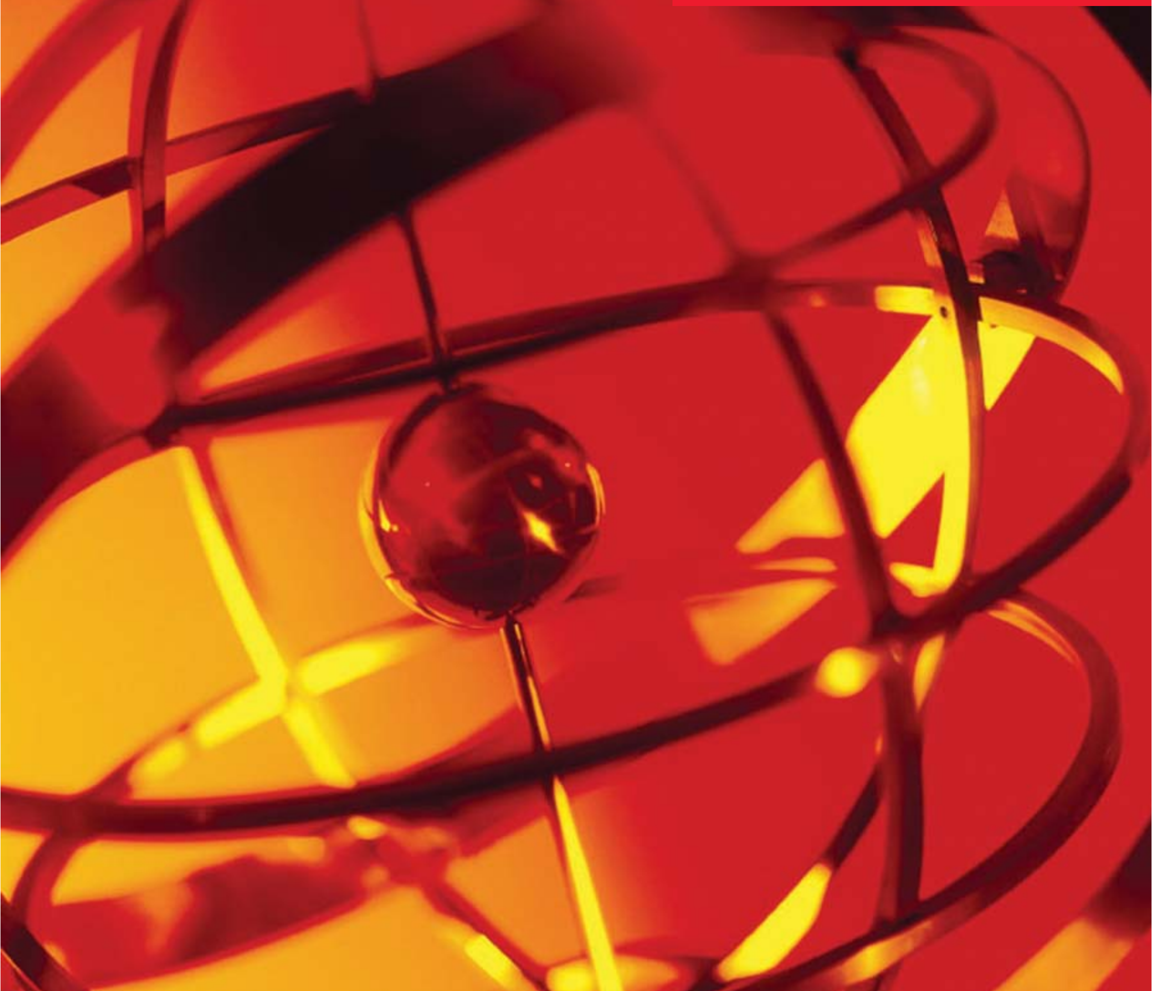
TAX AND BUSINESS GUIDE



ERNST & YOUNG

Quality In Everything We Do

Doing Business in India

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Preface

This book was prepared by Ernst & Young, India with the intention of giving busy executives a quick overview of the investment climate, taxation, forms of business organisations and business and accounting practices in India. The complex decision-making process involved in undertaking foreign operations requires an intimate knowledge of a country's commercial climate, along with a realisation that the climate is constantly evolving. Companies doing business in India, or planning to do so, are well-advised to obtain current and detailed information from experienced professionals. This book reflects information current at May 31, 2006.

List of frequently used abbreviations

ADR	American Depository Receipts
BCTT	Banking Cash Transaction Tax
BPO	Business Process Outsourcing
BTP	Biotechnology Park
CAGR	Compounded Annual Growth Rate
CBDT	Central Board of Direct Taxes
CCI	Competition Commission of India
DDT	Dividend Distribution Tax
EHTP	Electronic Hardware Technology Park
EOU	Export Oriented Unit
EPZ	Export Processing Zone
FBT	Fringe Benefit Tax
FCCB	Foreign Currency Convertible Bond
FDI	Foreign Direct Investment
FEMA	Foreign Exchange Management Act, 1999
FII	Foreign Institutional Investor
FIPB	Foreign Investment Promotion Board
FTP	Foreign Trade Policy
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GDR	Global Depository Receipts
HTP	Hardware Technology Park
IRDA	Insurance Regulatory and Development Authority
IT	Information Technology
ITA	Information Technology Agreement
ITES	IT Enabled Services
MNC	Multinational Corporation
MoF	Ministry of Finance
MoP	Ministry of Power
NBFC	Non-Banking Financial Company

NHPC	National Hydel Power Corporation
NPC	Nuclear Power Corporation
NRIs	Non-resident Indians
NTPC	National Thermal Power Corporation
PIO	Person of Indian Origin
PSB	Public Sector Bank
PSU	Public Sector Unit
RBI	Reserve Bank of India
Rs	Indian Rupee
SDR	Special Drawing Rights
SEBI	Securities and Exchange Board of India
SEZA	Special Economic Zones Act, 2005
SEZ	Special Economic Zone
STP	Software Technology Park
STT	Securities Transaction Tax
TRAI	The Telecom Regulatory Authority of India
VAT	Value Added Tax
WTO	World Trade Organisation


INDIA
States and Union Territories
N
JAMMU & KASHMIR
Srinagar
HIMACHAL PRADESH
Shimla
Chandigarh
PUNJAB
PAKISTAN
CHINA (TIBET)
UTTARANCHAL
Dehradun
DELHI
HARYANA
ARUNACHAL PRADESH
NEPAL
SIKKIM
Gangtok
BHUTAN
Itanagar
UTTAR PRADESH
Lucknow
RAJASTHAN
Jaipur
Patna
BIHAR
ASSAM
Dispur
NAGALAND
Kohima
Imphal
MANIPUR
MEGHALAYA
Agartala
TRIPURA
Aizawl
MIZORAM
MYANMAR
GUJARAT
Gandhinagar
Bhopal
MADHYA PRADESH
Ranchi
JHARKHAND
CHHATTISGARH
Raipur
ORISSA
Bhubaneshwar
BANGLADESH
DIU
DAMAN
DADAR & NAGAR HAVELI
MAHARASHTRA
Mumbai (Bombay)
Hyderabad
ANDHRA PRADESH
YANAM (Pondicherry)
ARABIAN SEA
Panaji
GOA
BAY OF BENGAL
KARNATAKA
Bangalore
Chennai (Madras)
PONDICHERRY (Puduchchery)
LAKSHADWEEP
MAHE (Pondicherry)
TAMILNADU
KARAIKAL (Pondicherry)
Port Blair
ANDAMAN & NICOBAR ISLANDS
KERALA
Thiruvananthapuram
Map not to Scale

Introduction

Basic Statistics

Land area: 3.29 million square kilometres

Capital: New Delhi

Population: 1.107 billion (estimated as at October 1, 2005)

Languages spoken: Eighteen principal languages; majority speak Hindi; business language: English

International airports: Ahmedabad, Amritsar, Bangalore, Chennai, Dabolim, Guwahati, Hyderabad, Kochi, Kolkata, Mumbai, Nagpur, New Delhi, Srinagar and Thiruvananthapuram

Major seaports: Chennai, Ennore, Haldia, Kandla, Kochi, Kolkata, Marmagao, Mumbai, New Mangalore, Paradip, Tuticorin and Vishakhapatnam

The Land

Spread over 3 million square kilometres and located entirely in the northern hemisphere, India is the seventh largest country in the world in terms of geographical size. India's neighbours are Bangladesh and Myanmar in the east; Bhutan, China and Nepal in the north; Pakistan in the west and Sri Lanka in the south.

The People

Population

As per the last census carried out in 2001, India had a population of approximately 1.029 billion. Based on historical growth rates, the population as at October 1, 2005 was an estimated 1.107 billion, and the country is expected to overtake China and become the most populous nation by 2045.

Language

Given its cultural diversity, scores of languages and dialects are spoken in the country. Of these, 22 languages are recognised in the Indian Constitution, which include Bangla, Gujarati, Hindi, Kannada, Malayalam, Marathi, Oriya, Punjabi, Sanskrit, Tamil, Telugu and Urdu. Hindi, written in the Devanagari script, is the national language, while English is the business language.

Religion

As India is a secular country, it does not advocate any one religion, and all religions are accorded equal status before the law. The various religions practiced in the country are Hinduism, Islam, Christianity, Sikhism, Buddhism, Jainism, Judaism and Zoroastrianism.

Education
India has over one million schools and around 9,200 colleges in general fields, 4,600 colleges in professional fields and 300 universities / institutions of national importance. There are a large number of private and government or municipal corporation-run schools, in the urban areas. However, in the rural areas, education is imparted largely by government-run schools. Professional educational institutes, with a combined intake of over half a million students per annum, constantly add to the country's large pool of skilled English-speaking work force, which is a tremendous competitive advantage vis-à-vis other nations.

Cost of Living
India offers the advantage of a low cost of living, relative to American and European countries. The cost of living varies by type of location (urban / rural), size of location (small / large / metro), etc.

Travel
Most parts of the country are well connected by air, rail and road transport. For domestic air travel, there are a number of regular airlines-Indian, Jet Airways, Air Sahara and Kingfisher Airlines as well as budget airlines for inexpensive air travel Air Deccan, Spice Jet, GoAir, and Paramount Airways. Nearly every major international airline operates flights to and from the country. The country also has an extensive rail and road transport network. Railway services are offered by the government-owned Indian Railways. Bus services (regular, deluxe and luxury) over shorter distances are provided by government agencies and private operators. Numerous car rental agencies offer cars for hire and public taxis are available in some cities.

Tourism
Tourism is in a high-growth phase in the country. In 2005-06[1], foreign tourist arrivals numbered more than 4 million and the country earned over US$ 5.9 billion from foreign tourist spending. Foreign tourists comprise business and leisure travellers and with growing foreign investment interest in India, the business travel segment is expected to witness rapid growth.

Besides the Indian Tourism Development Corporation (ITDC) which is run by the Central Government, each state has its own tourism development corporation.

Time Zone

India is five and one-half hours ahead of the Greenwich Mean Time. It has not adopted daylight saving time and uses standard time countrywide throughout the year.

Business Hours
Normal business hours are from 9:00 am to 6:00 pm, Monday through Friday. Some commercial establishments also work on Saturdays. Banking hours are

[1] *'2005-06' refers to the fiscal year beginning April 1, 2005*

usually from 9:00 am to 3:00 pm although some banks have branches open till 8:00 pm. Shops are usually open till 9:00 pm six days a week. Sunday is the weekly holiday, although this can vary from place to place for various markets.

Public Holidays

Public holidays are announced by the central government and by individual state governments. There are three national holidays-Republic Day (January 26th), Independence Day (August 15th) and Gandhi Jayanti (October 2nd). In addition, there are several holidays for festivals, the dates of which change from year to year.

Useful Addresses and Telephone Numbers

For a listing of useful addresses and telephone numbers, please refer to Appendix 1.

A. Government Structure and Economic Climate

A.1 Government Structure

As enshrined in its Constitution, India is a sovereign, socialist, secular, democratic republic. It comprises 29 states and six union territories. Each state is administered by a state government, while the central government is in charge of the overall administration of the country. The union territories are administered by representatives nominated by the central government.

India follows a parliamentary form of government. Even though the President is the Head of the Republic, the real powers are vested in the Prime Minister, who is the elected representative of the people. The government has three branches - legislature, executive and judiciary.

The Legislature
At the central level, India has a bicameral legislature. The Union Parliament comprises the Lok Sabha (House of the People or the Lower House) and the Rajya Sabha (Council of the States or the Upper House). Members of the Lok Sabha are directly elected by the people of the country, while the majority of members of the Rajya Sabha are representatives of the states and union territories.

At the state level, some states have a unicameral legislature (Legislative Assembly) while some have bicameral legislature (Legislative Assembly and Legislative Council). The members of the Legislative Assembly of a state are directly elected by the people of that state.

The Election Commission is an independent body with the mandate to oversee the election process to ensure free and fair elections at the central and the state levels.

The Executive
The leader of the majority party in the Lok Sabha usually becomes the Prime Minister of the country. The Prime Minister and the Council of Ministers, collectively called the Union Cabinet, are vested with the responsibility of running the day-to-day affairs of the central government. The past few governments in the country have been coalition governments, with no single political party securing absolute majority in the Lok Sabha.

Similarly, at the state level, the leader of the majority party in the Legislative Assembly becomes the Chief Minister of the state. The Chief Minister along with his Council of Ministers (together called the State Cabinet) are responsible for the day-to-day affairs of the state government.

The Judiciary
India has an independent judicial system. The Supreme Court is the apex judicial authority, and below it are the High Courts which head the judicial system in each

state. Under each High Court there is a hierarchy of subordinate courts (district level and lower).

Political Parties
India has numerous political parties, including national, regional and local parties. The major national parties are the Congress (I), the Bhartiya Janata Party (BJP), the Communist Party of India (CPI), the Communist Party of India - Marxist (CPM) and the Janata Dal (JD).

A.2 Financial System

Reserve Bank of India

The Reserve Bank of India (RBI), established in 1935, is the central bank of the country. Its role is four-fold:

- Regulate and supervise the Indian financial system;
- Formulate, implement and monitor the monetary policy of the country;
- Manage the country's foreign exchange reserves and prescribe exchange control norms to facilitate external trade and payment; and
- Act as banker to the Central and State Governments.

RBI, through its policies, directives and guidelines, has been placing increasing emphasis on the monitoring of and provisioning for non-performing assets, capital adequacy and risk management.

Types of Institutions

The banking system in India comprises scheduled commercial banks, urban and state cooperative banks and regional rural banks. Scheduled commercial banks, in turn, can be categorised into public sector banks, private sector banks and foreign banks. Besides banks, another segment of players in the Indian financial system, are non-banking financial companies (NBFCs).

Public Sector Banks
This segment comprises 28 banks, including the State Bank of India and its seven subsidiary banks. It is the dominant segment in the banking industry. The central government is the majority shareholder, holding more than 51% equity stake in all the public sector banks, although its shareholding has decreased over the years on account of public offerings of shares and return of equity capital to the Government by these banks.

Private Sector Banks
This segment comprises 28 banks, including seven new private sector banks and 21 old private sector banks. The new private sector banks are growing rapidly in size.

The last couple of years have witnessed some mergers and acquisitions in this segment, and this trend is expected to gain in strength in the years to come. The RBI has placed restrictions on shareholding in private sector banks and no shareholder can hold more than 5% shareholding in a private sector bank.

Foreign Banks

This segment comprises 29 banks, including most of the leading international banks, although their presence is restricted to the metropolitan and large cities. Currently, there are several restrictions on foreign banks with respect to the expansion of branch network, location of new branches, acquisition of shareholding in Indian banks, etc. However, recently, RBI has come out with a road map for deregulation of foreign banks, whereby from 2009, a foreign bank would be on par with an Indian bank, and can freely compete with other Indian banks, carry out mergers and acquisitions, etc.

Cooperative Banks and Regional Rural Banks

Cooperative banks cater to the credit needs of specific communities or groups of people in a region and operate in both urban and rural areas. They have been established under the respective State Co-operative Societies Acts, and are administered by the state authorities, although their banking activities come within the purview of RBI. Regional rural banks were established under an act of the Parliament with a view to improving credit delivery in rural areas.

Non-Banking Financial Institutions (NBFIs)

NBFIs offer enhanced equity and risk-based products. They play a crucial role in broadening access to financial services and enhancing competition and diversification of the financial sector. The NBFI segment comprises all-India financial institutions, state-level financial institutions, NBFCs and primary dealers. The first two are government-owned and focus on long-term development financing; NBFCs are mostly private sector entities that provide niche financial services; and primary dealers play an important role in the primary and secondary government securities market.

A.3 Type of Economy

Sweeping economic reforms that commenced in 1991 have included the delicensing of most industries, deregulation of industries earlier monopolised by the public sector, liberalisation of foreign trade through a steady reduction in tariffs, and freeing up of the foreign investment limits in nearly all industries combined with an active wooing of FDI into the country. These measures have had far-reaching consequences and today, India has a strong, vibrant and fast-growing economy, which is rapidly integrating with the global economy. According to the Goldman Sachs BRICs report, India is forecast to become the third largest economy in the world, after China and the US, by the year 2050, overtaking all other developed economies.

The country's key strengths / competitive advantages are a dynamic and competitive private sector that accounts for over 75% of its GDP and offers considerable scope for collaborations; a sound and independent legal system; a large and growing consumer market; and a vast pool of English-speaking and skilled managerial and technical manpower that matches, if not surpasses, the best in the world. These factors have led numerous multi-national corporations (MNCs) to not only establish operations in India but also to count it among their key markets.

General Economic Trends

Key Economic Indicators

After growing by 7.5% in 2004 - 05, the economy accelerated in 2005 - 06, with real GDP growing by 8.4% y-o-y. With the agriculture sector growing by only 3.9% y-o-y, the industry and services sectors were the principal drivers of economic growth during the year growing by 8.7% and 10% respectively.

The economy is expected to maintain the growth tempo in the current year. As per the latest estimates of the Centre for Monitoring Indian Economy, real GDP growth for the full year is forecast to be 7.9% y-o-y, with agriculture, industry and services expected to grow by 2.5%, 8.5% and 9.6% respectively.

The country's foreign currency reserves, excluding gold and SDRs, swelled from US$ 135 billion at the end of 2005 to about US$ 158 billion (August 18, 2006). The principal factors responsible for this reserve accretion are the country's burgeoning services exports and strong capital inflows comprising FDI and foreign portfolio investments by foreign institutional investors (FIIs).

The Indian rupee (INR or Rs.) has appreciated against the US dollar over the past few years. The INR-US$ exchange rate, which stood at 48.80 on March 31, 2002, is currently ruling at 46.48 (August 18, 2006)[2] .

Inflation, measured on a weekly basis by the Wholesale Price Index, ruled lower at 4.4% on an average during 2005 - 06, as against 6.4% in 2004 - 05. However, in the current fiscal, inflation has inched up owing to a surge in international crude prices and strong growth in domestic demand for credit. To rein in inflation, RBI has tightened its monetary policy. As a result, interest rates, which had shown a steady decline over the years, have started moving up again. The maximum prime lending rate (PLR) has recently been hiked from 10.75% to 11.25%.

The Market

Consumer Market

India's large and growing consumer market is one of the chief attractions for multinational consumer product companies. Steadily increasing urbanisation and explosive growth of the electronic media have brought about sweeping changes in the lifestyles and consumption attitudes of people. The availability of cheap

[2] *For detailed information on the Indian currency, please refer to the note on 'Currency' in the following section*

consumer finance has served to fuel this boom in consumerism. These factors have generated a growing demand for a variety of quality products and services such as convenience foods, branded clothing, automobiles, toys, home appliances, electronic goods, restaurants, travel, communication and entertainment.

In the rural areas, the electronic media has played a great role in enabling consumer product companies create awareness about their branded products which has caused a shift in consumption from unbranded and traditional products to branded alternatives. Besides, the composition of the consumption basket has also changed, with the share of food items decreasing in favour of non-food products. While urban areas have a range of retail outlets from small mom-and-pop stores to large supermarkets, the villages are catered to by small shops.

Industrial Market

The industrial market is an equally large and diverse market comprising a wide range of products for industrial consumption. While the majority of requirements are met domestically, some products are imported. A significant quantum of production in certain industries is also exported. Recognising India's cost advantages and technical expertise in manufacturing, several MNCs have begun to use the country as a manufacturing base to outsource their regional or global product requirements. During the last three years (2004-06), industrial production (measured by Index of Industrial Production) grew at an average of 7.8% per annum. In the current fiscal, it is expected to grow by 8%.

Currency

India's monetary unit is the Indian rupee (INR/Rs). Only the central government is empowered to legislate on matters relating to currency and coinage and RBI is the sole authority empowered to issue currency. RBI notes are fully backed by approved security, including bullion, foreign securities, rupee coins and rupee securities of the government.

A rupee is divided into 100 paise. The denominations of currency notes and coins presently used are Rs 1,000, Rs 500, Rs 100, Rs 50, Rs 20, Rs 10, Rs 5, Rs 2, Re 1 and 50 paise.

As the rupee is not freely convertible into foreign currency, foreign exchange transactions are carried out through entities authorised by the RBI to deal in foreign exchange or foreign securities, i.e. an authorised moneychanger or an offshore banking unit. A person may purchase foreign exchange from an authorised dealer by providing a declaration of the intended use of the foreign exchange. Usage of the foreign exchange for purposes other than that declared would lead to contravention of the Foreign Exchange Management Act, 1999 (FEMA).

A.4 Leading Industries

Since the commencement of economic reforms in 1991, successive governments have implemented strong measures to liberalise the business environment and boost industrial growth. The elimination of licensing requirements for all but six industries has ushered in an era of competition and imparted dynamism to the industry.

Substantial reduction in import tariffs on raw materials and intermediate products, coupled with rationalisation of excise duties, have eased access to inputs and reduced costs. Forward-looking export-import policies have enhanced the competitiveness of the country's exports, and created an environment conducive to their rapid growth. In order to enable industry to imbibe state-of-the-art technology and global best practices, the government has been welcoming FDI and foreign collaborations; FDI limits in almost all industries have been progressively liberalised and approval procedures simplified. With liberalisation, FDI in a large number of industries is permitted upto 100% automatically, without any approvals. FDI in sectors like telecom, real estate, retail, etc is permitted, but subject to certain restrictions.

Oil and Natural Gas

India is the world's fifth largest consumer of primary energy. Primary energy consumption has grown at a rate that is one of the highest in the world and is expected to double in the next two decades. About a quarter of the country's primary energy needs are met by oil and gas.

The total estimated consumption of crude oil and natural gas during 2005 was 131.6 million tonnes and 33.5 billion cubic metres respectively. Nearly 70% of the country's oil requirements are met through imports.

Regulatory scenario
The industry is under the administrative charge of the Ministry of Petroleum and Natural Gas. FDI up to 100% under the automatic route is permitted in all activities including exploration and production, pipelines and liquified natural gas terminals and refining and marketing (except in existing refineries owned by PSUs) subject to sectoral policy regulations.

In the upstream segment, under the New Exploration and Licensing Policy (NELP) III, the government has introduced a policy with attractive terms for private investors, which has boosted private investment. NELP VI is currently underway in which 55 blocks are on offer.

Recent developments and industry outlook
The enactment of the Petroleum and Natural Gas Regulatory Board Act, 2006 has paved the way for the establishment of a regulator for midstream and downstream refining and marketing activities. The Government has also constituted a task force

on 'Petroleum Chemicals and Petrochemicals Investment Regions' to devise a policy framework to promote the development of these regions.

The demand for oil and gas is projected to grow to 368 million tonnes and 141 billion cubic metres respectively by the year 2025. An estimated investment of US$ 100-150 billion would be required over the next 10-15 years to cater to the projected demand.

In the upstream segment, it is envisaged, that in the medium term, instead of rounds of bidding for the award of exploration blocks, there would be open availability of exploration acreages all round the year. In the natural gas segment, significant investment is expected to take place in the establishment of new gas transmission pipelines and city gas distributions (CGD) networks. Setting up of technology hubs by global energy companies is a trend likely to emerge in the Indian energy sector.

Power

The Indian power sector is undergoing major reform and restructuring with a thrust on encouraging private sector participation. As at April 2006, the total installed capacity was 146,386 megawatts (MW) and the total energy shortage during April 2005 to February 2006 was 47,845 MW (8.3%).

As per projections, over 100,000 MW additional generation capacity needs to be added by 2012 to bridge the gap between the demand and supply of power. The latest estimates suggest that the capacity addition expected to be achieved during the Tenth Plan is 34,024 MW.

The total investment required in capacity creation, transmission and distribution is estimated at US$200 billion, of which US$100 billion is required for generation projects alone.

Regulatory scenario

The Power industry is under the overall charge of the Ministry of Power. To facilitate reforms, the Central Electricity Regulatory Commission (CERC) at the national level and State Electricity Regulatory Commissions (SERCs) at the state level were established.

The government has been striving to provide a conducive policy environment to encourage free and fair competition in each element of the energy value chain and attract capital from all sources - public and private, domestic and foreign.

The Electricity Act, 2003 has introduced significant changes in the industry, by enabling private sector access to state electricity board transmission grids, allowing them to sell directly to large industrial consumers.

The National Electricity Policy 2005 allows for 100% FDI in all sectors (other than nuclear power plants).

Recent developments and industry outlook
Recent guidelines issued ensure that all future generation projects are developed by competitive bidding, further lowering the project cost and ensuring cheap power to consumers.

The National Tariff Policy 2006 states that power should be procured solely through the competitive bidding route. For global power companies, India offers a huge market with exemption from taxes on profits earned for 10 years.

The environment is right for the growth and maturing of the Indian power sector. The following are some key areas where opportunities for investments exist: Ultra Mega Power Projects, Hydro Projects, Captive Power, Nuclear Power and Renewables.

Mining

India is endowed with huge reserves of several metallic and non - metallic minerals. Mineral production constitutes 2.6% of the country's GDP.

Adequate survey and exploration activities are yet to be carried out to adjudge the full potential of the country's vast resources. Despite a favourable FDI regime, foreign investment is much below the desired level due to policy and procedural issues.

Regulatory scenario
The Ministry of Mines regulates the mining sector, other than coal and atomic minerals. State governments own the minerals in their respective states. The Mines and Minerals (Development and Regulation) Act, 1957 (MMDR Act) is the governing legislation in this sector.

FDI upto 100% is allowed under the automatic route for exploration and mining of minerals. However, no FDI/ private investment is permitted for coal mining except for captive consumption by power, cement, iron and steel companies. The FDI limit for exploration and mining of diamonds and precious stones has recently been raised to 100% from 74%.

Recent developments and industry outlook
The government has constituted a committee to review the National Mineral Policy, 1993 which has submitted its draft report and the key recommendations[3] *inter alia* including the following:

- Removal of delays for granting mineral concessions and forest clearances
- Preferential allocation of mines to steel plants that do not have captive mines
- Charging royalty on ad-valorem basis
- Preference to those willing to set up an industry in a mining state
- Prioritise infrastructural needs and facilitate investments to meet these needs
- Set up new mechanism in stock exchanges for raising funds

[3]*As available in the public domain*

The Indian mining sector can take a giant leap forward and significant investments can be expected if the above recommendations are accepted. However, the recommendation for captive mining can be a dampener. A comprehensive review of the coal policy is also underway which will further provide a fillip to the investment in coal mining in India.

Information Technology

The IT industry has been at the forefront of India's success story and continues to charter remarkable growth. The industry comprises software services, ITES (including BPO) and hardware. India's unparalleled prowess as an IT-ITES hub is well-established across the globe and the country is a key sourcing base and strategic market for the global IT-ITES sector.

Since 1999 - 2000, the sector has grown at a CAGR of over 28%; the industry's contribution to GDP has risen from 1.9% to a projected 4.8% in the current fiscal. The industry is anticipated to exceed US$36 billion in 2005 - 06 and should achieve the targeted US$ 60 billion by 2009 -10. Exports are estimated to exceed US$ 23.9 billion in 2006-07 while IT software and services employment is expected to reach 1.2 million in 2006-07.

Regulatory scenario
The government has been proactive in encouraging foreign investment in the IT-ITES sector. Not only has the FDI regime been liberalised, there are also various fiscal incentives (including export-related incentives) made available to IT operations in India.

Recent developments and industry outlook
The IT-ITES services is poised for rapid growth over the next few years by offering a wider services portfolio, catering to a larger set of industry verticals and increasingly evolving to become a global Knowledge Process Outsourcing (KPO) hub.

A new opportunity on the engineering services front is emerging. While currently India brings in around US$ 1.8 billion of this market, by 2020 as much as US$ 50 billion could belong to India.

Hardware is poised for robust growth with several MNCs setting up their manufacturing facilities in India. A policy for making India a preferred destination for the manufacture of semi-conductors and other high - technology products is proposed to be formulated shortly.

A national e-governance plan, which lays out the blueprint for a more e-enabled India, is to be implemented shortly. Further, amendments to the Information Technology Act, 2000 are proposed, with a view to effect special emphasis on strengthening the information security environment.

Telecommunications

India's rapidly growing telecom sector has seen much activity in the last couple of years. Today approximately five million telephone lines (both fixed and mobile) are added every month.

The total number of telephone connections touched 140.32 million at March 31, 2006 from 124.78 million at December 2005. Mobile leads the subscriber numbers with 90.14 million subscribers as against the fixed line subscriber base of 50.18 million (as on March 31, 2006). Teledensity has gone up from 2% in 1999 to over 12.8% at the end of March 2006, and is expected to cross 20% in the next five years.

The wireline segment is dominated by Bharti Sanchar Nigam Limited (BSNL) and Mahanagar Telephone Nigam Limited (MTNL), the state-owned enterprises. However, private players like Bharti have also made significant inroads. In the mobile segment (which is the main driver of the growing teledensity), Bharti and Reliance are the market leaders.

Regulatory scenario

The Department of Telecommunications (DoT), under the Ministry of Communications, is the administrative department for monitoring the telecommunications sector. The Telecom Regulatory Authority of India (TRAI) and the Telecom Dispute Settlement and Appellate Tribunal (TDSAT) are other government agencies responsible for governing the industry.

FDI upto 49% under the automatic route and 74% subject to conditions is allowed for telecom services. However, in case of Internet services (without gateway) and for telecom equipment/ handset manufacturing activities, FDI upto 100% is permitted.

To promote competition in national/international long distance services, the government has liberalised certain licensing conditions and roll-out obligations and has relaxed the one-time entry fee.

Recent developments and industry outlook

Recently, there has been a spate of acquisitions with bigger players snapping up smaller players in an attempt to become larger and stronger. Vodafone purchased 10% equity stake in Bharti for more than US$1.5 billion; Maxis (Malaysia's largest mobile phone company) bought out Aircel for more than US$1 billion and Telekom Malaysia has bought 49% stake in Spice Telecom for more than US$ 178 million.
Global telecom equipments manufactures like Nokia and Ericsson have also established their manufacturing facilities in India.

The total number of telecom subscribers is expected to touch approximately 250 million by 2007-08. Revenue from telecom industry is expected to grow to US$ 23-25 billion by 2009.

Entertainment

The entertainment industry is one of the fastest growing sectors in India. The current size of the industry is estimated at US$ 4.5 billion, and it is expected to grow to US$ 10 billion by 2009.

The estimated revenue of the film industry is US$ 1.25 billion; television reach is 59.5% of the population. The estimated revenue of the music industry is US$ 150 million; radio broadcasting reaches 99% of the population.

Regulatory scenario
The Ministry of Information and Broadcasting is responsible for laws, rules and regulations relating to information, broadcasting, the press and films. TRAI is the regulator for the Broadcasting and Cable Services.

The Cinematograph Act, 1952 and the Prasar Bharati (Broadcasting Corporation of India) Act, 1990 regulate the functioning of films, national television and national radio. Cinema exhibition rules, entertainment tax regulations, etc. are state specific and almost all states have enacted laws on the same.

Presently, FDI upto 100% is allowed in the film industry; 49% in television broadcasting, 26% in FM broadcasting and 26% in publishing newspapers and periodicals dealing in news and current affairs.

Recent developments and industry outlook
Several countries such as Canada and France have signed film co-production agreements with India. A rapid growth in television penetration and the number of television channels was witnessed with the entry of private channels in the early 1990s. The radio segment has witnessed a jump in listenership with the launch of new FM radio stations pursuant to the privatisation of FM radio in 2005.

The film segment is poised to grow at an impressive rate in the future, primarily due to expansion in exhibition infrastructure and development of multiplexes, availability of finance from institutional sources, exports of film and animation software, etc. The concepts of insurance and institutional financing of films have also taken off recently.

The total revenue of the film, music and radio industries is estimated to touch US$ 2.9 billion, US$ 172 million and US$ 144 million respectively, by 2009.

Banking

Prior to the reforms in 1991, India's banking system was almost entirely owned by the government, except for about 22 private sector banks and foreign banks. The reforms of 1991 led to the banking system's movement from a totally administered sector into a more market driven one. The entry of new private sector banks has brought increased competition, though public sector banks (PSBs) still continue to dominate the banking system.

There are 94 scheduled commercial banks which account for around 68,000 branches with total asset size of US$ 530 billion.

Regulatory scenario
The Ministry of Finance is responsible for the policies of the financial system. RBI regulates the banking system, NBFCs and key financial institutions.

The Banking Regulation Act, 1949; RBI Act, 1934; and Companies Act, 1956 are the governing regulations in this sector.

In private sector banks, foreign equity upto 74% is allowed under the automatic route including FII investments (upto a maximum of 49%) and NRI investment (upto a maximum of 24%).

Recent developments and industry outlook
RBI has announced norms for the ownership of foreign banks in Indian private sector banks. A roadmap for the presence of foreign banks in India has been announced and from 2005-09, foreign banks are permitted to set up wholly-owned subsidiaries in India.

With a view to provide banks additional options for raising capital funds, to meet both the increasing business requirements as well as the Basel II requirements, Indian and foreign banks have been allowed to augment their capital funds by the issue of certain hybrid instruments.

All commercial banks are expected to implement Basel II norms with effect from March 31, 2007.

From April 2009, RBI proposes to accord full national treatment to wholly-owned subsidiaries of foreign banks.

Capital Markets

The Indian capital markets have witnessed a transformation over the last decade and India is now placed among the mature markets of the world.

Regulatory scenario
SEBI was established as a statutory body in 1992 to:

- regulate and promote development of the securities market and protect the interest of small retail investors;
- regulate the functioning of capital markets and issue detailed guidelines

concerning capital markets, disclosures by public companies and investor protection; and

- formulate regulations to govern various intermediaries and also regulate the mutual fund industry, investments by FIIs and venture capital investments.

Dealings in securities are also governed by the provisions of The Securities Contracts (Regulation) Act, 1956.

Mutual Funds

The entry of private sector funds in 1993 has given the Indian retail/corporate investor a wider choice of fund families.

In 2005 - 06, overall assets under management grew by 55% to US$ 33.2 billion at March 2006. A total of 190 new schemes were launched during the year as against 97 in the previous year. The dominance of the private sector has increased from 32.89% in 2001 to 78.28% in March 2006.

SEBI recently issued broad guidelines permitting real estate mutual funds (REMFs).

Foreign Institutional Investors

India has, of late, generated a high level of interest among FIIs on account of its deep and liquid stock market and relatively high returns generated by it. Total investment by FIIs increased from US$ 35.93 billion to US$ 45.11 billion during 2005 - 06. The number of FIIs registered with SEBI increased from 540 in March 2004 to 685 in March 2005 and 882 in March 2006.

Venture Capital Funds (VCF)

VCF visibility has increased over last couple of years with several large funds looking actively at investments in India. VCFs and private equity investors invested an estimated US$ 1.1 billion in 66 India-based companies in 2004. At March 2006, there were 80 VCFs and 45 foreign VCFs registered in India.

Insurance

The insurance industry in India was traditionally the domain of government-owned insurance behemoths such as the Life Insurance Corporation (LIC) in the life insurance segment, and the General Insurance Corporation and the Export Credit and Guarantee Corporation in the non-life insurance segment. In August 2000, the insurance sector was opened up to private participation and since then, 15 new life insurance companies and 11 new general insurance companies have entered the market as joint ventures with major global insurance companies.

During 2005-06, life insurance companies underwrote a first year premium of US$ 8 billion, representing a 41% growth over the previous year. During the year 35.46 million policies were underwritten. In the non-life insurance, the total gross premium income during 2005-06 was US$ 4.67 billion, a 16.13% increase over the previous year.

LIC dominates the life insurance sector with a market share of 71% during 2005-06. The performance of private sector players has been robust and their market share in premium has increased to 29% in 2005-06 compared with 22% in 2004-05. In non-life insurance, the share of private insurers has increased to 26.6% in 2005-06 compared with 20.2% in 2004-05.

Regulatory scenario

The Insurance Regulatory and Development Authority (IRDA) regulates the insurance and reinsurance business in India.

FDI (including FII and NRI investments) of upto 26% is allowed under the automatic route subject to obtaining license from IRDA.

Recent developments and industry outlook

There has been an intention to increase FDI in the sector from 26% to 49%. However, this policy initiative has been stalled on account of opposition from certain political parties.

A committee set up by IRDA for examining the feasibility of setting of 'Standalone Health Insurance Companies' has recommended an increase in the FDI limit in such companies upto 49% and a reduction in minimum capital requirements to US$ 5.56 million[4] (equivalent of Rs 250 million) from the current limit of US$ 22.2 million (equivalent of Rs 1 billion) applicable to any insurance company.

IRDA has issued a roadmap for time bound de-tariffing of the general insurance industry. The roadmap specifies December 31, 2006 as the proposed date for the discontinuation of tariffs.

Retail

With an estimated market size of US$ 258 billion, India's retail sector is at the peak of its appeal for international and Indian players. Being the second-largest employer after agriculture, and contributing 14% to the country's GDP, the retail sector has emerged as one of the mainstays of the Indian economy.

Organised retailing in India is a recent phenomenon and accounts for a mere 3.5% of retail. Given the prevailing FDI restrictions, foreign players primarily operate through the franchise model or in the wholesale (cash-and-carry) segment.

Regulatory scenario

FDI up to 100% is allowed under the automatic route in cash-and-carry wholesale trading and export trading. FDI up to 51%, with prior government approval, has also been recently permitted in retailing of 'single-brand' products.

[4] *The US$ value is an approximation; the currency conversions have been performed on the basis of Rs 45 = US$1*

The government is likely to adopt a calibrated approach, spread over a period of two to three years, to further open up the industry to foreign investment. The government has also announced its plan to amend the Shops and Establishments Act, 1948 to facilitate modern trade and reduce over-legislation and state intervention.

Recent developments and industry outlook

Many large Indian conglomerates and business houses are expressing strong interest or making significant headway in the retail sector. Reliance's recent announcement of an initial investment of US $750 million for its retail foray is just one example. Other key Indian players like the Tata Group, ITC, the Birla Group as well as big players in associated industries such as real estate and textiles are also making substantial investments.

With the easing of FDI restrictions in 'single-brand retailing', international retailers are proposing to enter the Indian market in a big way.

The organised retail segment is estimated to grow at more than 30% annually and cross US$ 20 billion by 2010. Food and grocery, apparel, consumer durables and footwear retailing will continue to occupy the highest share of organised retailing in India.

The structure of retailing is also developing rapidly, with malls becoming increasingly common in large as well as small cities.

Health Sciences

The Indian pharmaceutical industry grew at 8% in 2004 - 05 and was worth nearly US$ 12 billion in the year 2005. The domestic pharmaceutical market (globally fourth in volume and thirteenth in value terms) accounts for a little over half of the industry; exports (US$ 3.8 billion) and contract research (US$ 1.8 billion) make up the rest.

The Indian biotechnology industry grew by 37% in 2005 - 06 to US$ 1.4 billion in revenue.

The Indian healthcare industry was worth about US$ 34.9 billion (2004) and is growing at 13% annually. The private healthcare segment is by far dominant, with public health spending accounting for less than 1% of the country's GDP.

Regulatory scenario

The Drug Controller General of India is the Regulator for the pharmaceutical industry being responsible for the approval of new drugs and clinical trials and for setting drug quality standards. Under the Drugs and Cosmetics Act, it also coordinates with and regulates the state drug control authorities. Certain drugs are also subject to price controls imposed by the Ministry of Fertilisers and Chemicals (Drug Price Control Order).

The Department of Biotechnology is the nodal agency for policy-making, promotion of research and development (R&D), international cooperation and manufacturing activities pertaining to biotechnology in the country.

Healthcare services come under the purview of the Union Ministry of Health and Family Welfare. The National Accreditation Board for Hospitals & Healthcare Providers is in the process of evolving a process of accreditation for healthcare facilities.

FDI of 100% is permitted under the automatic route in pharmaceuticals, biotechnology, research services and healthcare services.

Recent developments and industry outlook

As part of its WTO commitments, India has amended its patent laws to recognise product patents with effect from January 2005.

In pharmaceuticals, the export market is expected to grow at 35% annually to over US$ 13.7 billion by 2010. Through M&A deals, leading Indian companies have acquired the capability to exploit the global generics market and India is also becoming an increasingly attractive destination for contract manufacturing, contract research and clinical research for global pharmaceutical companies. The contract research segment is expected to grow to US$ 5 billion by 2010.

The biotechnology industry too has high growth potential; revenues are expected to grow to US$ 5 billion by 2010 on the back of higher domestic consumption and rapid growth in exports.

Buoyed by rising healthcare spending and a growing boom in inbound medical tourism, the healthcare industry size is expected to reach US$ 40 billion by 2012.

Roads

India has one of the largest road networks in the world spanning around 3.8 million kilometres. Roadways account for 87% of passenger traffic and 65% of freight traffic in the country. Over the past few years, road traffic has been growing at 7%-10% and vehicle population at approximately 14% annually.

Regulatory scenario

The Department of Road Transport and Highways, under the Ministry of Shipping, Road Transport and Highways, is responsible for all policy matters relating to national highways. The National Highways Authority of India (NHAI) and the state-level departments of highways or public works departments are responsible for national and state highways respectively.

The government is encouraging the participation of the private sector in road infrastructure projects by providing incentives, such as tax exemptions and duty-free import of road-building equipment. FDI upto 100% under the automatic route is permitted in roads and highways, toll roads, vehicular bridges and road transport services.

Recent developments and industry outlook

Recognising the critical importance of expanding and strengthening the national highway network, the Government launched the National Highways Development Project (NHDP) in 1999. NHDP is being implemented in multiple phases. In Phases I and II, about 14,300 kilometres of national highways are being converted into four-lane or six-lane highways; in Phase III (kicked off in 2005) about 10,500 kilometres of national highways are to be upgraded to four-lane dual carriageways.

NHDP is being funded through various mechanisms budgetary allocation from the government, loan assistance from multilateral agencies (such as the World Bank, Asian Development Bank and Japanese Bank for International Cooperation) and private sector participation.

The government is considering upgrading 23,000 kilometres of single lane highways to two-lane highways and also the accelerated development of roads in the north-eastern region. The government has also launched the Pradhan Mantri Gram Sadak Yojna, which involves providing good quality road connectivity to rural areas. The project will involve new road construction of 368,000 kilometres and upgradation of 370,000 kilometres of roads.

Ports

India is presently ranked 17th in the maritime nations of the world. About 95% by volume and 70% by value of the country's trade is carried on through maritime transport. The country's coastline comprises 12 major ports (Chennai, Ennore, Haldia, Paradip, Kandla, Kochi, Kolkata, Marmagao, Mumbai, New Mangalore, Tuticorin and Visakhapatnam) and 187 minor and intermediate ports.

The total traffic handled by major ports increased by 10.3% to 423.4 million tonnes in 2005 - 06, while container traffic increased by 12.9%. The overall capacity utilisation of these ports was 96.5% in 2004 - 2005.

Regulatory scenario

The Department of Shipping, under the Ministry of Shipping, Road Transport and Highways, has the primary responsibility for development and management of the country's maritime infrastructure. The principal legislations governing Indian ports are The Indian Ports Act, 1908 and The Major Ports Trusts Act, 1963.

Major ports are governed by port trusts while the administration of minor ports is the responsibility of the respective state governments. With the entry of private sector players into port operations, the power to fix and revise tariffs has been entrusted to an independent authority - the Tariff Authority for Major Ports.

FDI up to 100% under the automatic route is permitted in the construction and maintenance of ports and harbours, maritime transport services and internal waterways transport services.

The Department of Shipping is also planning to enact a Shipping Trade Practices Act, which is presently in the draft stage.

Recent developments and industry outlook

The government has formulated a draft maritime policy for sprucing up the maritime infrastructure and creating a framework to facilitate public and private investments, promote competition and enhance efficiencies.

The Government has launched the National Maritime Development Programme involving an investment of nearly US$22 billion. The programme comprises 276 projects at major ports and 111 projects in shipping and inland water transport sectors.

The total port traffic is expected to increase at 6.6% CAGR to reach 705.8 million tonnes by 2013 - 14. Simultaneously, the capacity of ports is also expected to be upgraded to 917.6 million tonnes.

Real Estate

Residential sales account for more than 75% of the total real estate market in value terms. There is scope for over 400 township projects of a population of 0.5 million each over the next five years spread over 30-35 cities.

There has been a sharp increase in demand for office space which over the next three years is expected to be in excess of 70 million square feet in the top seven cities. The IT and BPO sectors account for 70% of the total office space requirement. Supply must increase by 55 million square feet each year to keep pace with the growing demand.

There has also been a sharp rise in business and tourism related travel; the first five months of 2006 saw a 14% increase in foreign tourist arrivals compared to the same period last year.

Regulatory scenario

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

- Township, housing, built-up infrastructure and the construction-development projects
- Hotel and tourism
- Setting up/ development of industrial park/ model town/ SEZ
- Construction and related engineering services

Corporate tax exemptions of up to 100% are available for projects like industrial parks, SEZs, housing projects meeting certain conditions.

Recent developments and industry outlook
The sector is currently at the forefront of the government's agenda and has assumed growing importance with the recent opening of the sector to foreign investment. SEBI has also recently approved introduction of real estate mutual funds (REMFs) which is a positive move forward and in line with global best practices followed by mature real estate/security markets.

Growing residential demand has created an estimated shortage of 22.4 million dwelling units, and approximately 5.7 million housing units would have to be completed each year up to 2030 to achieve equilibrium.

The current boom in the hospitality segment has resulted in existing hotels increasing their capacity and international hotels and service apartment chains establishing their operations in India. By 2020, India is expected to be a leading tourist destination in South Asia and demand for hospitality-focused real estate during 2005 - 09 is estimated to require a capital investment of US$ 8-9 billion.

Automotive

The Indian automotive industry, worth over US$ 25 billion in 2004 - 05, comprises two segments - automobiles (about US$ 16 billion) and auto components (about US$ 9 billion).

The automobiles segment in turn comprises passenger vehicles, commercial vehicles and two and three wheelers. The segment has grown at nearly 16% CAGR in volume over the past four years to 9.7 million vehicles in 2005 - 06 of which exports have accounted for a steadily increasing share from 3.4% of total vehicles sold in FY2002 to 8.3% in FY2006.

The auto components segment comprises the Original Equipment Manufacture (OEM) market, the replacement market and exports. The auto components segment overall has grown at nearly 20% CAGR in value terms over the past four years to US$ 9.8 billion in 2005 - 06. As in automobiles, exports have accounted for a steadily increasing share. The industry is quite fragmented, with more than 400 players, including several global ones.

Regulatory scenario
Setting up operations is easy and does not require any industrial license. FDI of 100% under the automatic route is allowed; and if a unit is set up in an SEZ, it is entitled to several fiscal benefits. Besides, most state governments offer additional incentives to units set up in their respective states.

Recent developments and industry outlook
Almost all the major passenger car manufacturers are expanding their capacities to

meet an expected double-digit growth in domestic demand. This would involve an aggregate investment of about US$ 2.6 billion.

Auto component companies in the US, Europe and Japan, are under tremendous pressure to cut costs, and are looking for low-cost production bases to outsource components. Leading Indian players are snapping these up to acquire direct access to global clientele and latest technology and to have synergistic global operations.

The automobiles and auto components segments are expected to grow at 11% CAGR in volume terms and 15% CAGR in value terms respectively by 2010 - 11. The growth rate in exports is expected to be maintained with increased outsourcing to India. India's share in total global outsourcing is expected to more than triple to 6.7% by 2015.

B. Investment Climate and Foreign Trade

B. 1 Foreign Investment Framework

The FDI regime has been progressively liberalised during the course of the 1990s (particularly after 1996) with most restrictions on foreign investment being removed and procedures simplified. With limited exceptions, foreigners can invest directly in India, either wholly by themselves or as a joint venture.

Today, there are very few industries where foreign investment is prohibited. Moreover, investment ceilings, which are applicable in certain cases, are gradually being removed.

Industrial Policy

The Industrial Policy Resolution, 1956 and the statement on the Industrial Policy, 1991 provide the basic framework for the overall industrial policy of the government.

Industrial Licensing

The requirement of obtaining an industrial license for manufacturing is now limited only to the following areas:

- Industries reserved for the public sector.
- Five industries of strategic, social or environmental concern (alcohol, tobacco, aerospace and defence equipment, industrial explosives and hazardous chemicals).
- Manufacture of items reserved for the small-scale-sector by non-small-scale industrial units or units in which foreign equity is more than 24%.

All other industries are exempt from licensing, subject to certain locational restrictions in metropolitan areas.

Foreign Investment Policy

India welcomes FDI in virtually all sectors, except those of strategic concern such as defence (opened to a limited extent), railway transport and atomic energy, where the existing and notified sectoral policy does not permit FDI beyond a certain ceiling.

B. 2 Economic Policies and Incentives for Foreign Investment

Features of the foreign investment policies and incentives

- No government approval required for FDI in virtually all sectors/activities, except for a small negative list notified by the government.

- Government has notified 'Sector Specific Guidelines for FDI' wherein investments up to specified sectoral caps are covered under the automatic route, with a few exceptions.
- FIPB considers proposals for foreign participation that do not qualify for automatic approval.
- Decisions on all foreign investment proposals are usually taken within 30 days of submitting the application.
- Free repatriation of capital investment and profits thereon is permitted, provided the original investment was made in convertible foreign exchange.
- Use of foreign brand names/trademarks for the sale of goods in India is permitted.
- Indian capital markets are open to FIIs.
- Indian companies are permitted to raise funds from international capital markets.
- Special investment and tax incentives are given for exports and sectors such as power, electronics, software and food processing.
- 'Single window' clearance facilities and 'investor escort services' are available in various states to simplify the approval process for new ventures.

Foreign Direct Investment

The government permits FDI on an automatic basis, except with respect to a small negative list comprising the following:

- Proposals involving a foreign collaborator who has an existing venture/tie-up in India in the same field (except in the IT and mining sector), and investments made by international financial institutions such as the Asian Development Bank, International Finance Corporation, Commonwealth Development Corporation and Deutsche Entwicklungs Gescelschaft.
- Proposals falling outside notified sectoral policy/caps.

Proposals for investment in public sector units, as also for EOU/EPZ/EHTP/STP units qualify for the automatic approval route subject to satisfaction of certain prescribed parameters.

Proposals for foreign investment, which are not covered under the automatic approval route, are considered for approval by the government.

Foreign Investment Promotion Board (FIPB)
FIPB is a specially empowered board chaired by the Secretary, MoF, set up specifically for expediting the approval process for foreign investment proposals.

Proposals for FDI may be sent to the FIPB Unit, Department of Economic Affairs, MoF or through any of India's diplomatic missions abroad. FIPB has the flexibility to examine all proposals in totality, free from predetermined parameters or procedures.

Recommendations of FIPB in respect of proposals falling in the non-automatic route and involving an investment of US$ 130 million (equivalent of Rs 6 billion) or less are considered and approved by the Finance Minister. Projects with an investment greater than this value are submitted by FIPB to the Cabinet Committee on Economic Affairs for approval.

Foreign Technology Agreements
Foreign technology collaborations include the following:

- Technical know-how fees.
- Payment for designs and drawings.
- Payment for engineering services.
- Other royalty payments.

RBI accords automatic approval to foreign technology agreements in all industries, within certain prescribed monetary limits.

Foreign Portfolio Investment
FIIs must register themselves with SEBI and comply with the exchange control regulations of RBI.

Foreign pension funds, mutual funds, investment trusts, asset management companies, nominee companies and incorporated/institutional portfolio managers or their power of attorney holders are allowed to invest in India as FIIs. FIIs are allowed to invest in securities traded in the primary and secondary capital markets in India under the portfolio investment scheme. These securities include shares, debentures, warrants, units of mutual funds, government securities and derivative instruments.

Certain investment limits are prescribed in the FII Guidelines and the RBI Regulations to regulate the investment by FIIs. However, these investment restrictions do not apply to the investments made by an FII through offshore funds, GDRs, ADRs or Euro-convertible Bonds.

Registration Eligibility
FII Guidelines require FIIs to meet certain qualifying conditions for registration. SEBI also examines whether the grant of registration is in the interest of the development of the Indian securities market.

Registration of Sub-accounts
Besides entities that are eligible as FIIs, other foreign investors are also eligible for

registration as sub-accounts. The sub-accounts may be (i) collective investment funds and institutions; (ii) proprietary funds; or (iii) foreign corporations and individuals.

ADRs / GDRs / FCCBs
Qualifying Indian companies are allowed to raise equity capital overseas through the issue of ADRs/GDRs/FCCBs. Where an issue of ADRs, GDRs or FCCBs by a company is likely to increase the permissible investment limits of FDI under the automatic route, or where such an investment is made in the form of a project that requires government approval, the company must seek approval from the FIPB.

Preference Shares
Another way to invest in India is through the issue of preference shares. Foreign investment through convertible preference shares is treated as FDI. These investments may be made through the automatic route or the government route.

Investment by Non-resident Indians
NRIs can invest on a non-repatriable basis in the shares or convertible debentures of an Indian company. These investments do not require FIPB approval. NRIs cannot invest in companies that are engaged in certain financial services activities or in agricultural/plantation activities. While the capital is non-repatriable, the dividends and interest income can be remitted as current account transactions.

Foreign Exchange Controls

Foreign Exchange Policy
Since 1991, the country's foreign exchange reserves have surged from US$ 2 billion to approximately US$ 163 billion in June 2006.

Prior to 1999, India had stringent exchange control regulations under the Foreign Exchange Regulation Act, 1973 (FERA). The government, in 1999, replaced controls under FERA with regulations under the FEMA.

With the introduction of FEMA in 1999, the objective of the government shifted from the conservation of foreign exchange to promoting an orderly development and maintenance of the foreign exchange market in India.

Current Account Transactions
The rupee is fully convertible for trade and current account purposes. Except for certain specified restrictions where RBI approval is necessary, foreign currency may be freely purchased for trade and current account purposes.

Capital Account Transactions
Capital account transactions are not permitted unless they are specifically allowed and prescribed conditions are satisfied. Capital account transactions specifically allowed include the following:

- Investment in India by a person resident outside India.

- Acquisition and transfer of immovable property in India by a person resident outside India.
- Guarantee by a person resident outside India in favour of, or on behalf of, a person resident in India.
- Import and export of currency/currency notes into/from India by a person resident outside India.
- Deposits between a person resident in India and a person resident outside India.
- Foreign currency accounts in India of a person resident outside India.
- Remittance outside India of capital assets in India of a person resident outside India.
- Remittances abroad that require prior approval arrangements, such as a joint venture and technical collaboration agreements.
- Remittance of interest, dividends, service fees, royalties, repayment of overseas loans and so forth.

The provisions in respect of repatriation of foreign exchange for select purposes have been summarised below.

Repatriation of Capital: Foreign capital invested in India is generally allowed to be repatriated along with capital appreciation, if any, after the payment of taxes due on them, provided the investment was approved on a repatriation basis.

Royalties and Technical Know-how Fee: Indian companies that enter into technology transfer agreements with foreign companies are permitted to remit payments towards know-how and royalty under the terms of the foreign collaboration agreement, subject to limits.

Technical Service Fee: Companies can hire the services of foreign technicians and make remittances for technical service fees, subject to certain conditions, regardless of the duration of engagement of foreign nationals in any calendar year.

Dividends: Profits and dividends earned in India are repatriable after the payment of taxes due on them. No permission of RBI is necessary for effecting remittance, subject to compliance with certain specified conditions.

Interest: Remittances towards interest on bonds, debentures, government securities, bank deposits in India and dividends on the units of the Unit Trust of India to individuals permanently resident outside India are permitted.

Other Remittances: No prior approval is required for remitting profits earned by Indian branches of companies (other than banks) incorporated outside India to their Head Offices outside India. Remittances of the winding-up proceeds of a branch of a foreign company in India are permitted, subject to RBI approval. In addition, sundry remittances are allowed for items like gifts, repair charges for imported machinery, maintenance and legal expenses.

External Commercial Borrowings (ECBs)
Debts raised in foreign currency fall within the purview of the definition of ECBs, and are regulated by MoF and RBI. ECB can be accessed under two routes, viz., automatic route and approval route.

ECBs up to US$ 500 million have been put under the automatic route subject to the compliance of the ECB policy. ECB can be availed by corporates registered under the Companies Act except for financial intermediaries and must be availed from an internationally recognised source, export credit agencies, suppliers of equipment, foreign collaborators and foreign equity holders (subject to certain minimum equity holding requirements in the borrower's company). ECB proceeds, under no circumstances, can be used for on-lending, investment in capital market, working capital and real estate.

The minimum maturity period of the loan shall be three years for a loan amount less then US$ 20 million, and for ECBs above US$ 20 million and up to US$ 500 million the minimum average maturity period will be five years.

The all-in-cost ceiling for the ECB up to three years and up to five years is six months London Interbank Offered Rate (LIBOR) (in the respective currency in which the loan has been availed) plus 200 basis points. The all-in-cost ceiling for the ECB above five years is six months LIBOR plus 350 basis points.

An empowered committee of RBI decides all cases falling outside the purview of the automatic route.

B.3 Economic Laws and Regulations

Key Economic Laws

- Indian Contract Act, 1872
- Copyright Act, 1957
- Trademarks Act, 1999
- Geographical Indications of Goods Act, 1999
- Indian Patents Act, 1970
- Designs Act, 2000
- Industrial Disputes Act, 1947
- Maternity Benefit Act, 1961
- Payment of Bonus Act, 1965
- Payment of Gratuity Act, 1972
- Workmen's Compensation Act, 1923
- Industrial Employment (Standing Orders) Act, 1946
- Minimum Wages Act, 1948

Key Economic Laws
• Payment of Wages Act, 1936
• The Factories Act, 1948
• Employees Provident Fund and Miscellaneous Provisions Act, 1952
• Monopolies and Restrictive Trade Practices Act, 1969
• Competition Act, 2002
• Consumer Protection Act
• The Negotiable Instruments Act, 1881
• The Sale of Goods Act, 1930
• Arbitration and Conciliation Act, 1996

Indian Contract Act, 1872 (ICA)

The Indian law of contract is based on the common law principles of contract and is codified as the ICA. ICA has borrowed extensively from the provisions of codes governing the law of contracts in other countries.

Through subsequent amendments, the provisions concerning certain specific forms of contract including contract of partnership, contract of carriage and contract for sale of goods were removed from ICA and enacted into a separate legislation.

Intellectual Property Rights Protection

The laws relating to intellectual property in India are still in the process of transition and are being harmonised with corresponding laws in developed countries.

As a signatory to GATT and trade-related aspects of intellectual property rights (TRIPS) agreements in the capacity of being a member of WTO, India is required to lay down minimum norms and standards with respect to the following areas of intellectual property:

- Copyrights and other related rights
- Trademarks
- Geographical indications
- Patents
- Industrial designs

Copyrights
India's copyright law, laid down in the Indian Copyright Act, 1957 as amended by Copyright (Amendment) Act, 1999, fully reflects the Berne Convention on Copyrights, to which India is a party.

Additionally, India is party to the Geneva Convention for the Protection of Rights of Producers of Phonograms and to the Universal Copyright Convention. India is also an active member of the World Intellectual Property Organisation (WIPO), Geneva.

As per the Copyright Act, 1957, copyright subsists in original literary, dramatic, musical and artistic work or a cinematographic film or a sound recording.

The copyright law in India has been amended from time to time to keep pace with the changing requirements. The amendments made to the copyright law have ushered in comprehensive changes and brought it in line with the new developments in satellite broadcasting, computer software and digital technology.

Several measures have been adopted to strengthen and streamline the enforcement of copyright protection. These include setting up of a Copyright Enforcement Advisory Council, training programmes for enforcement officers and setting up special police cells to deal with cases relating to the infringement of copyright.

Trademarks

To provide for the registration and protection of trademarks and for the prevention of the use of fraudulent trademarks, the Trade and Merchandise Marks Act was passed in 1958. Subsequent to a comprehensive review of the same, a bill to repeal and replace the 1958 Act was passed by the parliament in 1999. The Trademarks Act, 1999 provides for the registration of trademarks for services and goods, including collective marks, and for the assignment and transmission of trademarks.

There is provision for an appellate board for speedy disposal of appeals, rectification of applications and simplification of procedures for the registration of the registered user and for enlarging the scope of the permitted use of trademarks and prohibition on the use of someone else's trademarks as part of corporate names or names of business concerns.

The Act also provides for the incorporation of other provisions like amendment in the definition of 'marks', provision for filing of a single application for registration in more than one class, a 10-year period for the registration and renewal of trademarks and for making the trademarks offence cognisable. The Trademarks Rules, 2002 were notified on February 26, 2002.

The Controller General of Patents, Trademarks and Designs has been appointed by the government to administer the various provisions of the Trademarks Act. As per the provisions of the Act, and with a view to fulfill the obligations of the WTO agreements and the other treaties entered into by India, the Act grants the holder of a foreign trademark the right to register a trademark in India.

Geographical Indications of Goods

The Geographical Indications of Goods (Registration and Protection) Act, 1999 (GI Act) was passed by the Parliament in December 1999 and the Geographical Indications of Goods (Registration and Protection) Rules, 2002 were notified on March 8, 2002.

The GI Act has been introduced to conform with the TRIPS regime. It seeks to provide for the registration and better protection of geographical indication relating to goods in India, and is designed to protect the use of such geographical indication from infringements by others and to protect the consumers from confusion and deception.

Patents

The Indian Patents Act, 1970 provides for the grant, revocation, registration, license, assignment and infringement of patents in India. Any infringement of a patent is punishable under the terms of this Act.

The Indian Patents Act, 1970 and the Patent Rules, 1972 were amended by the Patents (Amendment) Act and Rules, 1999. The main objective of these amendments was to grant product patents for inventions relating to drugs and medicines and to outline the procedure to deal with the claims made in the applications filed on or after January 1, 1995.

To harmonise the law pertaining to patents and other forms of intellectual property, and to fulfill its obligations under the WTO agreement, India has become an active party to the International Convention for the Protection of Industrial Property (Paris Convention), GATT and TRIPS agreements.

Industrial Designs

The Designs Act, 2000, passed to give recognition to the obligations under the WTO agreements, encourages and protects those who produce new and original designs and seeks to enhance industrial development and competitive progress. The purpose of the Designs Act is to protect the novel designs made with the object of applying the design to particular articles to be manufactured and marketed commercially for a specific period of time, from the date of registration.

The Controller General of Patents, Designs and Trademarks appointed under the Trade and Merchandise Marks Act, 1958 is the Controller of Designs and is responsible for administering the various provisions of the Act.

Labour Laws

India is a member of the International Labour Organisation and complies with the conventions that it has ratified. It has enacted comprehensive legislations to provide a good working environment for the labour and to protect their interests.

In the following paragraphs, the key labour laws applicable to employers and employees in India have been outlined.

Industrial Disputes Act, 1947 (IDA)

IDA provides for the investigation and settlement of industrial disputes or certain other matters in an industrial establishment relating to lockouts, lay-offs, retrenchment, etc. It provides the machinery for the conciliation and adjudication of disputes or differences between the employees and the employers, among workmen and among different employers.

Further, IDA prescribes penalties for any person who indulges in any unfair labour practices.

Maternity Benefit Act, 1961 (MBA)
MBA regulates the employment of women in certain establishments for a prescribed period before and after childbirth and provides certain other benefits, including leave to a woman who has undergone miscarriage, illness arising from pregnancy, delivery and/or premature birth of a child.

MBA prescribes penalties for the contravention of its provisions by the employer.

Payment of Bonus Act, 1965 (PBA)
PBA provides for the payment of bonus to persons employed in certain establishments on the basis of profits or on the basis of production or productivity, and for matters connected therewith.

PBA provides for the appointment of inspectors by the government by notification. These inspectors can call upon the employer to furnish any such information that may be considered necessary. They can further ask the employer to submit books and registers and other documents relating to the employment of persons or the payment of salary or wages or bonus.

Penalties are prescribed for the contravention of the provisions of the PBA or rules, or failure to comply with the directions or requisitions made under PBA.

Payment of Gratuity Act, 1972 (PGA)
PGA provides for a scheme for the payment of gratuity to all employees getting wages to do any skilled, semi-skilled or unskilled, manual, supervisory, technical or clerical work, whether the terms of such employment are express or implied, and whether or not such a person is employed in a managerial or administrative capacity.

Gratuity is payable to an employee on his retirement/resignation, superannuation, termination on account of death or disablement due to accident or disease or retirement.

PGA prescribes conditions under which an employer can deny payment or forfeit the gratuity of an employee. It also prescribes penalties and prosecutions for the contravention of the provisions of PGA.

Workmen's Compensation Act, 1923 (WCA)
The object of WCA is to compensate an employee for any injury suffered during the course of his employment. WCA provides that compensation shall be paid to a workman in the case of his surviving an injury and to his dependants in the case of his death.

WCA also prescribes conditions under which compensation may be denied to an employee.

Industrial Employment (Standing Orders) Act, 1946 (IEA)
IEA requires employers in industrial establishments to clearly define the conditions of employment to their workers by issuing standing orders/service rules relating to the matters set out in the schedule of IEA. The standing orders are to be certified by the certifying officer appointed under IEA.

The Industrial Employment (Standing Orders) Central Rules, 1946 provides for model standing orders, with respect to the classification of workmen, holidays, shifts, payment of wages, leaves, termination, etc.

Minimum Wages Act, 1948 (MWA)
MWA seeks to determine the minimum rates of wages in certain employments specified in the Schedule of the Act. MWA applies to any person who is employed for hire or reward to do any work in a scheduled employment, and includes an outdoor worker to whom any articles or materials are given for doing some work either at home or at any other premises.

Payment of Wages Act, 1936 (PWA)
PWA seeks to regulate the payment of wages to certain classes of employees in an industry. It seeks to ensure that the wages payable to the employees covered under PWA are disbursed by the employers within the prescribed time limit and that no deductions, other than those authorised by law, are made by the employers.

In addition to the above Acts, several states have enacted Shops and Establishment Acts which regulate the working hours, prescribe minimum standards of working conditions and provide for overtime and leave salary payments to workers in certain categories of shops and other establishments.

The recent years have seen many companies successfully using the voluntary retirement scheme in an effort to restructure operations or to exit from a particular line of business. Retraining schemes for workers have been used to increase productivity and competitiveness.

Factories Act, 1948
The Factories Act extends to the whole of India and it is the principal legislation that governs the health, safety and welfare of workers in factories. Many amendments were made with the aim of keeping the Act in tune with developments in the field of health and safety. However, it was not until 1987 that the elements of occupational health, safety and prevention and protection of workers employed in hazardous processes got truly incorporated in the Act.

The Act also contains regulations for the functioning of factories and detailed procedure relating to inspection, registration, licensing, etc. of factories.

Employees Provident Fund and Miscellaneous Provisions Act, 1952 (EPFMPA)
EPFMPA seeks to ensure the financial security of the employees in an establishment by providing for a system of compulsory savings. A provident fund, as required to be established under EPFMPA, is a contributory fund created to secure the future of the employees after retirement. Employees are also allowed to withdraw a part of their provident fund before retirement for certain specified purposes.

The government has prescribed various penalties at prescribed rates for any default, which the employer may make in connection with the payment of any contribution, arrears, accumulations, administrative charges, to the fund and/or has also prescribed imprisonment.

Anti-Trust Regulations

In line with global norms and to prevent monopolies from creating restraints on trade or commerce and reducing competition in India, the government has evolved an anti-trust regulatory framework that revolves principally around the following legislations:

- Monopolies and Restrictive Trade Practices Act, 1969, which is in the process of being replaced by the Competition Act, 2002 (No. XII of 2003)
- Certain provisions under the Companies Act, 1956
- Consumer Protection Act, 1986

Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act)
The Competition Act received the assent of the President on January 13, 2003 and was published in the Gazette on January 14, 2003. The Act intends to repeal the MRTP Act. However, as of date, no substantive provision of the Act is in force and the same would come into force as and when notified by the central government. As of now, the MRTP Act is still in force.

The MRTP Act governs the activities/practices of all industrial undertakings being such enterprises, which are engaged in the production, storage, supply or distribution of articles/goods either directly or indirectly through any of its units or divisions. However, government undertakings do not come under the purview of the MRTP Act. It encompasses within its ambit, essentially the following types of prohibited trade practices, namely, ‘restrictive trade practice’, ‘unfair trade practice’ and ‘monopolistic trade practice’.

Under the MRTP Act, the regulatory body is the Monopolies and Restrictive Trade Practices Commission. The Commission is assisted by the Director General of Investigation and Registration who is responsible for providing assistance to it in carrying out investigations, maintaining a register of agreements, which are required to be regulated under the Act and undertaking carriage of proceedings during the enquiry before the Commission.

There are certain provisions in Part IV of the Companies Act, 1956 regulating the acquisition and transfer of shares of a body corporate owning any undertaking to which the provisions of Part A of Chapter III of the MRTP Act would be applicable. These provisions intend to prevent acquisition or takeover of companies to further concentration of economic power. Accordingly, these provisions stipulate that certain types of acquisitions would require prior approval of the central government.

Competition Act

The Competition Act, which shall replace the MRTP Act, seeks to achieve the following objectives:

- Promote and sustain competition in markets.
- Protect the interest of consumers.
- Ensure freedom of trade.
- Provide for the establishment of Competition Commission of India (CCI).

The major provisions of the Competition Act relate to Prohibition of Anti-Competitive Agreements, Prohibition of Abuse of Dominant Position, Regulation of Combinations, Establishment, Powers, Functions and Duties of CCI.

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Consumer Protection Act (CP Act)

The CP Act is a legislation, which has been enacted for the protection of consumer interest. It provides for the establishment of consumer councils and other authorities to settle consumer disputes. Under the terms of the CP Act, an entity, which provides any goods/services in India, is required to avoid any trade practice that may be classified as 'unfair' or 'restrictive', as defined under the Act.

The CP Act aims to regulate the activities of a 'manufacturer' or 'service' provider to ensure that the consumer does not suffer from defective goods and/or deficiency of services.

This Act contains provisions for district, state and national consumer disputes redressal fora to adjudicate over claims, complaints and disputes, which result under the provisions of the CP Act.

Negotiable Instruments Act, 1881 (NI Act)

The law relating to promissory notes, bills of exchange, cheques and other negotiable instruments is codified in India under the NI Act. The main object of the NI Act is to legalise the system by which the instruments contemplated by it could pass from hand to hand through negotiations like any other goods.

The Act provides for the liability of an agent, legal representative, drawer, drawee, maker and acceptor of a bill, endorser, holder in due course, suretyship, etc. Detailed provisions have been made in the Act concerning presentment, payment, interest, discharge from liability, notice of dishonour, noting and protest, reasonable time for payment, acceptance and payment for honour and reference in case of need, compensation, special rules of evidence, providing for certain presumptions and estoppels, cross cheques, bills in sets, etc.

Sale of Goods Act, 1930

The Sale of Goods Act is complimentary to the Contract Act. The basic provisions of the Contract Act apply to the contract of sale of goods also. The basic requirements of a contract, i.e. offer and acceptance, legally enforceable agreement, mutual consent, parties competent to contract, free consent, lawful object, consideration, etc. apply to the contract of sale of goods.

A contract of sale of goods is a contract whereby the seller transfers or agrees to transfer the property (ownership) in the goods to the buyer for a price. A sale is an executed contract, i.e. there is a contract plus conveyance. In other words, the property in the goods is transferred from the seller to the buyer.

Certain stipulations are essential for the main purpose of the contract of sale of goods. These go to the root of the contract and non-fulfilment will mean loss of the foundation of contract. These are termed as 'conditions'. Other stipulations, which are not essential, are termed as 'warranty'. These are collateral to the contract of sale of goods. A contract cannot be avoided for the breach of warranty, but the aggrieved party can claim damages.

The Sale of Goods Act requires that the goods transferred by the seller to the buyer must be ascertained and there should be an intention of the seller to pass such goods to the buyer. The Act also deals with transferring the title in the goods by a person who is not the owner of the goods.

The Act casts various duties and grants certain rights on both buyer and seller, e.g. it is the duty of the seller to deliver the goods and of the buyer to accept and pay for them in accordance with the terms of the contract of sale.

If goods are sold and property is transferred to the buyer and he refuses to pay for the same, the only remedy with the seller is to approach the court. The seller has no right to take forceful possession of goods from buyer, once the property in goods is transferred to him. However, the Act gives some rights to the seller if his dues are not paid and the goods are not transferred to the buyer.

An elementary principle of law is that a buyer or a seller who is responsible for a breach of a contract is bound to pay compensation for any loss or damage caused to the other party, provided that the loss or damage arose in the usual course of things from such a breach or was such that the parties knew when they made the contract that such loss or damage was likely to result from such breach of it. The Sale of Goods Act helps buyers to obtain redress when their purchase goes wrong.

Arbitration and Conciliation Act, 1996

The Arbitration and Conciliation Act, 1996 has been enacted to replace three previous laws dealing with the various aspects of arbitration. This Act is essentially based on the Model Law on International Commercial Arbitration adopted by the United Nations Commission on International Trade Law (UNCITRAL) in 1985. The important feature of the UNCITRAL laws and rules are that they have harmonised concepts on the arbitration and conciliation of different legal systems of the world. It has consolidated into one statute, the law relating to domestic arbitration, international commercial arbitration, enforcement of foreign arbitral awards and conciliation. It allows the contracting parties to decide upon the venue/place and procedure of the arbitration proceeding.

B.4 Special Investment Considerations

Special Economic Zones (SEZ)

Overview
FTP provides for the setting up of SEZs in the country with a view to enable an internationally competitive and hassle-free environment for exports. Units may be set up in an SEZ for manufacture, trading, reconditioning and repair or for services activity.

The policy provides for the setting up of SEZs in the public, private or joint sectors or by state governments. The central government has also converted some of the existing EPZs/ FTZs (Free Trade Zones) into SEZs to give momentum to this sector. There are 14 functional SEZs in India which include multi-product as well as product-specific SEZs.

More than 150 SEZs have been approved by the government and are under various stages of establishment. Some of the SEZs approved for setting up are located at Dronagiri (Maharashtra); Kulpi (West Bengal); Paradip (Orissa); Bhadohi, Kanpur and Greater Noida (Uttar Pradesh); Kakinada (Andhra Pradesh); Hassan (Karnataka); and Positra, Dahej, Mundra, Vanj-Surat, Hazira-Surat and Icchapur-Surat (Gujarat) on the basis of the proposals received from the state governments. Some of these SEZs are in the initial stages of development while some are ready for operation.

The Ministry of Commerce has estimated that SEZs would generate direct and indirect employment for 500,000 people by December 2007. FDI of US$ 5-6 billion is also expected by the end of December 2007 in infrastructure development of the SEZs and in setting up of units in the Zones.

SEZ Scheme
The SEZ scheme has the following salient features:

- Designated duty-free enclave to be treated as foreign territory for trade operations and duties and tariffs.
- Permitted activities are manufacture of goods, services, production, processing, assembling, reconditioning, re-engineering, packaging, trading, etc.
- SEZ units to be positive net foreign exchange earners.
- Duty-free goods to be utilised within the approved period of five years.
- Performance of SEZ units to be monitored by a unit approval committee consisting of the Development Commissioner and the Customs Authority.

Incentives for SEZ Units

- Duty-free import of capital goods (including second-hand capital goods), raw materials, consumables and spares.
- Duty-free procurement of capital goods (including second-hand capital goods), raw materials and consumable spares from the domestic market.
- Exemption from payment of central sales tax on interstate purchases from the domestic market.
- Exemption from service tax for services provided to a unit (including a unit under construction) of an SEZ.
- Subject to the achievement of positive net foreign exchange earnings, SEZ units permitted to sell production in the domestic tariff area (DTA) on payment of full customs duty, subject to the import policy in force.
- Certain supplies in DTA such as supplies to other EOU/ STP/ EHTP/ BTP/ SEZ units, holders of special import licences, sale of ITA bound items etc. (payment for which is received in Indian rupees) would be counted towards the achievement of positive net foreign exchange earnings.
- Full freedom for subcontracting.
- Subcontracting of part of production permitted abroad.
- No routine examination by the customs of export and import cargo.
- Re-export imported goods found defective, goods imported from foreign suppliers on loan basis without Guaranteed Receipt waiver under intimation to the development commissioner.
- Facility to retain 100% of the foreign exchange receipts in the export earner's foreign currency account.

Incentives for Developers of SEZs

- No net foreign exchange earning requirement / export obligation imposed on SEZ developers.
- Procure goods from the DTA without payment of duty or import specified goods without payment of customs duty as may be notified by the government for the development of the SEZ.
- Full freedom in allocation of developed plots to approved SEZ units on a purely commercial basis.

- Full authority to provide services like water, electricity, security, restaurants and recreation centres on commercial lines.
- Facility to develop a township within the SEZ with residential areas, markets, playgrounds, clubs and recreation centres adhering to the SEZ norms.
- Exemption from service tax on input services and output services (provided prescribed export of services criteria is met).
- Exemption from central sales tax.

For information on direct tax incentives, kindly refer to section C4.

Institutional Framework

The development commissioner/ approval committee of the SEZs has been entrusted with the responsibility of granting approvals for setting up units in SEZs. Post-approvals, wherever required, are also given by the development commissioner of SEZs.

100% Export-Oriented Units (EOU)

With a view to encouraging exports, in addition to the SEZ scheme, the government has formulated the EOU scheme. Such units may be set up as 100% EOUs outside SEZs.

FDI in EOUs qualifies for the automatic approval route, subject to its conforming with existing guidelines for FDI. The units need to be positive net foreign exchange earners.

The following incentives are available for EOUs:

- Exemption from customs duty on industrial inputs and capital goods including second-hand capital goods (without age limit).
- Local procurement of inputs and capital goods (including second-hand capital goods) exempted from the payment of excise duty.
- Credit of service tax paid on input services.
- Reimbursements of central sales tax paid on interstate purchases.
- DTA sale of goods or rendering of services is permitted up to 50% free on board value of exports / or 50% of foreign exchange earned subject to fulfillment of other obligations of the scheme.
- Certain supplies to the DTA counted towards fulfillment of positive net foreign exchange earner.

Similar incentives are offered to units engaged in the field of biotechnology, electronics and software, which can be set up under the BTP, EHTP or STP schemes.

State-level Incentives

State governments have proactively come up with several incentives to encourage investment and attract capital which include the following:

- Special tax incentives.
- Rebate on cost of land.
- Rebate on stamp duty on sale/lease of land.
- Concession in power tariff for new units.
- Self-certification under various Acts.
- Special incentive packages for mega projects.
- Employment subsidies.

Investment Incentives
Various states have incentive schemes to attract investment by financing a certain percentage of the fixed capital cost of a project. These states have designated areas as 'A', 'B' and 'C' according to their level of development. The level of incentives provided by states varies and is generally larger for investments made in backward areas. Further, the terms and ceiling of the incentives vary across states, depending on the nature of industry that the state is trying to promote.

Power tariff incentives
Power tariff incentives are extended by state governments in various ways, such as exemption from the payment of electricity duty, freeze on the tariff charged for new units for a few years after commencement of production, assurance of uninterrupted electricity supply, concessional rates of billing subject to certain conditions and financial incentives for purchase and installation of captive power generation sets.

Other incentives
Some states extend other incentives to small-scale units or priority industries as defined in their industrial policy statements. An indicative list of such incentives is:

- Concessional rate of interest on loans granted by state finance corporations.
- Price preference on goods made by small-scale industries in purchases made by government and semi-government organisations.
- Exemption from the payment of octroi (entry tax) for a certain specified period.
- Preferential allotment of land and sheds in industrial areas to small-scale industries.
- VAT can be deferred in lieu of interest-free loans.

A few states have taken the initiative to streamline the investment approval process by introducing common application forms for various approvals. A 'green channel facility', has been introduced in some states, whereby applications required for clearances will be received and processed through the various institutional offices on a time-bound basis.

Government-owned Industries and Privatisation

Rapid industrialisation has been the basic objective of India's development policy since independence in 1947, when the government adopted several promotional and protective measures to foster industrial growth.

The government now recognises that most industries develop through the enterprise and initiative of private individuals and companies. Consequently, since 1991, to accelerate economic growth and to enhance international competitiveness, the government is taking measures to deregulate trade and industry, dismantle bureaucratic controls, liberalise international trade, privatise the public sector, encourage entrepreneurial activity and technological development and introduce financial sector and trade reforms.

The government has reduced the number of industries reserved for the public sector to the following two industries, which are deemed significant from a security and strategic perspective:

- Atomic energy
- Railway transport

Recently the railways announced opening up of its containerised operations to other private and public sector companies thereby breaking the monopoly enjoyed by its subsidiary Container Corporation of India. Interested companies can now take route-specific or all-India permission by making a one-time registration fee for an operation period of 20 years which is further extendable by another 10 years. These companies would be free to decide the tariff charged to their customers for haulage, terminal handling and ground rent. Further, the companies can exit operations by transferring the permission to another eligible operator with the railways approval.

B.5 Regional and International Trade Agreements and Associations

India has entered into bilateral and regional trading agreements over the years. These agreements besides offering preferential tariff rates on the trade of goods among member countries also provide for wider economic cooperation in the fields of trade in services, investment and intellectual property, etc. Some of the recent prominent trade agreements are India Sri Lanka Free Bilateral Trade Area, India Thailand Free Trade Agreement, and the South Asia Association for Regional Cooperation (SAARC) Preferential Trade Agreement. Most recently, India and Singapore have signed a Comprehensive Economic Cooperation Agreement which is an integrated package of agreements embracing trade in goods, services, investments and economic cooperations in education, science and technology, air services and intellectual property. The agreement which came into effect on August 1, 2005 provides wide-ranging exemptions and reductions on basic customs duty on products imported from Singapore into India.

B.6 Major Trading Partners and Leading Imports and Exports

Trading Partners

The US has replaced the former Soviet Union as India's major export market. Japan is India's largest trading partner in Asia and the third largest trading partner worldwide. Australia is a primary source for supplies of coking coal, pulses, wool and non-ferrous metals.

Foreign Trade Policy (FTP)

FTP announced by the government seeks to complete the process of India's integration with the global economy by the removal of quantitative restrictions. It seeks to provide fresh direction to exports by setting up agricultural export zones, providing special benefits to SEZs and providing various export incentive schemes. The FTP is forward-looking and liberal and is the logical conclusion to India's commitments under the WTO agreement.

It covers duty-free import facility for the service sector and status holders on the fulfillment of certain conditions. It aims to boost the electronic hardware and software industries and the gems and jewelry sector. The policy has brought about radical changes in the various export-oriented schemes and has thus benefited the economy.

Imports

Most goods are freely importable on the payment of a specified customs duty. A small number of goods fall in the prohibited/restricted list of imports. Such restrictions are generally on grounds of national security, health and environmental protection.

There are no quantitative restrictions on the import of capital goods and intermediates including second-hand capital goods and ?restrictions exist only in respect of a few items.

- Import of second-hand capital goods is allowed freely.
- Duty drawback is available for imported raw materials for export production.
- Duty-free import of raw is materials possible for export production in specified conditions.
- Concessional duty rate is available for capital goods under the Export Promotion Capital Goods Scheme.
- Imports from certain countries are permissible at reduced rates.

Raw materials, intermediates and components meant for the manufacture of goods for export can be imported duty-free against an advance license. Input-output norms have been laid down to determine the amount of duty-free import of inputs allowed for specific products to be exported. The issue of a duty-free license under this scheme is subject to the achievement of positive value-addition and export obligations.

New or second-hand (without age limit) capital goods may be imported under the Export Promotion Capital Goods Scheme. These capital goods may be imported at a concessional basic customs duty rate of 5%. However, this concession is subject to an export obligation to be fulfilled over a specified period.

Exports

Export of goods is allowed freely, except for a few restricted items. Exports are the major focus of India's trade policy and are a thrust area in the new economic policy of the country. The export promotion package compares favourably with incentives offered anywhere in the world. It makes a special effort to attract foreign investors to set up EOUs and units in SEZs.

Foreign Trade - Key Statistics

Exports: US$ 79.41 billion (2004-05)

Principal exports: Traditional exports include cotton yarn and textiles, readymade garments, gems and jewelry and agricultural products. However, IT services, engineering products, chemicals, pharmaceuticals and petroleum products are rapidly growing export segments now.

Principal markets for export: Principal markets for exports are the US, UK, Germany, Japan, Italy, France, Netherlands, Belgium, UAE, China, Hong Kong, Singapore and Bangladesh.

Imports: US$ 107.28 billion (2004-05)

Principal imports: Capital goods, crude petroleum and petroleum products, gold, precious and semi-precious stones, chemicals, edible oils, electronic goods and coal.

Principal markets for import: Principal markets for import are the US, UK, Japan, Germany, Belgium, Switzerland, UAE, Saudi Arabia, South Africa, China, Malaysia, South Korea, Singapore, Indonesia and Australia.

Balance of Trade

The performance of India's exports has been excellent during the last three years with acceleration in growth rates. In 2004-05 exports in US dollars terms increased by 24.1% as against 21.1% and 20.2% increases in 2003-04 and 2002-03 respectively. Imports have also shown accelerated growth. In 2004-05 imports grew by 36.9% as against 27.3% in 2003-04 and 19.4% in 2002-03.

In 2004-05 imports of both petroleum and non-petroleum products surged; the former due to the steep rise in international crude prices and the latter due to the strong industrial production and investment. On account of higher growth imports, the trade deficit in 2004-05 nearly doubled from US$ 14.3 billion in 2003-04 to US$ 27.9 billion in 2004-05.

In 2005-06, during the April-October period, exports grew by 22.2% over the corresponding period in the previous year to US$ 51.68 billion. Imports also registered a strong growth of 33.1% over the corresponding period in the previous year to US$ 75.26 billion. The trade deficit was US$ 23.58 billion as against US$ 14.23 billion for the corresponding period for 2004-05.

Tariff Liberalisation

The current trade policy is characterised by rationalised tariff levels and the removal of quantitative restrictions.

There has been a consistent decline in the rates over the past 15 years - from peak rates of 350% in June 1991 to 15% in 2005-06. Most capital goods imports attract a basic customs duty at the rate of 15%. Import duties on equipment are lower for projects in specific sectors. The tariff structure is favourable for companies wanting to import equipment to set up projects in the infrastructure sector.

C. Companies

C.1 Forms of Enterprise

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

- Corporations
- Partnerships
- Sole proprietorships

Corporations incorporated in India and foreign corporations having a presence in India are regulated by the provisions of the Companies Act, 1956, which draws heavily from the Companies Act of the UK. The Registrar of Companies and the Company Law Board (CLB), both working under the Ministry of Company Affairs, have been entrusted with the responsibility of ensuring compliance with the provisions of the Companies Act, 1956. An amendment was passed under the Companies Act through which a National Company Law Tribunal (NCLT) is proposed to be set up to take over the functions being hitherto performed by CLB and to discharge various other functions under the Companies Act.

Major Types of Corporate Forms

Corporations in India may broadly be classified into public and private sector corporations. A private sector corporation can further be classified as a public or private corporation having limited or unlimited liability. A corporation can be limited by shares or by guarantee. In the former, the personal liability of members is limited to the amount unpaid on their shares while in the latter; the personal liability is limited by a pre-decided nominated amount. For a corporation with unlimited liability, the liability of its members is unlimited.

A corporation established for charitable purpose would be allowed to be formed under the provisions of Section 25 of the Companies Act, 1956. The profit generated from the activities is not allowed to be distributed to the shareholders, but must be used for the purpose for which the corporation is established.

Private Corporations

A private corporation* incorporated under the Companies Act, 1956 has the following characteristics:

- Right to transfer shares is restricted.
- Maximum number of shareholders is limited to 50.
- No offer can be made to the public to subscribe to its shares and debentures.
- No invitation or acceptance of deposits from persons other than members, directors or relatives is allowed.

A private corporation is required to have a minimum paid-up capital of Rs 0.1 million (US$ 2,170) with a minimum of two directors and two shareholders.

Public Corporations
A public corporation* is defined as one that is not a private corporation. A subsidiary of a public corporation is also treated as a public corporation. A public corporation is required to have a minimum paid-up capital of US$ 11,100 (equivalent of Rs 0.5 million) with a minimum of seven members and three directors.

* In both public and private corporations, if the name of the Indian company contains the word 'India', the minimum authorised capital would be US$ 11,100 (equivalent of Rs 0.5 million)

Foreign Corporations
Foreign corporations that are incorporated outside India but have a presence in India in the form of liaison offices, project offices, branch offices, etc. are also governed by the Companies Act, 1956, which contains special provisions for regulating such entities.

Structures Typically Used by Foreign Investors

Subsidiary Companies
Foreign corporations can set up their subsidiary companies in the form of private companies in India. The subsidiary company, incorporated under the laws of India, is treated as a domestic company for tax purposes.

In comparison with branch and liaison offices (discussed in the following paragraphs), a subsidiary company provides maximum flexibility for conducting business in India. However, the exit procedure norms of such companies are relatively more cumbersome. Below are some of the features of a subsidiary company:

- Funding could be via equity, debt (both foreign and local) and internal accruals.
- Indian transfer pricing regulations shall apply.
- No approval is required for the repatriation of dividends.

Branch office
Foreign corporations may open branch offices to conduct business in India and this requires a specific approval from RBI. A foreign corporation cannot undertake any activity in India that is not specifically permitted by RBI.

A branch office is also required to register itself with the Registrar of Companies and comply with certain procedural formalities prescribed under the Companies Act, 1956. A branch office is permitted to undertake the following activities:

- Export/import of goods.
- Rendering professional or consultancy services.
- Carrying out research work, in which the parent company is engaged.

- Promoting technical or financial collaboration between Indian companies and the parent or overseas group company.
- Representing the parent company in India and acting as a buying/selling agent in India.
- Rendering services in IT and software development in India.
- Rendering technical support to the products supplied by parent/group companies.
- Undertaking activities of foreign airline/shipping companies.
- Manufacturing, by a branch located in a SEZ

For income tax purposes, a branch office is treated as an extension of the foreign corporation in India and taxed at the rate applicable to foreign companies.

A branch office provides the advantages of ease in operation and an uncomplicated closure. However, since the operations are strictly regulated by exchange control guidelines, a branch may not provide a foreign corporation with the most optimum structure for its expansion/diversification plans.

Liaison Office

Foreign corporations are permitted by RBI to open liaison offices in India (subject to obtaining specific approval) for undertaking liaison activities on their behalf. These offices act as a communication channel between the foreign corporations and the Indian customers. Such offices are normally established by foreign corporations to promote their business interests in the country by spreading awareness of their products and exploring opportunities for setting up a more permanent presence. A liaison office also requires registration with the Registrar of Companies.

A liaison office in India is permitted to undertake the following activities:

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

Project Office

A foreign corporation which has secured a contract from an Indian company to execute a project in India may establish a project office in India without obtaining prior permission from RBI. However, the exchange control norms prescribe certain requirements in this regard.

Like a branch office, a project office is also treated as an extension of the foreign corporation in India and taxed at the rate applicable to foreign corporations.

Funding of Indian Businesses

Share Capital
The Companies Act, 1956 permits companies to issue only two kinds of share capital viz.:

- Preference share capital (preferred stock).
- Equity share capital (common stock) with/without voting rights.

The restriction is not applicable to private companies which are not subsidiaries of a public company. The nominal value of shares is not prescribed by the Companies Act, 1956 but it is normally Rs 10 per share for equity shares and Rs 100 per share for preference shares.

The issue of capital to the public is governed by guidelines issued by SEBI, the body that regulates and oversees the functioning of the Indian stock markets.

Shares can be issued at par, at a premium or at a discount by existing companies. A company has to obtain permission from regulatory authorities before issuing shares at a discount under specific circumstances.

The amount of capital a company can issue is limited by the authorised capital specified in its memorandum of association. A company can increase its authorised capital only if permitted by its articles of association.

A company can increase its subscribed capital by offering a rights issue, the only condition being that the shares have to be offered to the existing shareholders first, in proportion to their shareholding. A company can also increase its subscribed capital by issuing bonus shares out of its retained earnings available for paying dividends.

Debentures and Borrowings
Companies can raise funds by issuing debentures, bonds and other debt securities. They can also raise funds by accepting deposits from the public. However, the Act strictly forbids debentures from carrying voting rights and prescribes the manner and the source from which deposits can be invited and accepted. Debentures can be redeemable or perpetual, bearer or registered and convertible or non-convertible.

Issue of Shares and Debentures
Shares can be issued to the public as long as the company complies with SEBI disclosure requirements while issuing a prospectus. The prospectus has to be approved by the stock exchange before it is filed with the Registrar of Companies. It is also scrutinised by SEBI.

C.2 Mergers and Acquisitions

The SEBI (Substantial Acquisition of Shares and Takeovers) Guidelines, 1997 (the Takeover Code) seek to protect the interests of small investors and also strengthen the regulatory framework for takeovers. The Takeover Code essentially gets triggered if the acquisition of the shares of a company listed on a stock exchange (together with the shares already held) results in a holding of 15% or more of the voting capital or a change in management control.

Reorganisations and Mergers

Reorganisations of a company by a compromise (sacrifice by shareholders, creditors and others of their claims and entitlements to resurrect the company) or by an arrangement between the company and its creditors requires sanctioning by the jurisdictional High Court. The power to approve reorganisation and mergers has recently been shifted from the High Courts to NCLT. However, the NCLT is still in the process of being formed.

Buy-back of Shares

The Companies Act, 1956 permits a company to buy-back its share capital up to a ceiling of 10% of the paid-up equity capital and free reserves provided the same is sanctioned in the company's board meeting. A company may also buy-back 25% of the company's paid-up capital and free reserves provided the buy-back is sanctioned by a special resolution of shareholders.

However, a company buying back shares is not allowed to issue further shares of the same class or other specified securities for a period of six months following the buy-back. The Companies Act, 1956 also prescribes certain conditions relating to reserves, debt equity ratios, etc. for a company to be eligible for undertaking a buy-back of shares.

The procedure for affecting a buy-back is relatively simple and does not involve a court process.

Companies listed on a stock exchange in India are subject to the guidelines prescribed by SEBI in this regard.

Capital Reduction

Capital reduction is a court-regulated process whereby a company can pay off its shareholders by canceling or reducing capital or by canceling the share capital against accumulated losses.

Capital reduction requires sanction by the jurisdictional High Court. The power to approve capital reduction has recently been shifted from the High Courts to NCLT. The process also requires the company to obtain sanctions from various parties whose interest is likely to be affected as a result of the capital reduction scheme.

Demerger

Demerger is a reorganisation tool that is increasingly being employed by companies to segregate their core and non-core businesses. Demerger is also a court-regulated process which requires sanction by the jurisdictional High Court. Again, the power to approve demergers has recently been shifted from the High Courts to NCLT.

Slump Sale

A slump sale involves the transfer of an identified business from one company to another. Unlike a demerger, a slump sale is not a court-regulated process and can be achieved through a simple shareholders' resolution and legal agreement.

C.3 Taxes on Corporate Income and Gains

India has a well-developed tax structure with the authority to levy taxes divided between the central and the state governments. The central government levies direct taxes such as personal income tax, wealth tax, corporate tax and indirect taxes such as customs duty, excise duty, central sales tax and service tax. The states are empowered to levy professional tax and state sales tax apart from various other local taxes such as entry tax, octroi, etc.

Administration

The power of administration, supervision and control in the area of direct taxes lies with the Central Board of Direct Taxes (CBDT). The CBDT works under the MoF and exercises significant influence over the working of direct tax laws of the country in order to ensure effective discharge of executive and administrative functions.

Further, the Central Board of Excise and Customs, under MoF, deals with the formulation of policy concerning levy and collection of customs, central excise duties and service tax.

The Indian fiscal year runs from April 1 to March 31; a corporation’s tax year also ends on the same date. All corporations are required to file tax returns by October 31 and must file the same even in the event of loss. Non-resident corporations must file Indian income tax returns if they carry on business in India or have any office in India or earn income from any Indian source, asset, and property or business connection.

All corporations having Indian taxable income must register with their respective jurisdictional tax authorities. Corporate tax liability is required to be estimated and discharged by way of advance tax in four installments on June 15, September 15, December 15 and March 15.

Filing of late returns and delay in payment/shortfall in taxes are liable to penal interest at prescribed rates. Interest is imposed on the balance of unpaid tax due and on the underpayment of advance tax due.

Reforms in Indian Taxation

In the late 1980s and early 1990s, the Indian fiscal framework was highly complex and marred with multiple exemptions, extensive compliance requirements, high incidence of litigation, etc, on the one hand and lack of buoyancy in tax collections, unsatisfactory state of tax administration, dissatisfied taxpayers and a plethora of such issues on the other.

In 1991, faced with a severe balance of payments crisis, the government initiated a reform process premised on the understanding that foreign enterprise and capital are essential ingredients for a robust and progressive economic order in India. The government set up various committees and working groups over the years to review the fiscal framework and recommend reforms in light of the changing economic order.

However, some of the reforms initiated in the early 1990s are today being considered inequitable and regressive. In view of this, the government has recently set up working groups to review the tax policy and recommend reforms.

The Kelkar Committee Task Force

The Task Force (TFR), constituted under the chairmanship of Dr Vijay Kelkar submitted a report to the Finance Minister on the implementation of the Fiscal Responsibility and Budget Management Act, 2003 (FRBM Act). The FRBM Act was enacted to provide for the elimination of revenue deficit and the reduction of fiscal deficit below 3% of GDP by 2007-08. In order to achieve this objective, the report suggested a wide range of reforms across direct taxes, indirect taxes and government expenditure by means of the following steps:

- Widening the tax base.
- Low and few tax rates.
- Enhancing the equity of the tax system.
- Shifting to non-distortionary consumption taxes to increase efficiency in production.
- Enhancing international competitiveness of Indian goods and services.

Some of the key indirect tax proposals recommended by TFR are:

Introduction of the Goods and Services Tax Act (GST): Salient features are as follows:

- Tax to be levied on the 'sale' of goods and services.
- All goods and services to be taxed except those covered under a negative list.
- All exports to be zero rated.

- Credit allowed of tax paid on intermediate goods.
- Three-tier ad valorem rate structure.
- GST to be extended to immovable property transactions and financial service providers including banks, stock exchanges, etc.

Introduction of State Goods and Services Tax legislation (SGST): Salient features are as follows:

- A comprehensive SGST legislation proposes to replace various central and state enactments, including existing local and central sales tax legislation, octroi, entry tax, stamp duties, tax on transportation of goods and passengers, electricity tax, telecom license fee based on revenue sharing, etc.
- Three-tier ad valorem rate structure.

Customs duty
While recognising the decline in customs rates over recent years, the TFR has proposed to further reduce customs duty on basic raw materials, intermediate goods and finished goods. However, a higher duty has been proposed for motor vehicles and consumer durables. It is proposed to eliminate all exemptions except those relating to life-saving goods, goods of security and strategic interest, goods for relief and charitable purposes and international obligations including contracts.

Besides the above recommendations, TFR has inter alia recommended complete refund of import GST and SGST in the case of exports and has also recommended that the drawback scheme be restricted to basic customs duties only. It has also proposed merging the duty entitlement passbook scheme with the drawback scheme.

Corporate Income Tax

For Indian income tax purposes, a corporation's income essentially comprises income from business or property, capital gains realised on any disposition of the corporation's capital assets and residual income arising from non-business activities.

Corporations resident in India (whether owned by Indians or non-residents) are taxed on their worldwide income arising from all sources. Non-resident corporations are essentially taxed on the income earned from a business connection in India or from other Indian sources. A corporation is deemed to be resident in India if it is incorporated in India or if its control and management is situated entirely in India.

If a tax treaty exists between India and the country in which the taxpayer is resident, the provisions of the treaty or the Act, whichever are more beneficial, will apply to the tax - payer. Accordingly, the determination of whether a non-resident is taxable in India may be restricted or modified and lower rates may apply. In general, India's tax treaties provide that residents of other countries are subject to Indian tax on business profits derived from a business in India only if the non-resident has a permanent Indian establishment.

Rates of Corporate tax

Normal Rate

Domestic corporations are subject to tax at a basic rate of 30% enhanced by a 10% surcharge. Foreign corporations are subject to a basic tax rate of 40% enhanced by a 2.5% surcharge. Further, the tax payable by all the corporations is enhanced by an education cess at the rate of 2% on the tax payable, inclusive of surcharge.

Corporations are subject to wealth tax at the rate of 1%, if the net wealth exceeds US$ 33,000 (equivalent of Rs 1.5 million).

Special Rates for Non-Resident Corporations

Royalty or Fees from Technical Services: Non-resident corporations are taxed in the following manner:

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

Notes:

1. Royalties and fees for technical services earned in pursuance of agreements made after March 31, 2003 that are *effectively connected with the foreign corporation's permanent Indian establishment* are taxed at the rate of 40% (plus surcharge and education cess) on a net income basis.
2. Royalties and fees for technical services *(not effectively connected with the foreign corporation's Indian permanent establishment)* that are not received from the government or where received from Indian corporations under agreements not approved by the government or which are not in accordance with the industrial policy are also taxed at the rate of 40% (exclusive of surcharge and education cess) on a net income basis.

The above rates may be subject to more beneficial provisions contained in a tax treaty entered into between India and the country in which the taxpayer is resident.

All the tax rates mentioned above, excluding the rates prescribed under the relevant treaty, must be enhanced by a surcharge of 2.5%. Further, the tax payable by all the corporations should be enhanced by an education cess at the rate of 2% on the tax payable inclusive of surcharge.

<u>*Dividend Income:*</u> Dividend income distributed by domestic corporations is exempt from tax in the hands of the recipients. However, such corporations are required to pay DDT at the rate of 14.025% (including 10% surcharge and 2% education cess thereon) on dividends declared, distributed or paid by them.

<u>*Interest on Foreign-Currency Loans:*</u> Non-resident corporations earning interest on foreign-currency loans extended to Indian business enterprises or to the government of India are taxed at the rate of 20% on the gross amount of interest.

<u>*Overseas Financial Organisations:*</u> Specified overseas financial organisations earning income from units of specified mutual funds, purchased in foreign currency, are taxed at the rate of 10% on the gross amount of such income. Long-term capital gains arising on the transfer of such units are also taxed at the rate of 10%. However, if the transaction is liable to securities transaction tax (STT), then no tax is leviable on long-term capital gains, whereas short-term capital gains are subject to taxes at the rate of 10%.

FIIs are taxed at the rate of 10% on long-term capital gains and at the rate of 30% on short-term capital gains arising from the transfer of securities (other than units). However, if the transaction is liable to STT, the long-term capital gains may be exempt from tax and short-term capital gain may be liable to tax at 10%.

The above rates (excluding DDT) may be subject to more beneficial provisions contained in the tax treaty between India and the country in which the taxpayer is resident. All the tax rates mentioned above, excluding the rates prescribed under the relevant treaty, must be enhanced by a surcharge of 2.5% and an education cess at the rate of 2% on the tax payable inclusive of surcharge

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For a sample corporate tax calculation, see Appendix 4.

Minimum Alternate Tax (MAT)

The Indian tax law provides for MAT to be paid by corporations on the basis of profits disclosed in the financial statements. Corporations must pay 10% (plus applicable surcharge of 10% for domestic companies and 2.5% for foreign companies and 2% education cess thereon for both) of book profits as tax, if the tax payable as per regular tax provisions is less than 10% of its book profits. Book profits for this purpose are computed by making prescribed adjustments to the net profit disclosed by the corporations in their financial statements.

MAT paid by corporations for income years beginning on or after April 1, 2005 may be carried forward for seven years and MAT paid for prior years (that is, for income years ending on or before March 31, 2000) may be carried forward for five years and offset against income tax payable under the normal provisions of Income Tax Act, 1961. 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.

A report from a chartered accountant certifying the amount of book profits must be filed together with the corporate tax return.

C.4 Corporate Taxes at a Glance

Corporate income tax for domestic companies (%)	30 (a)
Dividend distribution tax (%)	12.5 (a)
Long - term capital gains tax (%)	20 (a) (d) (e)
Tax on foreign corporations tax (%)	40 (a)
Withholding tax (%) (a)	
Dividends	
Paid to domestic companies	0
Paid to foreign companies	0
Interest	
Paid to domestic companies	20
Paid to foreign companies	20 (b)
Royalties from patents, know-how, etc.	
Paid to domestic companies	0
Paid to foreign companies	20 / 10
Technical services fees	
Paid to domestic companies	5
Paid to foreign companies	20 / 10
Branch remittance tax	0
Fringe benefit tax	30% of value of fringe benefits (f)
Net operating losses (years)	
Carry back	0
Carry forward	8 (c)

(a) For the income year ending March 31, 2007, the rates listed above for corporate income tax, including capital gains tax, DDT and withholding taxes are increased by a surcharge equal to 10% of such taxes in case of resident corporations. In case of foreign corporations and branches, income tax, capital gains and the withholding taxes are increased by a surcharge equal to 2.5% of such taxes. In addition, the tax payable by corporations is increased by an education cess, which is imposed at a rate of 2% of the tax payable, inclusive of the surcharge.

(b) This rate applies only to interest from foreign currency loans. Other interest is subject to tax at a rate of 41.82% (including 2.5% surcharge and 2% education cess).

(c) Unabsorbed depreciation may be carried forward indefinitely to offset taxable profits in subsequent years. Unabsorbed business loss may be carried forward to offset profits of eight subsequent assessment years.

(d) Capital gains arising from the sale of assets held for more than three years (one year in the case of some assets such as shares, etc.) are termed as long-term capital gains. Capital gains other than such long-term capital gains are termed as short-term capital gains, which are taxed at normal corporate rates.

(e) Long-term capital gain arising on the sale of listed securities/units may be taxable at 10% (without indexation benefit). Long-term capital gain arising from the transfer of equity shares or the units of an equity-oriented fund on any recognised stock exchange in India or from the transfer of units of an equity-oriented fund to the mutual fund, will be exempt from tax if STT is payable on such transaction.

(f) Fringe benefit tax of 30% (plus education cess and applicable surcharge) on the value of fringe benefits is levied on the employer in respect of the fringe benefits provided/deemed to be provided to the employees during any financial year commencing from April 1, 2005.

Tax Incentives

The government of India has been extending a host of incentives and concessions to eligible corporations in certain industries. Broadly, the tax incentives include tax holidays for corporate profits, accelerated depreciation allowances and deductibility of certain expenses subject to the fulfillment of prescribed conditions. Some of the key direct tax incentives have been outlined in the following paragraphs.

Profits from New Undertakings

New undertakings are defined as undertakings that are formed by means other than the division or reconstruction of a business already in existence or the transfer to a new business of machinery or plant previously used in India for another purpose. The following table sets forth the available tax exemptions.

Type of Business activities	Quantum of exemption: Percentage of Profit	Period
Undertakings engaged in the generation or generation and distribution of power or laying a network of new transmission or distribution lines or carrying out substantial renovation and modernization of the existing transmission or distribution lines (a)(c)	100	10 years
Companies (or Consortium of companies) carrying on the business of developing, or maintaining and operating or developing, operating and maintaining infrastructural facilities (b)	100	10 years
Undertakings which develop, develop and operate or maintain and operate an industrial park or a notified special economic zone on or before March 31,2006 (a)	100	10 years
Undertaking located in areas other than North Eastern region of India, that begins commercial production of mineral oil or refining of mineral oil	100	7 years
Undertakings engaged in developing and constructing housing projects, approval by local authority before March 31, 2007 and completed within four years from such approval and fulfilment of other prescribed conditions	Entire profit derived from the project	
Undertakings manufacturing or producing any article or thing, not being specified articles or things in specified zones or areas in Sikkim, Himachal Pradesh, Uttaranchal and the North Eastern states (d) (e)	100	10 years
Undertakings manufacturing or producing any specified articles or things or commence any specified operations in Sikkim, Himachal Pradesh, Uttaranchal and the North Eastern states (d) (e)	100	10 years

Type of Business activities	Quantum of exemption	
	Percentage of Profit	Period
Undertakings engaged in the integrated business of handling, storing and transporting food grains	100 30	5 years 5 years
Undertakings engaged in collecting and processing or treating of biodegradable waste for generating power; producing bio-fertilisers, bio-pesticides or other biological agents; producing biogas; or making pallets or briquettes for fuel or organic manure	100	5 years
Undertakings engaged in the business of processing, preservation and packaging of fruits and vegetables	100 30	5 years 5 years
Undertakings engaged in operating and maintaining hospitals in rural areas	100	5 years

(a) The exemption is available for a continuous period of 10 years falling within the period of the initial 15 years.

(b) The exemption is available for a period of 10 years falling within the period of the initial 20 years. However, in the case of ports, airports, inland ports, inland waterways, the exemption may be available for 10 years falling within the period of the initial 15 years.

(c) Substantial renovation / modernisation, if undertaken, should be completed by March 31, 2010. Generation and/or transmission and/or distribution should commence before March 31, 2010.

(d) Profit derived from substantial expansion undertaken by the existing undertaking or enterprise also eligible for exemption.

(e) 30% for the last five years for Himachal Pradesh and Uttaranchal.

A tax deduction equal to 100% of the profits derived from the export of articles, things or computer software by the following types of undertakings: units located in FTZs, HTPs/STPs, SEZs (established before March 31, 2005) and 100% EOUs. The deduction is calculated by applying to the taxable income the ratio of export turnover to total turnover and it is available up to the income year 2008-09.

Undertakings Established in SEZs

Nature of Corporate Tax Incentive

- Profits derived by undertakings set up in SEZs from the export of articles, things or computer software are allowed as a deduction from the computation of taxable income.
- No liability for MAT on the profits derived by the undertakings set up in SEZs from exports.
- Undertakings set up in SEZs which provide ITES also qualify for the incentive.

Conditions for Availing the Tax Incentive

- The undertaking must commence manufacture or production of articles or things or computer software in a SEZ.
- There must be export of such articles, things or computer software (export includes supply by one undertaking to another in the same or different SEZ).
- The sale proceeds of the articles, things or computer software exported out of India are received in or brought into India in convertible foreign exchange, within a period of six months from the end of the previous year or within such extended period as may be allowed (this condition is not applicable for units established in SEZs on or after April 1, 2005).
- The undertaking is not formed by the splitting up or the reconstruction of a business already in existence. (This condition is not applicable for units established in SEZs on or after April 1, 2005)
- The undertaking is not formed by the transfer to a new business of machinery or plant previously used for any purpose. However, if any machinery or plant or any part thereof previously used for any purpose is transferred to a new business, and the total value of the machinery or plant or part so transferred does not exceed 20% of the total value of the machinery or plant used in the business, then the aforesaid condition shall be deemed to have been complied with. Any machinery or plant used outside India by any other person, provided it was never used in India, or it has been imported into India from any country outside India and no depreciation has been claimed on the same in India, shall not be regarded as machinery or plant previously used for any purpose (this condition is not applicable for units established in SEZs on or after April 1, 2005).
- Assessee should furnish a report from a chartered accountant certifying the deduction.

Computation of Profits from Export

The formula for the computation of profits derived from exports is as follows:

= Profits of the business of the undertaking * export turnover/ total turnover of the business of the undertaking

Amount of Deduction

Percentage of profits derived from export	Undertakings established in SEZs on or after April 1, 2002 but before March 31, 2005	Undertakings established in SEZs on or after April 1, 2005 under SEZA
100%	For the first five years starting from the year in which manufacture or production commences	For the first five years starting from the year in which manufacture or production commences
50%	For the next two years	For the next five years
50% (subject to fulfilment of reinvestment conditions*)	For the next three years	For the next five years

* These conditions require transferring of the profits to a separate reserve account which is to be utilised for capital expansion.

Tax holiday for SEZ developers on or after April 1, 2005 (under the SEZA)

Proposal to grant 100% deduction in respect of profits and gains derived by an undertaking engaged in the development of SEZ (SEZ developer) for a period of 10 consecutive assessment years, out of 15 years from the year in which SEZ is notified by the central government. Further, various other fiscal incentives have also been prescribed under SEZA.

Exemption from Capital Gains
Exemption from capital gains tax on the sale of fixed assets (subject to fulfillment of use condition) will be granted to industrial undertakings, shifting base from urban areas to an SEZ.

Exemption of rentals on lease of aircraft/aircraft engine

The lease rentals for an aircraft or aircraft engine paid by an Indian company engaged in the operation of aircraft to the government of a foreign state or a foreign enterprise are exempt from income tax if the agreement was entered into before April 1, 2007. However, the agreement should not have been entered into between April 1, 1997 and March 31, 1999.

The income tax borne by Indian companies engaged in the operation of aircraft on lease rentals paid to the government of a foreign state or a foreign enterprise is exempt from grossing-up requirements if:

- the lease rentals are paid in respect of an agreement entered into between April 1, 1997 and March 31, 1999; and
- the agreement is approved by the central government.

Capital Gains and Losses

Proceeds in excess of cost from disposition of capital assets are generally taxed as capital gains. Capital assets include all kinds of property except stock-in-trade, raw materials and consumables used in business or profession, personal effects (except jewelry), agricultural land and notified gold bonds.

General Provisions

Long-term Capital Gains. Profits earned from the transfer of long-term capital assets are referred to as long-term capital gains. Long-term capital assets are assets held for more than three years and the following assets held for more than one year:

- Shares.
- Other securities listed on a recognised stock exchange in India.
- Units of Unit Trust of India (UTI).
- Units of specified mutual funds.
- Specified zero coupon bonds.

In general, long-term capital gains are taxed at a basic rate of 20%. The cost of the capital asset is adjusted for inflation (indexation) to arrive at the indexed cost (the benefit of indexation is not available to non-residents), which is allowed as a deduction while computing such long-term capital gains. However, no adjustment is allowed on account of inflation for computing the cost of bonds and debentures.

Gains derived from the transfer of the units of UTI, mutual funds, or listed securities are taxed at the rate of 10%, without allowing for indexation adjustments or at the rate of 20% with indexation benefits.

Long-term capital gain arising on the transfer of equity shares or units of an equity-oriented fund on any recognised stock exchange in India or from the transfer of the units of an equity-oriented fund to the mutual fund, will be exempt from tax if the transaction is entered on or after date on which STT comes into force, i.e. October 1, 2004 and STT has been paid on such a transaction.

For assets acquired on or before April 1, 1981, the market value prevailing on that date may be substituted for the cost of the asset. For computing capital gains arising from the transfer of bonus shares, its cost is considered to be nil.

Long-term capital losses are allowed to be carried forward for eight consecutive years, but may be offset only against taxable long-term capital gains.

Short-term capital gains. Capital gains arising from the transfer of short-term capital assets (assets that do not qualify as long-term capital assets) are referred to as short-term capital gains and are taxed at the normal corporate income tax rates.

Short-term capital gains arising on the transfer of equity shares or units of an equity-oriented fund on any recognised stock exchange in India or from transfer of units of an equity-oriented fund to the mutual fund on or after the date on which STT comes into force, and STT has been paid on such transactions will be taxable at a lower rate of 10% (plus applicable surcharge and education cess thereon).

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

Capital Gains on Depreciable Assets. To compute capital gains arising from the sale of assets on which depreciation has been allowed, the sale proceeds of the assets are deducted from the declining-balance value of the classes of assets (including additions during the year) of which the assets form a part. If the sales proceeds exceed the declining-balance value on the sale of the entire block, the excess is treated as short-term capital gain. Else, no capital gain results from the sales of such assets even if the sales proceeds for a particular asset are greater than the cost of such an asset.

Special Provisions Relating to Capital Gains

Domestic tax law contains a special provision for the taxation of capital gains earned by non-residents from the transfer of shares and debentures of an Indian corporation acquired by utilising foreign currency. Any gain (short or long-term) arising is reconverted into Indian rupees at the exchange rate prevailing on the date of transfer to arrive at the taxable capital gains.

This special provision acts as a measure to mitigate the effect of any fluctuation in the exchange rates of foreign currency on the capital gains earned by the non-resident. No indexation benefits are extended for calculating capital gains in such cases.

Amalgamations, Demergers and Slump Sale

Amalgamations. Amalgamations are tax neutral subject to the satisfaction of prescribed conditions. In case of non-compliance with any of the prescribed conditions, any brought forward business loss and unabsorbed depreciation which has been set off by the amalgamated company is treated as its income for the year in which the failure to fulfill any of the conditions stated above occurs. The amalgamation procedure involves a court process.

Demergers. Demerger of businesses by existing companies is tax neutral subject to the fulfillment of prescribed conditions. The accumulated losses and depreciation of the demerged company attributable to the resulting company will qualify to be carried forward and set off by the resulting company subject to satisfaction of the prescribed conditions. The demerger procedure involves a court process.

Slump sale. Profits derived from a slump sale are taxed as long-term capital gains if the transferred undertaking has been held for more than 36 months. Taxable capital gain arising from a slump sale is the excess of consideration received over the net worth of the undertaking. The net worth is the difference between the value of the total assets (the sum of the tax-depreciated value of assets that are depreciable for income tax purposes and the book value of the other assets) and the book value of the liabilities of such an undertaking or division.

Foreign Tax Relief

Tax treaties entered into by India and several other countries govern foreign tax relief for the avoidance of double taxation. If no such agreement exists, resident corporations may claim a foreign tax credit for the foreign tax paid by them. The amount of credit granted is the lower of the Indian tax payable on the income that is subject to double taxation and the foreign tax discharged.

For a list of tax rates prescribed under various treaties, see Appendix 5.

C.5 Determination of Taxable Income

Taxable profits are computed in accordance with common business or accounting principles, modified by statutory tax provisions.

Deductions

Deduction is allowed only for business-related revenue expenses; capital expenditure (other than those specified) and personal expenses are not deductible.

Inventories
Inventories should be valued at the lower of the cost or net realisable value.

Provisions
In general, ad hoc provisions are not tax deductible. Provisions for duties, taxes (other than income tax and wealth tax), bonuses, leave salary and interest on specified loans are deductible on accrual basis provided the corresponding payments are discharged before the due date for filing the return of income (ROI) or else the deduction is allowed in the year of actual payment.

General provisions for doubtful debts are not deductible unless the bad debt is actually written off in the accounts. However, relief is available to banks and financial institutions for non-performing assets.

Redundancy and Retirement Payments
Payments made to employees under voluntary retirement schemes are deductible over a period of five years commencing from the year in which the sum has been paid.

Contributions to retirement benefits and other similar welfare funds are deductible provided the corresponding payments are discharged before filing the ROI, or else deduction is allowed in the year of actual payment.

Depreciation and Amortisation Allowances

Depreciation or amortisation included in the financial statements is not deductible. Except for undertakings engaged in the generation or the generation and distribution of power, depreciation for tax purposes must be calculated on the block of assets as per the declining-balance method at the prescribed rates. Allowance for depreciation is available only after the asset is ready for use for its business purposes. In the event assets are acquired during the year and put to use for a period of less than 180 days, only half of the admissible depreciation is allowable.

Depreciation is computed on the amount arrived at after adding to the declining-balance value at the beginning of the year, the actual cost of assets acquired during the year reduced by the sale proceeds from the disposition of any asset in that block.

Tax depreciation rates (declining-balance method):

Assets	Per cent
Plant and machinery	15*
Cars other than those used in the business of running them on hire	15
Computers (including software)	60
Purely temporary erections	100
Furniture and fittings, including electrical fittings	10
Buses and lorries used in the business of running them on hire	30
Ships	20
Residential buildings	5
Buildings other than above	10
Intangible assets (such as know-how, patents, copyrights trademarks, licenses, franchises or any other business or commercial right of similar nature form a separate block of assets)	25

* Subject to fulfillment of certain prescribed conditions, accelerated depreciation equal to 20% of the actual cost is allowed with respect to plant and machinery (other than ships or aircrafts) acquired or installed after March 31, 2005.

Corporations engaged in the generation or the generation and distribution of power have the option of claiming depreciation on a straight-line basis.

Restrictions on Interest Deductions

India does not currently have mandatory thin capitalisation rules. However, banks and financial corporations are required to comply with prescribed capital adequacy norms. Interest is allowed as a deduction provided it is in respect of capital borrowed for the purposes of business.

Restriction on Payments to Residents and Non-residents
In order to enforce the tax-withholding provisions, certain payments on which tax has not been withheld or deposited as per the law are allowed as deductions in the year in which the taxes withheld are deposited.

Foreign Exchange Losses
Foreign exchange fluctuations are considered in computing taxable income provided they are on revenue account. Realised exchange fluctuations on the liability in respect of assets acquired outside India can be adjusted with its declining-balance value.

Relief for Losses

Business losses, other than unabsorbed depreciation may be carried forward to be set off against taxable business income derived for the next eight years, provided the ROI for the year of loss is filed by the due date. However, closely held corporations are required to satisfy a 51% continuity of ownership test to carry forward business losses.

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

Dividend Distribution Tax (DDT)

Dividends paid by resident companies are exempt from tax in the hands of the recipients. However, resident companies must pay DDT at a rate of 14.025% (including a 10% surcharge and a 2% education cess) on dividends declared, distributed or paid by them. Such tax paid is a non-deductible expense.

Fringe Benefit Tax (FBT)

FBT has been introduced in India from the income year beginning April 1, 2005. It is payable by a covered employer on the benefits provided or deemed to have been provided to past and present employees. The benefit need not be provided directly by the employer for FBT to apply.

The FBT legislation has identified an exhaustive list of expenses which are deemed to be fringe benefits to the extent of 20% or 50% of the cost incurred or payment made by the employer. A concessional rate of 5% has also been prescribed in select instances. Payment of FBT is not allowed as a deductible expense from the taxable income. Further, FBT is payable irrespective of whether the employer has taxable income in India or not.

In case of a domestic company, FBT is payable at a rate of 33.66% (including the 10% surcharge and the 2% education cess). However, in case of a foreign company, FBT is payable at a rate of 31.365% (including the 2.5% surcharge and the 2% education cess).

In a recent circular issued by CBDT, it has been clarified that no segregation of expenses between employees and non-employees will be allowed for computing FBT. Further, it has also been clarified that foreign companies would be liable to pay FBT only if they have employees based in India, and in which case FBT would be payable only on expenses attributable to Indian operations.

Furthermore, the circular states that FBT is allowable deduction for computing book profits for the purpose of computing MAT.

Banking Cash Transaction Tax (BCTT)

A new levy in the form of BCTT has come into force from June 1, 2005. BCTT is payable at a rate of 0.1% on the value of every taxable banking transaction. In case of a company, 'taxable banking transaction' includes a transaction involving cash withdrawal and encashment of one or more term deposits on any single day exceeding US$ 2,200 (equivalent of Rs 0.1 million). No BCTT is charged in case the amount of term deposits is credited to any account with the bank. The concerned scheduled bank is liable to collect and deposit BCTT.

Deemed Basis of Taxation

Income derived from providing services, facilities or plant and machinery with respect to prospecting, extraction or production of mineral oil, from the operation of ships or aircrafts and also from the business of civil construction, etc. in certain turnkey power projects, by non-residents are taxed on a deemed-profit basis.

Tonnage Tax Scheme

An optional tonnage tax scheme has been introduced for the Indian shipping industry on or from April 1, 2004 which taxes the income on a deemed profits basis.

Oil and insurance companies have a separate code of taxation.

Related Companies

Transfer Pricing
Comprehensive transfer-pricing regulations (TPRs) have been introduced, effective from April 1, 2001 with the objective of preventing MNCs from manipulating prices in intra-group transactions such that the profits are not shifted outside India.

Under TPRs, international transactions between two or more associated enterprises (including permanent establishments) must be at arm's length prices (ALP). These regulations also apply to cost-sharing arrangements.

TPRs also require persons entering into international transactions to maintain prescribed documents and information, and to obtain and furnish to the revenue authorities an accountant's report containing prescribed details regarding the international transactions.

Stringent penalties have been prescribed for non-compliance with the procedural requirements and for understatement of profits.

Controlled Foreign Corporations
India does not currently contain any provisions in relation to controlled foreign corporations.

Consolidated Returns
India does not provide for the consolidation of income or common assessment of group companies. Each company, including a wholly-owned subsidiary, is assessed separately.

C.6 Other Significant Taxes

Securities Transaction Tax (STT)

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

The rates of STT are:

Nature of transaction	Amount of STT
Delivery-based transactions in equity shares or units of an equity-oriented fund	Buyer and seller each to pay 0.125%
Sale of units of an equity-oriented fund to the mutual fund	Seller to pay 0.25%
Non-delivery based transactions in equity shares or units of an equity-oriented fund	Seller to pay 0.25%
Derivatives (futures and options)	Seller to pay 0.017%

Excise Duty

Excise duty is a tax applicable on the manufacture of goods within the country. Excise duties are governed by the Central Excise Act, 1944, and the Central Excise Tariff Act, 1985.

Most products attract a uniform rate of 16%. Education cess at a rate of 2% is levied on the aggregate of the duties of excise.

Excise duty is mostly levied on an ad valorem basis (i.e. expressed as a percentage of the value of goods) or on maximum retail price (for notified goods). Valuation of goods is determined in the following manner:

- Transaction value: The price at which the goods are sold by an assessee at the time and place of removal where price is the sole consideration for sale and the seller and buyer are not related.
- Maximum Retail Price: Certain notified goods (which are statutorily required to declare on the package thereof a retail sale price) are charged to excise duty on such retail sale price as reduced by applicable abatement.

The Cenvat Credit Rules, 2004 (Credit Rules) allow manufacturers to avail and utilise the credit (cenvat credit) of additional duty of customs/ excise duty/ service tax paid on inputs and capital goods/ input services used in relation to manufacture. Cenvat credit can be utilised by the manufacturer to pay the output liability of excise duty on manufacture.

Customs Duty

Customs duty is levied under the Customs Act, 1962 (the Customs Act) on the import of goods into India. The rates of customs duty are laid down in the Customs Tariff Act, 1975 (the Tariff Act). Customs duty on imports comprises the following:

- Basic customs duty.
- Additional customs duty in lieu of excise duty.
- Additional duty of customs to countervail state taxes/ VAT.
- Education cess.

The rates of basic customs duty are specified under the Customs Tariff Act, 1975 (Tariff Act) for each item, and the general rate of basic customs duty ranges between 0% to 20% with most products being charged duty at a rate of 12.5%.

However, additional duty in lieu of and equivalent to the excise duty payable on like goods manufactured in India and additional duty of 4% in lieu of the sales tax/ VAT payable on the sale of the goods, is also leviable on the imported goods. In addition, 2% education cess is also charged on the aggregate customs duties. Certain specified categories of goods are exempt from this levy in accordance with commitments under WTO.

Thus, imported goods which have a basic customs duty rate of 12.5% are subject to an effective customs duty rate of 36.74% as a result of the aforesaid additional duties.

Further, certain exemptions/ concessions (drawback of duties, benefit under export promotion capital goods scheme, etc.) are available for import of the specified products such as IT products or for imports under specific schemes or projects.

The primary basis for the valuation of goods under the Indian customs law is the transaction value.

The government of India has entered into a number of free trade agreements with trade partners like Thailand, Sri Lanka, South Asian Association for Regional Cooperation (SAARC) countries and Singapore to promote trade in terms of which preferential tariff rates have been extended for certain identified goods. Similar trade agreements with Association of South East Asian Nations (ASEAN), Mercosur countries and the European Union are also on the anvil.

Service Tax

Service tax is a tax levied on certain identified taxable services provided in India by specified service providers. Currently, service tax is levied at the rate of 12.24% (inclusive of 2% education cess). The Finance Act, 2006 introduced 15 new service categories taking the total taxable service categories liable to service tax to more than 90.

Specific provisions have also been introduced to levy service tax on taxable services provided by a person located outside India (having a business/ fixed establishment/ permanent address outside India) to a person in India (having place of business/ fixed establishment/ permanent address in India). The Import of Service Rules, 2006 specifies the criteria based on that a service would qualify as an import.

The government has issued Export of Services Rules, 2005 (the Export Rules) that provide the specific criteria based on which a particular service would qualify as an 'export' on which no service tax is payable. Further, a mechanism has been provided where an exporter of a service has the option to claim rebate/ refund of excise duty/ service tax paid on inputs/ input services used in export of the service.

Credit Rules allow a service provider to avail and utilise the credit of additional duty of customs/ excise duty (paid on inputs/ capital goods used in rendering output services) for the payment of service tax. This is in addition to the availment and utilisation of the credit of service tax on input services for the discharge of output service tax liability. However, credit of additional duty of customs paid in lieu of sales tax/ VAT is not available to a service provider.

The Service Tax (Determination of Value) Rules, 2006 have been recently introduced for determining the value of non-monetary consideration which can be subjected to service tax levy.

Value Added Tax (VAT)/ Sales tax

Most Indian states have replaced the erstwhile sales tax regime, prevailing for more than five decades, with VAT from April 1, 2005.

Interstate sales continue to be liable to Central Sales Tax (CST), which is imposed by the central government. The rate of CST is generally 4% subject to the provision of declaration forms prescribed under the CST Act. CST is proposed to be phased out.

The key features of VAT are as follows:

- VAT is a multi-point tax system and is levied on value added at each stage.
- VAT has replaced existing state sales level taxes like sales tax, lease tax, turnover tax, resale tax, etc. VAT covers tax on sale of goods, works contract transactions and lease of goods.
- The basic rate slabs under VAT are as follows:
  - 0% for natural and unprocessed products and other essential goods;
  - 1% for silver, gold ornaments, etc.;
  - 4% for agricultural and industrial inputs, IT products, capital goods, items of basic necessities, etc.; and
  - 12.5% for other goods.
- Full input tax credit is available in respect of locally procured goods and can be set off against output tax liability including CST.
- No credit is available for taxes paid in other states and CST.
- Full input tax credit / refund is available in respect of goods exported outside India.
- For stock transfer/ consignment sale of goods out of state, input tax paid in excess of 4% is eligible for credit.
- Generally, input credit on capital goods is available on a staggered basis - over a period of 24 to 36 months.
- Composition scheme is available for dealers having turnover up to US$ 0.11 million (Rs 5 million) in most states. Under this scheme, tax is payable at a nominal flat rate (usually 1%), without any provision for input tax credits.

Currently, VAT is implemented in the majority of the states and is proposed to be implemented in the remaining states shortly.

Octroi /Entry Tax

Octroi/ entry tax is a levy on the entry of goods into a particular municipal/state jurisdiction for use, consumption or sale within such jurisdiction. The rate of entry tax on different products may vary from state to state. Some states have abolished the entry tax legislations while in other states entry tax paid is available as a set-off against the VAT liability of the importer or the sales tax payable on the sale of goods.

Research and Development Cess

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

Other Taxes

- Transfer of assets attracts stamp duty.
- Some states impose real estate taxes based on assessed values.
- Municipalities levy tax on real estate in their jurisdiction.
- Some states also levy luxury tax on certain specified goods.

C.7 Financial Reporting and Auditing

Sources of Generally Accepted Accounting Principles

The Accounting Standards Board of the Institute of Chartered Accountants of India (ICAI) issues the accounting standards to be followed by enterprises. All accounting standards issued to date are mandatory and companies are required to comply with these standards and disclose significant accounting policies in the preparation of their financial statements. ICAI also issues guidance notes and auditing and assurance standards, which are designed primarily to guide auditors on matters that may result during the course of their professional work.

Statutes/Bodies Governing the Reporting Requirements
The ICAI, National Advisory Committee on Accounting Standards (NACAS), SEBI, the Companies Act, 1956 and the Income Tax Act, 1961, primarily govern the financial reporting requirements of companies in India. In addition, the central government, through special acts and orders, also governs the financial reporting requirements.

Sources of Accounting Standards
Indian accounting standards have been sourced from the International Accounting Standards (IAS), now renamed International Financial Reporting Standards (IFRS). However, it may be noted that there are several differences between the Indian accounting standards and the IAS.

Significant Fundamental Concepts

Accounting Methodology
The fundamental accounting assumptions of going concern consistency and accrual of income and expenses need not be disclosed in the financial statements. Departures from these basic concepts, however, must be disclosed.

All significant accounting policies should be disclosed in one place in a separate statement or schedule to the financial statements. The effect of any material changes in accounting policies must be quantified and the reasons for such changes explained.

Inflation accounting is not used in India; accounts are prepared using the traditional cost accounting convention.

Change in Method of Accounting
Companies may change a method of accounting. A change can be made to comply with a statute or an accounting standard, or if it is felt that the change would result in more appropriate presentation of the financial statements of the enterprise. The new method should be followed consistently. A description of the change and the reasons for it should be disclosed in the financial statements in the year of the change.

Disclosure, Reporting and Filing Requirements

Disclosure Requirements
General Requirements. Financial statements should consist of the following items:

- Balance sheet.
- Profit and loss account.
- Notes to the financial statement.
- Auditor's report.
- Cash-flow statement? (not required for small and medium size enterprises).

The balance sheet and the profit and loss account should provide all disclosures necessary to give a true and fair view of the company's financial position and the results of operations.

Companies are also required to disclose basic and diluted earnings per share with the accounting policy and the method of computation. However, companies classified as small and medium size enterprises are not required to disclose diluted earning per share.

Financial statements must be signed and dated by the secretary, if any, and by at least two directors, including a managing director, if any, apart from the statutory auditor.

Directors' Report. The directors' report must accompany each set of financial statements and must contain certain prescribed information including a separate section on corporate governance with a detailed compliance report on corporate governance (for listed companies). Non-compliance with any mandatory requirement with reasons thereof and the extent to which the non-mandatory requirements have been adopted should be specifically highlighted.

Auditors' Report. The auditors' report must include an opinion on the financial statements of the company and must state whether the company and its branches have maintained the books of account as required by law, and whether these books agree with the balance sheet and profit and loss account.

In addition to the above, the auditors are also required to report on the matters stated in the Companies (Auditor's Report) Order, 2003 issued by the central government which include inter alia reporting on various specific aspects of internal control, inventory valuation, payment of statutory dues, description of contingent/contested liabilities, description of fraudulent transactions by or on the company, utilisation of long-term/short-term funds, etc.

Interim Financial Reporting Requirement of Listed Companies

Quarterly Financial Statements. Each listed company is required to announce unaudited financial results on a quarterly basis, within one month from the end of a quarter, in the specified format and announce the same in the newspapers and subject the results to limited review by the statutory auditors.

If the sum total of the first, second, third and fourth quarterly results with respect to any item given in the format varies by 20% when compared with the audited results for the full year the company must explain the reasons to the stock exchange.

Secretarial Audit. Issuer companies are to subject themselves to a secretarial audit to be undertaken by a qualified chartered accountant or a company secretary, for the purposes of reconciliation of the total admitted capital with both the depositories and the total issued and listed capital.

The issuer companies are to submit the audit report on a quarterly basis to the stock exchange(s) where they are listed. Any difference observed in the admitted, issued and listed capital shall immediately be brought to the notice of SEBI and both the depositories by the stock exchanges.

Annual Reporting Requirements

Reporting. Companies are required to comply with various reporting requirements which are greater for public companies than for private companies. Significant documents that need to be filed are the annual return, balance sheet, profit and loss account and the auditor's and directors' reports and charges. The formats of the balance sheet and the profit and loss account are prescribed by the Companies Act, 1956.

Annual financial statements must be sent to all shareholders and debentures holders at least 21 days before the annual general meeting (AGM). Listed companies must send annual financial statements to their stock exchange. In addition, listed companies have to publish quarterly financial statements.

Dividend Payments. Companies having shares are allowed to pay dividends only out of their profits after providing for depreciation on fixed assets in the manner prescribed and after certain minimum amounts are transferred to the company's reserves. Further, payment of dividends is permitted out of the company's accumulated reserves subject to compliance with certain prescribed rules.

Dividends can be recommended only by the board of directors and require shareholder approval. Dividends are declared in percentage terms and can be declared more than once a year.

Filing Requirements
After the annual financial statements have been presented at the AGM, three certified copies of the same must be filed with the Registrar of Companies within 30 days of adoption by the shareholders.

Requirement for Different Industries
The government requires certain manufacturers to maintain cost accounts and may order an audit by a qualified cost auditor of the same.

Banking, electricity and insurance companies are governed by special acts, rather than the Companies Act, 1956.

Audit Requirements

All companies, banks and financial institutions must have their accounts audited by an auditor who is a practicing member of ICAI. The branch of a company is also required to be audited.

The first auditor of the company is usually appointed by the directors. The shareholders appoint subsequent auditors at every AGM and establish their remuneration. The Companies Act, 1956 sets out the matters on which the auditor has to report.

Every company with gross revenue in excess of US$ 0.09 million (equivalent of Rs 4 million) must get its accounts audited under the Income Tax Act, 1961. As part of the audit process, the auditor also needs to certify information pertaining to FBT. The Companies Act, 1956 also grants the government the powers to order other audits like cost audits and investigations. In addition, every listed company or company with paid-up capital and reserves exceeding US$ 0.11 million (equivalent of Rs 5 million) as at the commencement of the financial year, or average annual sales above US$ 1.1 million (equivalent of Rs 50 million) for three consecutive financial years immediately preceding the financial year concerned, is required to have an appropriate internal audit system.

VAT Audit
VAT legislation requires a VAT Audit certificate / report by a chartered accountant in a prescribed format. The format for each state is different, but generally contains the same requirements. The due date for signing the VAT audit report /certificate varies from state to state and ranges between the months of September and December.

Generally, VAT Audit is applicable to all dealers liable to pay VAT provided their turnover of either sale or purchase exceeds a specified limit. Further, VAT Audit is also mandatory for specified categories of dealers as prescribed by the state legislation.

D. Individuals

D.1 Income Tax

Liability for Income Tax

Liability for income tax is governed by the residential status of the individual during the tax year. Individuals are considered as 'residents', if they meet either of the following criteria:

- They stay in India for 182 days or more during the tax year (April 1 to March 31).
- They stay in India for 60 days or more during the tax year and have stayed in India for at least 365 days in aggregate during the preceding four tax years.

Individuals who do not meet either of the above conditions are considered to be 'non-residents'. Individuals are considered 'not ordinarily residents' if they have been non-resident in India in nine out of the preceding 10 tax years or have been in India for an aggregate for 729 days or less in the preceding seven tax years.

Scope of Income Liable to Tax

Residents are subject to tax on their worldwide income.

Individuals who are residents but 'not ordinarily residents' are taxed on income:

- accruing or arising in India;
- deemed to accrue or arise in India;
- received in India; or
- received outside India arising from either a business controlled, or a profession established, in India.

Non-residents are taxed on income:

- accruing or arising in India;
- received in India, or
- deemed to accrue or arise in India through a business connection, through or from an asset or source of income in India, or through the transfer of a capital asset situated in India or from other specified sources.

The income of non-resident individuals is generally computed in the same manner as the residents.

All employees rendering services in India are subject to tax in India, unless they are exempt under the Income Tax Act, 1961 or respective tax treaties.

Types of Income Subject to Tax in India

In general, all income received/accrued/arising in India is subject to tax.

Employment Income
Resident employees are taxed on salary income, regardless of the place where it is earned. Salary income relating to services rendered in India including the rest/leave period which is preceded and succeeded by services rendered in India and forming part of the employment contract is deemed to accrue or arise in India, regardless of the place where it is received or the residential status of the recipient.

Expatriate employees of a foreign enterprise are not taxed, subject to the satisfaction of the following conditions:

- The enterprise is not engaged in a trade or business in India.
- The employee did not stay in India for more than 90 days (generally extended under tax treaties to 183 days) in a tax year.
- The compensation paid is not liable to be deducted by the employer from his taxable income in India.

Similar exemptions are available under tax treaties, but conditions vary. Non-resident foreign citizens employed on foreign ships who stay in India not longer than 90 days in a tax year are also exempt from tax on their earnings.

In general, most elements of compensation are taxable in India. Bonus paid at the commencement or completion of employment is included in taxable salary income. Specified allowances are either tax-exempt or included in the taxable income at a lower value, subject to certain conditions. Also, specified benefits, example company-provided accommodation receive preferential tax treatment, subject to certain conditions.

The following employer-paid items are not included in an employee's taxable compensation to the extent that they do not exceed specified limits, i.e. reimbursed medical expenses, travel allowances and contributions to the retirement benefit funds in India such as the provident fund, gratuity and superannuating funds.

Taxation of Employer-Provided Stock Options
Special rules apply for the taxation of stock options in India depending on whether a plan is a 'qualified plan' or 'non-qualified plan' as per Indian income tax law.

Taxability under a Qualified Plan: Where the stock plan under which shares are issued is in accordance with central government guidelines, the incidence of income tax arises only at the time of sale of the shares as capital gains. However, in case of a person who qualifies as a non-resident or not ordinarily a resident, the gains earned out of the sale of a foreign company's shares can be claimed as non-taxable where the proceeds are received outside India.

Taxability under a Non-qualified Plan: Where the shares have been received under a plan which is not in compliance with the central government guidelines, the incidence of income tax arises both at the time of exercise of options and at the time of sale of shares. At the time of exercise it is taxable as employment income and at the time of sale as capital gains.

Self-Employment and Business Income

All individuals who are self-employed or are engaged in business in India are subject to tax in accordance with the source and residence principles. All income received or deemed to be received, or accrued or deemed to be accrued, in India is subject to tax.

Capital Gains and Losses

Long-term capital gains are taxed at 20% plus applicable surcharge, if any. Long-term capital gain arising on the transfer of equity shares or units of an equity-oriented fund is exempt if the sale transaction is:

- entered into on or after October 1, 2004;
- through a recognised stock exchange or sale of units of equity oriented fund is to the mutual fund.

Long-term capital gain is exempt, if such gain or the sale proceeds of the long-term capital asset are invested in certain specified assets on satisfying certain conditions. Short-term capital gains are taxed at normal progressive tax rates applicable in the respective tax year.

Short-term and long-term capital losses may not be offset against other income. Short-term capital losses arising during the tax year can be set off against short-term capital gains or long-term capital gains. Long-term capital loss arising during the tax year can be set off only against long-term capital gains and not against any other income.

Income from House Property

Income from the letting of house property is taxable in the hands of the owner. Valuation of income from house property is prescribed under various scenarios of occupancy ranging from rented, vacant or self-occupied. The owner is entitled to a deduction on account of municipal taxes actually paid.

Further, he is entitled to a standard deduction towards repairs, etc. from such income at 30% of the prescribed value. Interest on borrowed capital, up to specified limits and upon fulfillment of prescribed conditions is also allowed as a deduction while computing the net income liable to tax.

Income from Other Sources

Income which does not specifically fall under any of the above types is liable to tax as 'income from other sources'. It includes investment income, winnings from lotteries, etc.

Investment Income
Dividends from Indian companies are currently taxed in the following manner:

- Domestic companies are required to pay DDT on profits distributed as dividends at the rate of 12.5% plus 10% surcharge and education cess of 2%.
- Amounts declared, distributed or paid as dividends are not taxable in the hands of the shareholders.

Non-residents are taxed on interest earned on loans made in India or technical services rendered in India, including the supply of know-how used in a business or profession carried on in India.

Deductions

An individual shall be allowed deduction in respect of life insurance premium, deferred annuity, contributions to provident fund, subscription to certain equity shares or debentures, investment in fixed deposit for a term of five years or more, etc., but subject to a maximum exemption limit of US$ 2,200 (equivalent of Rs 100,000).

Medical insurance premium may be deducted up to a maximum of US$ 220 (equivalent of Rs 10,000 and Rs 15,000 for Indian citizens over 65 years of age) against aggregate income from all sources.

Business Deductions
Taxpayers may generally deduct from the gross income accrued from business and profession all business-related expenses. Personal expenses and capital expenditure are generally not deductible. Allowable depreciation must be claimed, up to the available limit.

Rates

The following tax rates apply to resident and non-resident individual taxpayers for the year ending March 31, 2007.

Income Slabs (Rs.)	Income-tax
0-100,000*	Nil
100,000-150,000	10% of income in excess of Rs. 100,000
150,001-250,000	Rs. 5,000 plus 20% of income in excess of Rs. 150,000
250,001- Upwards	Rs. 25,000 plus 30% of income in excess of Rs. 250,000

**The minimum threshold limit in case of resident woman and resident senior citizen is Rs 135,000 and Rs 185,000 respectively, as against any other individual.*
***If the net taxable income exceeds Rs 1 million, a surcharge is levied at the rate of 10% on the tax payable (see Appendix 6).*
****An education cess of 2% is leviable on the income tax and surcharge.*

Relief for Losses

Business losses arising to the individual may be set off against income from any other source except for salary income. Business losses may be carried forward for eight years and set off against business income if the income tax return for the year of loss is filed on time. Unabsorbed depreciation may be carried forward indefinitely and be set off against income from any other source.

Tax Filing and Payment Procedures

All taxpayers, including non-residents, must file income tax returns if their taxable income exceeds the amount, which is not subject to tax in a tax year.

Income tax returns must be filed by July 31 immediately succeeding the tax year ending on March 31. Returns for the self-employed or business incomes must also be filed by July 31 except in a situation where the accounts are subject to a tax audit, in which case the return must be filed by October 31.

Taxpayers with employment income pay tax by way of the employer withholding taxes from salaries.

Non-residents generally are subject to the same filing requirements as residents. However, NRIs who have only investment income or long-term capital gains on foreign-exchange assets, need not file returns if the required tax is withheld at source. Non-residents are subject to assessment proceedings in the same manner as residents.

Before leaving the country, an individual not domiciled in India is required to furnish an undertaking to the prescribed authority of the purpose of his visit to India - for business, profession or employment. Such an undertaking is required to be obtained from his employer or from whom he is in receipt of income to the effect that tax payable by such a person shall be paid by the employer/the payer of income.

D.2 Other Taxes

Wealth Tax

Wealth tax in India is payable at a rate of 1% if the taxable value of the net wealth exceeds US$ 33,300 (equivalent of Rs 1.5 million). Assets subject to wealth tax include residential houses, cars, yachts, boats, aircraft, urban land, jewelry, bullion, precious metals, cash in excess of US$ 1,100 (equivalent of Rs 50,000), an amount not recorded in the books of the accounts of the company and commercial property not used as business, office or factory premises. The above assets, other than urban land (held for more than 10 years), are exempt from tax if they are owned as stock-in-trade or are used for hire. Productive assets, including shares, debentures and bank deposits, are not subject to wealth tax. The tax is levied on the net wealth held on March 31 of the relevant tax year. Wealth tax returns for individuals must be filed by July 31.

Inheritance (or Estate) and Gift Taxes

India does not impose tax on estates, inheritances or gifts.

Social Security

No social security taxes are levied in India.

D.3 Double Tax Relief and Tax Treaties

Taxpayers have the option to choose between the provisions of the tax treaty or the Income Tax Act, whichever is beneficial to them (see Appendix 5).

If the foreign income source of a resident is taxed in a country with which no double taxation avoidance agreement exists and such income is also taxed in India, then resident taxpayers may claim a tax credit in respect of such doubly-taxed incomes to the extent of the taxes paid in the source country or the rate of tax in India, whichever is lower.

D.4 Temporary Visas

Visitors to India need visas to enter the country unless they are Indian citizens. NRIs holding the citizenship of another country are also required to obtain visas before arriving in India unless they hold a PIO (Person of Indian origin) card issued by the Indian government. Visas must be obtained from the Indian embassy or consulate in the applicant's home country.

D.5 Visa and Registration Requirements

Foreign nationals can secure visas to enter India in the categories listed below:

Nature of visa	Purpose
Employment visa	Persons intending to take up employment
Business visa	Visiting India on business
Tourist visa	Visiting India for tourism
Student visa	Pursuing studies/academic courses
Entry visa	Other purposes not covered elsewhere (including accompanying families of foreign nationals)
Long-term visa	PIOs who have now obtained foreign nationality
Yoga visa	Persons interested in learning meditation or members of missionary organisations
Research visa	Pursuit of research in any field

Nature of visa	Purpose
Transit visa	Travelers passing through the country
Missionary visa	Missionaries of registered charitable trusts

Foreign Exchange Regulations

Under the prevailing foreign exchange regulations, an expatriate worker who is employed by a foreign company, but is resident in India while on deputation to office/branch/subsidiary/joint ventures of such foreign company in India, may open and maintain a foreign currency account with a foreign bank. The salary received for services performed in India may be paid into that account, subject to the following conditions:

- The amount paid into the foreign bank account may not exceed 75% of the salary. Should an employee wish to receive more than this percentage outside India, he must file a request with RBI.
- The remainder of the salary must be paid in rupees in India.
- Indian income tax must be paid on the entire salary.

Foreign nationals receiving salary in India from Indian firms or companies are allowed to remit their salaries to their home countries or may, alternatively, open an Indian bank account to be repatriated on retirement.

D.6 Residential Permit

All foreign nationals are required to register with the local immigration authorities called the Foreign Regional Registration Office (FRRO) within 14 days from their date of arrival, if their visas are valid for longer than six months. A foreign national holding a visa valid for six months or less who wants to stay in India beyond the period of validity must register within 14 days after 180 days from the time of arrival in India subject to holding a visa for the extended period. To register with the local registration office, certain prescribed documents must be presented.

The original passport and visa are also required at the time of filing the application with FRRO. Registration is valid for the term of the visa and may be extended on application. Failure to register may result in the immigration authority's refusal to allow the foreign national to leave the country.

D.7 Family and Personal Considerations

Work Visas for Family Members
Entry visas are issued to accompanying family members of individuals visiting India on business or for employment. Spouses or dependents of working expatriates must obtain separate work permits to be employed in India. Family

members intending to reside with a working expatriate must register separately at the local registration office. Children of working expatriates must obtain student visas to attend schools in India.

Drivers Permit

Foreign nationals are not allowed to drive in India using their home country drivers' licenses. They must obtain an international drivers' license in their home countries, which are generally valid for a period of six months. Alternatively, foreign nationals can go through the necessary procedures to obtain an Indian driver's license.

Appendices

Appendix 1: Useful Addresses and Telephone Numbers

When calling from an international location, the caller must dial the international country code for India (0091) followed by the city code (mentioned within brackets) and the local telephone number. When calling from within India, the caller must dial 0 followed by the city code and the local telephone number.

Business Facilitators	
Confederation of Indian Industry	CII Mantosh Sondhi Centre 23, Institutional Area, Lodhi Road New Delhi 110 003 Telephone: (11) 2462 9994 Facsimile: (11) 2462 1649 / 2463 3168 Website: www.ciionline.org
Federation of Indian Chambers of Commerce and Industry	Federation House Tansen Marg New Delhi 110 001 Telephone: (11) 2373 8760 70 Facsimile: (11) 2372 1504 / 2332 0714 Website: www.ficci.com
The Associated Chambers of Commerce Corporate and Industry in India	House, 147 B, Gautam Nagar Gulmohar Enclave New Delhi 110 049 Telephone: (11) 2651 2477 79 Facsimile: (11) 5164 3407 - 10 Website: www.assocham.org
Indian Investment Centre	Department of Economic Affairs Jeevan Vihar, 4th Floor Sansad Marg New Delhi 110 00 Telephone: (11) 2373 3673 / 79 Facsimile: (11) 2373 2245 Website: www.iic.nic.in
Department of Industrial Policy & Promotion	Ministry of Commerce & Industry Udyog Bhawan New Delhi 110 011 Telephone: (11) 2306 1222 Facsimile: (11) 2306 2626 Website: www.dipp.gov.in

Business Facilitators	
Foreign Investment Promotion Board	Department of Economic Affairs Ministry of Finance North Block New Delhi 110 001 Telephone: (11) 2309 4905 Facsimile: (11) 2309 3422 Website: www.finmin.nic.in
Software Technology Parks of India	Electronics Niketan 6, CGO Complex, Lodhi Road, New Delhi 110 003 Telephone: (11) 2436 2811 / 3596 2436 3187 / 3484 Facsimile: (11) 2436 4336 / 3436 Website: www.stpi.soft.net

Regulatory Bodies	
Reserve Bank of India	Central Office Shahid Bhagat Singh Marg Mumbai 400 001 Telephone: (22) 2266 1602 Facsimile: (22) 2266 2105 Website: www.rbi.org.in
Insurance Regulatory and Development Authority	3rd Floor, Parisrama Bhavanam Basheerbagh Hyderabad 500 004 Telephone: (40) 55820964/ 5578 9768 Facsimile: (40) 5582 3334 Website: www.irdaindia.org
Securities and Exchange Board of India	Mittal Court B Wing 224, Nariman Point Mumbai 400 021 Telephone: (22) 2285 0451 Facsimile: (22) 2285 5585 Website: www.sebi.gov.in
Telecom Regulatory Authority of India	A-2/14, Safdarjung Enclave New Delhi 110 029 Telephone: (11) 2610 1934 Facsimile: (11) 2610 3294 Website: www.trai.gov.in
Directorate General of Hydrocarbons	Hindustan Times House 4th and 11th Floors 18-20, Kasturba Gandhi Marg New Delhi 110 001 Telephone: (11) 2335 2650 / 17 2335 26 47 Facsimile: (11) 2331 7081 / 2335 2649 Website: www.dghindia.org
Directorate General of Civil Aviation	Aurobindo Marg, Opposite Safdarjung Airport New Delhi 110 003 Telephone: (11) 2462 2495 Facsimile: (11) 2462 9221 Website: www.dgca.nic.in

Regulatory Bodies	
Directorate General of Shipping	Jahaz Bhavan Walchand Hirachand Marg Mumbai 400 001 Telephone: (22) 2261 3651 / 54 Facsimile: (22) 2261 3655 Website:www.dgshipping.nic.in
Central Drugs Standard Control	Nirman Bhawan Organization New Delhi 110 011 Telephone: (11) 2301 8806 Facsimile: (11) 2301 2648 Website: www.cdso.nic.in
Central Board of Excise & Customs	North Block New Delhi 110 001 Telephone: (11) 2301 3908 Facsimile: (11) 2301 6475 Website: www.cbec.gov.in
National Highways Authority of India	G 5&6, Sector-10, Dwarka New Delhi 110 045 Telephone: (11) 2507 4100 Facsimile: (11) 2508 0360 Website: www.nhai.org

Key Ministries in the Government of India	
Ministry of Civil Aviation	Rajiv Gandhi Bhawan, B Block Safdarjung Airport Complex New Delhi 110 003 Telephone: (11) 2461 0358 Facsimile: (11) 2461 0378 Website: www.civilaviation.nic.in
Department of Chemicals & Petrochemicals	Shastri Bhawan, A Wing Dr Rajendra Prasad Marg New Delhi 110 001 Telephone: (11) 2338 4196 / 2338 2467 Facsimile: (11) 2338 7892 Website: www.chemicals.nic.in
Department of Commerce	Udyog Bhawan New Delhi 110 011 Telephone: (11) 2306 3664 Facsimile: (11) 2306 1796 Website: www.commerce.gov.in
Department of Information Technology	Electronics Niketan CGO Complex, Lodhi Road, New Delhi 110 003 Telephone: (11) 2436 4041 Facsimile: (11) 2436 3134 Website: www.mit.gov.in
Department of Telecommunications	Sanchar Bhawan 20, Ashoka Road New Delhi 110 001 Telephone: (11) 2371 9898 Facsimile: (11) 2371 1514 Website: www.dot.gov.in
Ministry of Environment & Forests	Paryavaran Bhawan CGO Complex, Lodhi Road New Delhi 110 003 Telephone: (11) 2436 1896 / 2436 0721 Website: www.envfor.nic.in

Key Ministries in the Government of India	
Ministry of Finance	North Block New Delhi 110 001 Telephone: (11) 2309 2947 Facsimile: (11) 2309 2145 Website: www.finmin.nic.in
Ministry of Food Processing Industries	Panchsheel Bhavan August Kranti Marg New Delhi 110 049 Telephone: (11) 2649 2475 Facsimile: (11) 2649 3228 Website: www.mofpi.nic.in
Ministry of Information & Broadcasting	Shastri Bhawan, A Wing Dr Rajendra Prasad Marg New Delhi 110 001 Telephone: (11) 2338 2639 Facsimile: (11) 2338 3513 Website: www.mib.nic.in
Ministry of Mines	3rd Floor, A Wing Shastri Bhawan Dr Rajendra Prasad Marg New Delhi 110 001 Telephone: (11) 2338 3082 Facsimile: (11) 2338 6402 Website: www.mines.nic.in
Ministry of Petroleum and Natural Gas	Shastri Bhawan Dr Rajendra Prasad Road New Delhi 110 001 Telephone: (11) 2338 3562 Facsimile: (11) 2307 0723 Website: www.petroleum.nic.in
Ministry of Power	Shram Shakti Bhavan New Delhi 110 001 Telephone: (11) 2371 1316 / 0271 Facsimile: (11) 2372 1487 Website: www.powermin.nic.in

Key Ministries in the Government of India	
Department of Shipping	Transport Bhavan 1, Parliament Street New Delhi 110 001 Telephone: (11) 2371 4938 Facsimile: (11) 2371 6656 Website: www.shipping.nic.in
Department of Road Transport & Highways	Transport Bhavan 1, Parliament Street New Delhi 110 001 Telephone: (11) 2371 4104 Facsimile: (11) 2335 6669 Website: www.morth.nic.in
Ministry of Steel	Udyog Bhawan New Delhi 110 011 Telephone: (11) 2379 3432 Facsimile: (11) 2301 3236 Website: www.steel.nic.in
Ministry of Textiles	Udyog Bhawan New Delhi 110 011 Telephone: (11) 2306 1320 / 30 / 38 Facsimile: (11) 2306 3711 / 3681 Website: www.texmin.nic.in
Ministry of Tourism	Transport Bhawan 1, Parliament Street New Delhi 110 001 Telephone: (11) 2371 1792 / 2332 1395 Facsimile: (11) 2371 7890 Website: www.tourism.nic.in

Industry Associations	
Indian Banks Association	6th Floor, Centre 1 World Trade Centre Complex Cuffe Parade Mumbai 400 005 Telephone: (22) 2217 4040 Facsimile: (22) 2218 4222 Website: www.indianbanksassociation.org
Association of Mutual Funds in India	106, Free Press House Free Press Journal Marg Nariman Point, Mumbai 400 021 Telephone: (22) 5637 3907 / 3908 Facsimile: (22) 5637 3909 Website: www.amfiindia.com
Chemicals and Petrochemicals Manufacturers Association	10th Floor, Vijaya Building, 17, Barakhamba Road New Delhi 110 001 Telephone: (11) 2332 6377 / 2332 2068 Facsimile: (11) 2331 0282 Website: www.cpmai.net
Indian Chemicals Manufacturers Association	Sir Vithaldas Chambers 16, Mumbai Samachar Marg Mumbai 400 023 Telephone: (22) 2204 7649 / 8043 / 2284 6852 Facsimile: (22) 2204 8057 Website: www.icmaindia.com
All India Plastics Manufacturers' Association	AIPMA House, A-52, Street No. 1 MIDC, Marol, Andheri East Mumbai 400 093 Telephone: (22) 2821 7324 / 7325 Facsimile: (22) 2835 2511 / 2512 Website: www.aipma.net

Industry Associations	
Bulk Drug Manufacturers Association	C-25, Industrial Estate Near SBH, Sanath Nagar Hyderabad 500 038 Telephone: (40) 2370 3910 / 6718 Facsimile: (40) 2370 4804 Website: www.bdm-assn.org
Indian Drug Manufacturers Association	102-B, Poonam Chambers Dr Annie Besant Road, Worli Mumbai 400 018 Telephone: (22) 2497 4308 / 2494 4624 Facsimile: (22) 2495 0723 Website: www.idma-assn.org
Organization of Pharmaceutical Producers of India	Ground Floor, Peninsula Chambers Ganpatrao Kadam Marg, Lower Parel Mumbai 400 013 Telephone: (22) 2491 8123 / 2486 / 5662 7007 Facsimile: (22) 2491 5168 Website: www.indiaoppi.com
Association of Biotechnology Led Enterprises	No 13, Second Floor, 4th C Block 10th Main Road, Koramangala Bangalore 560 034 Telephone: (80) 2553 3938 Facsimile: (80) 2553 3938 Website: www.ableindia.org
National Association of Software and Service Companies	International Youth Centre Teen Murti Marg, Chanakyapuri New Delhi 110 021 Telephone: (11) 2301 0199 Facsimile: (11) 2301 5452 Website: www.nasscom.org
Manufacturers' Association for Information Technology	4th Floor, PHD House Opposite Asian Games Village New Delhi 110 016 Telephone: (11) 2685 5487 / 2686 6976 Facsimile: (11) 2685 1321 Website: www.mait.com

Industry Associations	
India Semiconductor Association	3rd Floor, Divyasree Chambers Langford Town Bangalore 560 025 Telephone: (80) 2212 0009 Facsimile: (80) 2207 2186 Website: www.isaonline.org
Cellular Operators Association of India	14, Bhai Veer Singh Marg New Delhi 110 001 Telephone: (11) 2334 9275 Facsimile: (11) 2334 9276 9277 Website: www.coai.in
Association of Unified Telecom Service Providers of India	B-601, Gauri Sadan 5, Hailey Road New Delhi 110 001 Telephone: (11) 2335 8585 / 8989 Facsimile: (11) 2332 7397 Website: www.auspi.org
The Indian Broadcasting Foundation	D-21 A, South Extension Part II New Delhi 110 049 Telephone: (11) 2625 5238 / 5239 / 2625 1618 Facsimile: (11) 2625 5240 Website: www.ibf-india.com
Electronic Component Industries Association	ELCINA House 422, Okhla Industrial Estate New Delhi 110 020 Telephone: (11) 2692 4597 / 8053 Facsimile: (11) 2692 3440 Website: www.elcina.com
Indian Electrical & Electronics Manufacturers Association	501, Kakad Chambers 132, Dr Annie Besant Road, Worli Mumbai 400 018 Telephone: (22) 2493 0532 / 6528 / 2493 6529 Facsimile: (22) 2493 2705 Website: www.ieema.org

Industry Associations	
Consumer Electronics & TV Manufacturers Association	J-13, Jangpura Extension New Delhi 110 014 Telephone: (11) 2432 1616 / 3090 8288 Facsimile: (11) 2432 1616 Website: www.cetmaindia.org
Society of Indian Automobile Manufacturers	Core 4-B, 5th Floor, India Habitat Centre Lodhi Road New Delhi 110 003 Telephone: (11) 2464 7810-12 Facsimile: (11) 2464 8222 Website: www.siamindia.com
Automotive Component Manufacturers Association of India	6th Floor, The Capital Court Olof Palme Marg, Munirka New Delhi 110 067 Telephone: (11) 2616 0315 / 2617 5873 Facsimile: (11) 2616 0317 Website: www.acmainfo.com
Federation of Indian Export Organisations	3rd Floor, PHD House Opposite Asian Games Village New Delhi 110 016 Telephone: (11) 2685 1310 / 12 / 2685 1314/ 15 Facsimile: (11) 2686 3087 / 2696 7859 Website: www.fieo.org

Appendix 2: Exchange Rates

The table below provides the RBI reference exchange rates of the Indian Rupee against the four major currencies as on June 30, 2006.

Currency	Exchange Rate
US Dollar	46.08
Euro	58.54
UK Pound	84.45
Japanese Yen (per 100 JPY)	40.16
Source: Reserve Bank of India	

Appendix 3 : FDI Policy

I. Sectors prohibited for FDI

i. Retail Trading (except Single Brand Product retailing.)
ii. Atomic energy
iii. Lottery business
iv. Gambling and Betting

II. All Activities/Sectors would require prior Government approval for FDI in the following circumstances:

i. Where provisions of Press Note 1 (2005 Series) are attracted;
ii. Where more than 24% foreign equity is proposed to be inducted for manufacture of items reserved for the Small Scale sector.
iii. Proposals falling outside the prescribed sectoral limits.

III. Subject to the above, FDI is permitted up to 100% under the automatic route (subject to applicable sectoral rules / regulations).

IV. Sector-specific policy for FDI: The FDI policy specifically provides the limits and conditions on a sector-wise basis for foreign investment. 100% foreign investment under the Automatic route is permitted in sectors not covered by the FDI policy. Given below is an illustrative list of sectors:

Sector	FDI permitted
Airports - Greenfield projects	100% - Automatic
Air transport services	49% - Automatic
Asset Reconstruction Companies	49% - FIPB
Atomic minerals	74% - FIPB
Banking - Private sector	74% - Automatic
FM Radio	20% - FIPB
Cigars & cigarettes	100% - FIPB
Courier services	100% - FIPB
Defence production	26% - FIPB
Information technology services like ITES, BPO, software services	100% - Automatic
Insurance	26% - Automatic
Power	100% - Automatic
Single brand retailing	51% - FIPB
Satellites - Establishment and operation	74% - FIPB
Special Economic Zones	100% - Automatic
Telecommunications	74% ; FIPB beyond 49%
Wholesale cash and carry trading	100% - Automatic

Appendix 4: Corporate Tax Calculation

The following example illustrates the computation of taxable income and tax liability of a domestic company for the income year April 1, 2006 to March 31, 2007.

Net profit as per financial statement		14,500,000
Less:		
Net dividends received from domestic company	(2,000,000)	
(exempt from tax)		
Income from sub-leased property	(200,000)	
(considered separately)		(2,200,000)
		12,300,000
Add:		
Provision for tax	9,000,000	
Depreciation as per financial statements	3,000,000	
Disallowed expenses	200,000	12,200,000
(such expenses not related to the business)		24,500,000
Less:		
Tax depreciation		(5,560,000)
Business income		18,940,000
Income from other sources:		
Net income from sub-leased property		200,000
Gross total income		19,140,000
Deduction:		
Taxable income		19,140,000
Calculation of Tax		
Income tax at 30 % on Rs 19,140,000		5,742,000
Add:		
Surcharge at 10 %		574,200
Education cess at 2 %		126,324
Tax payable		6,442,524
Less:		
Advance tax paid during the income year		(5,700,000)
Balance tax payable/refundable with return of income(1)		*742,524*

The liability for tax excludes the interest chargeable on account of underpayment of advance tax.

Appendix 5 : Treaty Tax Rates

The following table presents the lower of the treaty rate or the rate under the domestic tax laws on outbound payments for countries that have concluded double tax avoidance treaties with India.

	Dividends (g) Per cent	Interest per cent	Royalties (f) per cent
Armenia	0	10 (b)	10 (d)
Australia	0	15	10 (c)
Austria	0	10(b)	10 (d)
Bangladesh	0	10 (b)	10 (d)
Belarus	0	10 (b)	10 (c)
Belgium	0	15 (b)	10 (c)(e)
Brazil	0	15 (b)	10 (c)
Bulgaria	0	15 (b)	10 (c)
Canada	0	15 (b)	10 (c)
China	0	10 (b)	10 (d)
Cyprus	0	10 (b)	10 (c)
Czech Republic	0	10 (b)	10 (d)
Denmark	0	15 (b)	10 (c)
Finland	0	10 (b)	10 (c)
France	0	10 (b)(e)	10 (d)(e)
Germany	0	10 (b)	10 (d)
Greece	0	20 (a)	10 (c)
Hungary	0	10(b)(e)	10 (c)(e)
Indonesia	0	10 (b)	10 (c)
Ireland	0	10 (b)	10 (d)
Israel	0	10 (b)(e)	10 (d)(e)

	Dividends (g) Per cent	Interest per cent	Royalties (f) per cent
Italy	0	15 (b)	10 (c)
Japan	0	15 (b) (h)	10 (c)
Jordan	0	10 (b)	10 (c)
Kazakhstan	0	10 (b)(e)	10 (d)(e)
Kenya	0	15 (b)	10 (c)
Korea	0	15 (b)	10 (c)
Kyrgyzstan	0	10 (b)	10 (c)
Libya	0	20 (a)	10 (c)
Malaysia	0	10 (b)	10 (d)
Malta	0	10 (b)	10 (c)
Mauritius	0	20(a)(b)	10 (c)
Mongolia	0	15 (b)	10 (c)
Morocco	0	10 (b)	10 (d)
Namibia	0	10 (b)	10 (d)
Nepal	0	15 (b)	10 (c)
Netherlands	0	10 (b)(e)	10 (d)(e)
New Zealand	0	10 (b)	10 (d)
Norway	0	15 (b)	10 (c)(e)
Oman	0	10 (b)	10 (c)
Philippines	0	15 (b)	10 (c)
Poland	0	15 (b)	10 (c)
Portugal	0	10 (b)	10 (d)
Qatar	0	10 (b)	10 (d)
Romania	0	15 (b)	10 (c)

	Dividends (g) Per cent	Interest per cent	Royalties (f) per cent
Russian Federation	0	10 (b)	10 (d)
Singapore	0	15 (b)	10 (c)
Slovenia	0	10 (b)	10 (d)
South Africa	0	10 (b)	10 (d)
Spain	0	15 (b)	10 (c)(e)
Sri Lanka	0	10 (b)	10 (d)
Sudan	0	10 (b)	10 (d)
Sweden	0	10 (b)(e)	10 (d)(e)
Switzerland	0	10 (b)(e)	10 (d)(e)
Syria	0	7.5 (b)	10 (d)
Tanzania	0	12.5(b)	10 (c)
Thailand	0	20 (a)(b)	10 (c)
Trinidad and Tobago	0	10 (b)	10 (d)
Turkey	0	15 (b)	10 (c)
Turkmenistan	0	10 (b)	10 (d)
Uganda	0	10 (b)	10 (d)
Ukraine	0	10 (b)	10 (d)
United Arab Emirates	0	12.5 (b)	10 (d)
United Arab Republic	0	20 (a)	10 (c)
United Kingdom	0	15 (b)	10 (c)
United States	0	15 (b)	10 (c)
Uzbekistan	0	15 (b)	10 (c)
Vietnam	0	10 (b)	10 (d)
Zambia	0	10 (b)	10 (d)
Non-treaty countries	0	20 (a)	10 (c)

(a) This rate applies to the interest on monies borrowed, or debts incurred, in foreign currency. Other interest is taxed at a rate of 40% plus a surcharge of 2.5%and an education cess of 2%).

(b) A reduced rate of 0%to 10%applies generally to banks and, in a few cases, to financial institutions local authorities, political subdivisions and the government.

(c) This rate is provided under the Indian income tax law, being the rate lower than that prescribed under the relevant treaty. This rate is increased by a surcharge of 2.5%and further enhanced by an education cess of 2%for the year ending March 31, 2006. It applies to royalties (not effectively connected to permanent establishment or fixed base in India) paid to foreign corporations under agreements that are approved by the Government of India or are in accordance with the industrial policy, and that are entered into after May 31, 2005. However, if royalty is paid under an agreement entered into after March 31, 2003, which is not approved by the central government or is not in accordance with the industrial policy, the royalty is taxed on a net basis at a rate of 40% (plus a surcharge of 2.5%and an education cess of 2%).

(d) This rate is provided under the relevant treaty. It applies to royalty not effectively connected with permanent establishment in India.

(e) A more restrictive scope of the definition of royalty may be available under the most favored nation clause in the relevant treaty.

(f) Most of India's tax treaties also provide for withholding tax rates for technical services fees. In most cases, the rates applicable to royalties also apply to the technical services fees.

(g) Under the Indian income tax law, Indian companies must pay dividend distribution tax at a rate of 12.5% plus a surcharge of 10%and an education cess of 2%) on dividends declared, distributed or paid by them. Such dividends are exempt from tax in the hands of the recipients.

(h) Reduced to 10% as per the recent protocol amending the India Japan treaty. The amendment would be effective for withholding taxes starting July 1, 2006, in Japan and starting April 1, 2007 in India.

Appendix 6 : Individual Income Tax Calculation

The following example illustrates the method of calculating taxable income and income tax liability for an individual for the income year April 1, 2006 to March 31, 2007.

	Rs.	*Rs.*
Calculation of Taxable Income		
Salary and perquisites		430,000
Income from self-occupied property		0
Less interest paid on construction loan,		
limited to Rs 150,000		(150,000)
Capital gains (long-term)		30,000
Income from other sources		
Interest income		20,000
Gross total income		**330,000**
Less allowable deductions:		
Medical insurance, limited to Rs 10,000	(10,000)	
Investments in: - **(a)**		
• Provident Fund	(20,000)	
• Life Insurance	(10,000)	
• Other Tax Saving Investments	(20,000)	*60,000*
Taxable income (b)		**270,000**
Calculation of Tax Liability		
Ordinary taxable income at rates from the		
personal income tax rate table		
[(240,000-150,000) x 20% + 5,000] **(c)**		23,000
Capital gains (long-term of 30,000 x 20%)		6,000
Total tax liability		29,000
Surcharge*		0
Education cess at 2%		580
Total tax payable		**29,580**
Less:		
Taxes withheld on salary and interest	23,460	
Advance tax payment	6,120	(29,580)
Balance due with filing of return		0

a) Contributions/investments in the savings plan will be allowed as deduction from gross total income up to Rs. 100,000 effective April 1, 2005.

b) Taxable income consists of long-term capital gains (Rs 30,000).

c) Effective April 1, 2005 in case of a resident woman and resident senior citizen*, the minimum taxable income threshold is Rs 135,000 and Rs 185,000 respectively, as against Rs 100,000 for any other individual.

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About Ernst & Young

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