and complex tax regime for determinate and in-determinate trusts is proposed to be removed;
- Provisions relating to taxation of business income of trust at maximum marginal rate have been dropped.

Venture Capital Funds (VCF) / Venture Capital Company (VCC)

- Code retains the existing tax regime applicable to VCF / VCC i.e. only in respect of investments of VCF / VCC in the venture capital undertaking. Venture capital undertaking is permitted to carry on business in nine specified sectors as well as in any other business as may be prescribed later;
- Income of VCF / VCC would be exempt and taxable in the hands of the investor in the VCF / VCC in the same manner on receipt basis.

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