Doing Business in INDIA

JC BHALLA & CO.

Preface

This guide has been prepared by JC Bhalla & Co. It is designed to provide information on number of subjects, important to those considering investing or doing business in India.

Doing Business in India has been designed for the information of readers. Whilst every effort has been made to ensure accuracy, information contained in this guide may not be comprehensive and recipients should not act upon it without seeking professional advice. Facts and figures as presented are correct at the time of writing.

Up-to-date advice and general assistance on Indian matters can be obtained from JC Bhalla & Co.; contact details can be found at the end of this guide.

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1. Fact Sheet

Introduction

India, a South Asian nation, is the seventh-largest country by area, the second-most populous country with over 1.33 billion people, and the most populous democracy in the world. India boasts of an immensely rich cultural heritage including numerous languages, traditions and people. The country holds its uniqueness in its diversity and hence has adapted itself to international changes with poise and comfort. While the economy has welcomed international companies to invest in it with open arms since liberalisation in 1990s, Indians have been prudent and pro-active in adopting global approach and skills. Indian villagers proudly take up farming, advanced agriculture and unique handicrafts as their profession on one hand while modern industries and professional services sectors are coming up in a big way on the other.

Thus, the country is attracting many global majors for strategic investments owing to the presence of vast range of industries, investment avenues and a supportive government. Huge population, mostly comprising the youth, is a strong driver for demand and an ample source of manpower.

Natural Resources: Coal (fourth-largest reserves in the world), iron ore, manganese, mica, bauxite, rare earth elements, titanium ore, chromite, natural gas, diamonds, petroleum, limestone, arable land.

Political Profile

Political System and Government:

The world’s largest democracy implemented its Constitution in 1950 that provided for a parliamentary system of Government with a bicameral parliament and three independent branches: the executive, the legislature and the judiciary. The country has a federal structure with elected governments in States.

Administrative Divisions: 29 States and 7 Union Territories

Constitution: The Constitution of India came into force on January 26, 1950

Executive Branch: The President of India is the Head of State, while the Prime Minister is the Head of the government and runs office with the support of the Council of Ministers who forms the Cabinet.

Legislative Branch: The Federal Legislature comprises of the Lok Sabha (House of the People) and the RajyaSabha (Council of States) forming both the Houses of the Parliament.

Judicial Branch: The Supreme Court of India is the apex body of the Indian legal system, followed by other High Courts and subordinate Courts.

Chief of State: President, Mr Pranab Mukherjee (since July 25, 2012)

Head of Government: Prime Minister, Mr Narendra Modi (since May 26, 2014)

Demographic profile

Population: 1,326,801,000

Population Growth Rate: 1.58 per cent (June 2015)

Religions: Hinduism, Islam, Christianity, Sikhism, Buddhism, Jainism

Languages: Hindi, English and at least 16 other official languages

Economic Profile

Indian Economy

According to The World Bank, the Indian economy will likely grow at 7.6 per cent in 2016-17, followed by further acceleration to 7.7 per cent in 2017-18 and 7.8 per cent in 2018-19.

Value of Exports: India’s exports stood at US$ 21.68 billion in July 2016

Export Partners: US, Germany, UAE, China, Japan, Thailand, Indonesia and European Union. India is also tapping newer markets in Africa and Latin America.

Currency (code): Indian Rupee (INR)

Fiscal Year: April 01 – March 31

Cumulative FDI Equity Inflows: US$ 288.513 billion (April 2000 to March 2016)

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2. Indian Corporate Tax at a Glance

Domestic Company Income Tax Rate (%)	30 (a)
Capital Gains Tax Rate (%)	20 (a)(b)
Branch Tax Rate (%)	40 (a)(c)
Withholding Tax (%)	
Dividends	10
Interest	
Paid to Domestic Companies	10 (d)
Paid to Foreign Companies	20 (a)(d)
Royalties from Patents. Know-how, etc.	10(a)(d)(e)
Technical Services Fees	10 (a)(d)(e)
Branch Remittance Tax	0
Net Operating Losses (Years)	
Carry back	0
Carry forward	8(f)

(a) The rates are subject to an additional levy consisting of a surcharge and a cess. They are increased by the following surcharges on such taxes:

- Domestic companies with net income exceeding INR100 million: 12%
- Foreign companies with net income exceeding INR 100 million: 5%
- Domestic companies with net income exceeding INR 10 million: *7%*
- Foreign companies with net income exceeding INR10 million: 2%

No surcharge is payable if the net income does not exceed INR10 million. The tax payable (inclusive of the surcharge, as applicable) is further increased by a cess levied at 3% of the tax payable. The withholding tax rates are increased by a surcharge for payments exceeding INR 10 million made to foreign companies and a cess (see above).

(b) See Section 3.

(c) For exceptions to this basic rate, see Section 3.

(d) A Permanent Account Number (PAN) is a unique identity number assigned to a taxpayer in India on registration with the India tax authorities. If an income recipient fails to furnish its PAN, tax must be withheld at the higher of the rate specified in the relevant provision of the Income Tax Act and 20%.

(e) The 10% rate (plus the 2% or 5% surcharge, as applicable, and the 3% cess) applies to royalties and technical services fees paid to foreign companies by Indian enterprises. However, if the royalties or technical services fees paid under the agreement are effectively connected to a permanent establishment or fixed place of the nonresident recipient in India, the payments are taxed on a net income basis at a rate of 40% (plus the 2%or 5% surcharge, as applicable, and the 3% cess).

(f) Unabsorbed depreciation may be carried forward indefinitely to offset taxable profits in subsequent years.

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3. Taxes on Corporate Income and Gains

Corporate Income Tax. A domestic company is defined for tax purposes as a company incorporated in India. The tax rates in India are specified with reference to a domestic company.

A company resident in India is subject to tax on its worldwide income, unless the income is specifically exempt. A company not resident in India is subject to Indian tax on Indian-source income and on income received in India. Depending on the circumstances, certain income may be deemed to be Indian-source income.

Companies incorporated in India are resident in India for tax purposes, as are companies incorporated outside India, if their place of effective management in that year is in India. As a result, if the place of effective management of a foreign company is in India, it is subject to tax in India on its worldwide income.

Rates of Corporate Tax. Domestic companies are subject to tax at a basic rate of 30%. Where the total turnover or gross receipts in the previous year 2015-16 does not exceed Rs.50 crores, such domestic company will be subject to tax at a basic rate of 25%.In addition, a 7% or 12% surcharge (for details regarding the surcharge, see footnote [a] in Section A) and a 3% cess are imposed on the income tax of such companies. Long-term capital gains are taxed at special rates (see *Capital gains).*

For foreign companies, the net income is taxed at 40% plus the 2% or 5% surcharge, as applicable, and the 3% cess. A rate of 10% plus the 2% or 5% surcharge and the 3% cess applies to royalties and technical services fees paid to foreign companies if the royalty or technical services fees agreement is approved by the central government or if it is in accordance with the Industrial Policy.

Minimum Alternate Tax. The minimum alternate tax (MAT) applies to a company if the tax payable by the company on its total income, as computed under the Income Tax Act is less than 18.5% of its book profit. It is levied at a rate of 18.5% of book profit, plus applicable surcharge and cess (the surcharge, as applicable, is imposed at a rate of 7% or 12% for domestic companies and 2% or 5% for foreign companies, and the cess is imposed at a rate of 3%). MAT is levied on companies only and does not apply to firms or other persons, which are separately subject to an alternative minimum tax of 18.5% (plus applicable surcharge and cess). In computing book profit for MAT purposes, certain positive and negative adjustments must be made to the net profit shown in the books of account.

MAT paid by companies can be carried forward and set off against income tax payable in subsequent years under the normal provisions of the Income Tax Act for a period of 15 years. The maximum amount that can be set off against regular income tax is equal to the difference between the tax payable on the total income as computed under the Income Tax Act and the tax that would have been payable under the MAT provisions for that year. Further, MAT credit will not be allowed to be carried forward to the extent that the amount of foreign tax credit ('FTC') that can be claimed against MAT exceeds the amount of FTC that is claimable against tax computed under the normal ITA provisions.

Capital Gains

General. The Income Tax Act prescribes special tax rates for the taxation of capital gains. Gains derived from "transfers" of "capital assets" are subject to tax as capital gains and are deemed to be income in the year of the transfer.

The tax rate at which capital gains are taxable in India depends on whether the capital asset transferred is a short-term capital asset or a long-term capital asset. A short-term capital asset is defined as a capital asset that is held for less than 36 months immediately before the date of its transfer. However, following are few exceptions to this:

- If the capital asset is a security (other than a unit) listed on a recognized stock exchange in India or a unit of an equity-oriented mutual fund or a specified zero-coupon bond: 12-months
- If the capital asset is share of a company (not being a share listed in a recognised stock exchange): 12-months
- If the capital asset is an immovable property: 24 months

A capital asset that is not a short-term capital asset is a long-term capital asset.

Capital gains on specified transactions on which Securities Transaction Tax has been paid. Long-term capital gains derived from the transfer of equity shares or units of an equity-oriented fund or units of a business trust on a recognized stock exchange in India are exempt from tax if Securities Transaction Tax (STT) has been paid on the sale and purchase transaction.

Short-term capital gains derived from the transfer of equity shares in a company, units of an equity-oriented fund or units of a business trust on a recognized stock exchange in India are taxable at a reduced rate of 15% plus the surcharge, as applicable, and the cess, if STT has been paid on the transaction.

Capital gains on transactions on which STT has not been paid. For sales of shares and units of mutual funds that have not been subject to STT and for capital gains derived from the transfer of a capital asset that is not a specified security, the following are the capital gains tax rates (excluding the applicable surcharge and cess).

Type of taxpayer	**Short-term capital gains rate *(%)* (a)**	**Long-term capital gains rate (%) (a)**
Domestic companies	30	20
FIIs	30	10
Nonresidents other than FIIs	40	20

(a) The above rates are subject to a surcharge and cess. The surcharge is levied at a rate of 7% for domestic companies and at a rate of 2% for foreign companies if the net income of the company exceeds INR 10 million. The surcharge rate is increased to 12% for domestic companies and 5% for foreign companies if net income exceeds INR 100 million. The rate of the cess is 3%.

Administration: The Indian fiscal year runs from 1 April to 31 March. All companies must file tax returns by 30 September or 30 November (for companies undertaking international transactions; see the discussion of transfer pricing in Section E). Tax is payable in advance on 15 June, 15 September, 15 December and 15 March. Any balance of tax due must be paid on or before the date of filing the return. The carry forward of losses for a fiscal year is not allowed if a return is filed late.

A nonresident with a liaison office in India is required to submit a statement in the prescribed form within 60 days after the end of the fiscal year.

Withholding Taxes. Payments to resident companies are subject to the following withholding taxes:

Type of payment	**Rate** (%) **(a)**
Dividends	10
Interest	10 (b)
Commissions	5
Payments to contractors	2
Rent	2/10 (c)
Income from lotteries and horse races	30
Professional and technical service fees	10
Royalties	10

Type of payment	**Rate** (%) **(a)**
Payments of compensation to residents for the compulsory acquisition of certain immovable property	10
Payment of consideration for transfer of immovable property	1

(a) If an income recipient fails to furnish its PAN, tax must be withheld at the higher of the rate specified in the relevant provision of the Income Tax Act and 20%.

(b) Sec footnote (c) in Section A.

(c) The withholding tax rate for rental payments is 10%. For equipment rental, the rate is 2%.

Payments to non-resident companies are subject to the following withholding taxes.

Type of payment	**Rate** *(%)* **(a)(b)**
Dividends	0
Interest on foreign-currency loans	20
Royalties and technical services fees	10
Rent	40
Income from lotteries and horse races	30
Long-term capital gains other than exempt gains	20
Other income	40

(a) The *2%* or 5% surcharge (applicable to payments made to foreign companies exceeding INR10 million or INR100 million, respectively) and the 3% cess are imposed on the above withholding taxes.

(b) If the income recipient fails to furnish *a* PAN to the payer, tax must be withheld at the higher of the following rates:

- Rate specified in the relevant provision of the Income Tax Act
- Tax treaty rate
- 20%

Dividends. Dividends paid by domestic companies are exempt from tax in the hands of the recipients. However, domestic companies must pay a dividend distribution tax (DDT) at a rate of 15% on the gross amount of dividend payable plus the surcharge and the cess on dividends declared, distributed or paid by them. The DDT paid is a non-deductible expense.

The amount of dividends (on which DDT is leviable) that are paid by a domestic company can be reduced by the amount of dividends received from its subsidiary on which the subsidiary has paid DDT, subject to the satisfaction of prescribed conditions.

Gross dividends received by a domestic company from a specified foreign company (in which it has shareholding 26% or more) are taxable at a concessional rate of 15% (plus applicable surcharge and cess).

Dividends received by an Indian company from a foreign company in which the Indian company has a shareholding of more than 50% can be set off against subsequent dividends paid by the Indian company to its shareholders on which DDT is payable, subject to conditions.

Further, dividends received from domestic company in excess of Rs.10 lakhs will be taxable @10% on gross basis in the hands of the recipient (all residents except for domestic companies).

Buyback tax. The buyback of unlisted shares by an Indian company is subject to buyback tax at a rate of 20% plus surcharge and cess. The tax is computed on the difference between the price at which shares are bought back and the consideration received by the company for issuance of shares. The amounts received are exempt in the hands of the shareholders.

Foreign tax relief. Foreign tax relief for the avoidance of double taxation is governed by tax treaties with several countries. If no such agreements exist, resident companies may claim a foreign tax credit for the foreign tax paid. The amount of the credit is the lower of the Indian tax payable on the income that is taxed twice and the foreign tax paid. Treaty benefits and relief are available only if a nonresident taxpayer obtains a tax-residency certificate indicating that it is resident in a country outside India. This certificate must be issued by the government of that country. In addition to obtaining the certificate, taxpayers must maintain certain prescribed documents and information.

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4. Determination of Trading Income

General. Business-related expenses are deductible; capital expenditures (other than on scientific research in certain cases) and personal expenses may not be deducted. Certain expenses on which taxes are required to be withheld are allowable as deductions only if the required taxes have been withheld and paid to the government. The deductibility of head-office expenses for nonresident companies is limited.

Provisions. Provisions for taxes (other than income tax, dividend distribution tax and wealth tax, which are not deductible expenses) and duties, bonuses, leave salary and interest on loans from financial institutions and scheduled banks are not deductible on an accrual basis unless payments are made before the due date of filing of the income tax return. If such payments are not made before the due date of filing of the income tax return, a deduction is allowed only in the year of actual payment. General provisions for doubtful trading debts are not deductible until the bad debt is written off in the accounts, but some relief is available for banks and financial institutions with respect to nonperforming assets. Interest payable on loans, borrowings or advances that is converted into loans, borrowings or advances may not be claimed as a deduction for tax purposes.

Depreciation allowances. Depreciation is calculated using the declining-balance method and is allowed on block of assets. Depreciation rates vary according to the block of assets. The following are the general rates.

Asset	**Rate (%)**
Plant and machinery	15
Motor buses, motor lorries and motor taxis used in a rental business	30

Asset	Rate (%)
Motor cars other than those used in the business of running them on hire	15
Buildings	10
Furniture and fittings	10

Depreciation is also allowed on intangibles, such as know-how, patents, copyrights, trademarks, licenses, franchises or other similar commercial rights. These items are depreciated using the declining-balance method at a rate of 25%.

Special rates apply to certain assets, such as 60% for computers and computer software, 80% for energy-saving devices and 100% for air or water pollution-control equipment. Additions to assets that are used for less than 180 days in the year in which they are acquired and placed in service qualify for depreciation in that year at one-half of the normal rates.

Relief for losses. Business losses, excluding losses resulting from unabsorbed depreciation of business assets (see below), may be carried forward to be set off against taxable income derived from business in the following eight years, provided the income tax return for the year of loss is filed on time. For closely held corporations, a 51% continuity of ownership test must also be satisfied.

Unabsorbed depreciation may be carried forward indefinitely to be set off against taxable income of subsequent years.

Losses under the heading "Capital Gains" (that is resulting from transfers of capital assets) may not be set off against other income, but may be carried forward for eight years to be set off against capital gains. Long-term capital losses may be set off against long-term capital gains only.

Group of companies. The income tax law does not provide for the consolidation of income or common assessment of groups of companies. Each company, including a wholly owned subsidiary, is assessed separately.

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5. Other Significant Taxes

The following table summarizes other significant taxes.

Nature of tax	Rate (%)
Securities Transaction Tax (STT); payable on transactions in equity shares, derivatives, units of an equity-oriented mutual funds and units of business trusts on a recognized stock exchange: the tax is imposed on the value of the transaction and varies according to the type of transaction	
Delivery-based transactions in equity shares or in units of equity-oriented funds	
Buyer	
- Shares	0.1
- Units	Nil
Seller	
- Shares	0.1
- Units	0.001
Sale of units of an equity-oriented mutual funds; tax paid by seller	0.001
Non-delivery-based transactions in equity shares or in units of an equity-oriented fund; tax paid by seller	0.025
Sale of derivatives	
Sale of option (seller); rate applied to option premium	0.017
Sale of option when option is exercised(buyer); rate applied to settlement price	0.125
Sale of futures (seller)	0.01
Sale of a unit of an equity oriented fund to the mutual fund (seller)	.001

Nature of tax	Rate (%)
Sale of unlisted equity shares under offer for sale to public	0.2
Sale of units of a business trust (delivery-based)	
Tax paid by buyer	0.1
Tax paid by seller	0.1
Sale of units of a business trust (non-delivery-based): tax paid by seller	0.025
Commodities transaction tax; tax paid by seller on taxable value on sales of commodities derivatives	0.01
Central value-added tax (CENVAT), on goods manufactured in India: levied by the central government	Various
Customs duty, on goods imported into India; levied by the central government	Various
Sales tax; generally imposed on sales of goods; levied either by the central government (central sales tax) on interstate sales or the state government (state sales tax: generally referred to as "value-added lax") on intrastate sales	Various
Luxury tax; levied by certain states on notified items (items officially prescribed by the relevant authority)	Various
Works contract tax; on goods for which title is transferred during execution of work contracts (for example, contracts for the construction, fabrication or installation of plant-and machinery)	Various
Lease tax on contracts involving transfer of rights to use goods	Various
Octroi/entry tax; levied by certain municipalities and states on the entry of goods into municipal jurisdiction or state for use, consumption or sale	Various
Research and development cess: imposed on payments made for the import of technology	5
Stamp duties; levied by each state on specified documents and transactions, including property transfers	Various

Nature of tax	Rate (%)
Social security contributions; paid by the employer for medical insurance plans for certain categories of employees and for minimum retirement benefit plans	Various
Service tax. on provision of services including imports of services into India; imposed on all services except those specified in "negative list," and certain exempt services	15

Goods & Services Tax (‘GST’)

GST is a proposed system of indirect taxation in India merging most of the existing indirect taxes into single system of taxation. GST is expected to be applicable from financial year 2017-18. GST would be a comprehensive indirect tax on manufacture, sale and consumption of goods and services throughout India, to replace taxes levied by the central and state governments.

The introduction of GST would be a significant step in the reform of indirect taxation in India. Amalgamating several Central and State taxes into a single tax would mitigate cascading or double taxation, facilitating a common national market. The simplicity of the tax should lead to easier administration and enforcement.

All the existing taxpayers registered under VAT, Service Tax, and Excise are required to furnish the details at GST Common portal for the purpose of migrating themselves into GST regime. Once the taxpayers provide their details there will be no need for them to register again with the State or Center once the GST Act is implemented. Enrollment process for other existing taxpayers not registered with VAT will be started at a later date.

As per the decisions made by GST Council on November 3, 2016, tax rates would be at 4 slabs of 5%, 12%, 18% and 28%. Luxury and demerit goods will be taxed at 28% plus cess. Daily needs will be taxed at 5%.

6. Miscellaneous Matters

Foreign-exchange controls. All cross-border transactions with nonresidents are subject to foreign-exchange controls contained in the Foreign Exchange Management Act. The rupee is fully convertible for trade and current account purposes. Except for certain specified restrictions, foreign currency may be freely purchased for trade and current account purposes. In general, such purchases must be made at the market rate. Capital account transactions are not permitted unless they are specifically allowed and the prescribed conditions are satisfied. Cross-border transactions that are specifically allowed include the following:

- All remittances abroad that require prior approval arrangements, such as joint venture and technical collaboration agreements.
- The remittance of interest, dividends, service fees and royalties.
- Repatriation of capital is also freely permitted for investment approved on a repatriable basis.

Transfer pricing. The Income Tax Act includes detailed transfer-pricing regulations. Although the guidelines are broadly in line with the principles set out by the Organisation for Economic Co-operation and Development (OECD), key differences exist.

Under these regulations, income and expenses, including interest payments, with respect to international transactions between two or more associated enterprises (including permanent establishments) must be determined using arms-Length prices. The transfer-pricing regulations also apply to, among other transactions, cost-sharing arrangements, certain capital-financing transactions, business restructurings or reorganizations and dealings in intangibles.

The transfer-pricing regulations contain definitions of various terms, including "associated enterprise," "arm’s-length price," "enterprise," "international transaction" and "permanent establishment.[1]’ It specifies methods for determining the arms-length price. The following are the specified methods:

- Comparable uncontrolled price method
- Resale price method
- Cost-plus method
- Profit split method
- Transactional net margin method
- Any other method that takes into account the price that has been charged or paid or would have been charged or paid, in the same or a similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances, considering all the relevant facts

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7. Treaty Withholding Tax Rates

Under the Income Tax Act, Indian companies are required to pay DDT (see Section B) at an effective tax rate of nearly 20.36% (base rate of 15% on gross amount plus a surcharge of 12% and an education cess of 3%) on dividends declared, distributed or paid by it. Such dividends are exempt from tax in the hands of the recipients.

Tax rates specified under the Income Tax Act are increased by a surcharge and cess. In general, if the relevant treaty specifies the same or lower rate for withholding, these treaty rates, which are more beneficial for the nonresident recipient, may be applied. In addition, these tax rates need not be increased by the surcharge and cess. To claim treaty benefits, the nonresident recipient must obtain a Tax Residency Certificate indicating that it is a resident of that country or specified territory. This certificate is issued by the government of such country or territory. The nonresident recipient is also required to provide certain information and documents to substantiate its eligibility to claim treaty benefits.

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