ELP
ECONOMIC LAWS PRACTICE
ADVOCATES & SOLICITORS

THE INDIA OPPORTUNITY

Tax and regulatory investment incentives available for doing business in/and with India

- India's rank jumps 14 places in the 'Ease of Doing Business Rankings' (63 among 190 countries)
- Poised to become the third-largest consumer market in the world
- Infrastructure spending to reach USD 1.4 trillion over 5 years
- Stable political environment with a stable federal structure
- Several new policies announced to fast track FDI into India
- Projected to be amongst the largest manufacturing hubs of the world by 2030

June 2020

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ENTITY STRUCTURES

While a Company form of organization is still the most conducive and effective form of setting-up business operations, especially for manufacturing entities, India also offers Limited Liability Partnership (**LLP**) as an alternate form (more effective for trading and service entities). An overview from an investor's perspective is given below:

Criteria	Company	LLP
Constitution	▪ Separate legal entity ▪ Regulated by the Companies Act, 2013	▪ Separate legal entity ▪ Regulated by the Limited Liability Partnership Act, 2008
Permissible funding	▪ Equity shares ▪ Preference shares ▪ Overseas debt funding permissible subject to exchange control regulations	▪ Partners' contribution to capital ▪ Overseas debt funding permissible subject to exchange control regulations
Broad process for incorporation	▪ Identification of minimum 2 shareholders and 2 Directors (1 resident director) ▪ Identification of the registered office ▪ Application for name approval ▪ Drafting of the charter documents ▪ Filing an application with ROC	▪ Identification of 2 partners and 2 designated partners who are individuals (1 resident designated partner) ▪ Identification of registered office ▪ Application for name approval ▪ Finalization of the LLP Agreement ▪ Filing an application with ROC
Broad timeline	Approximately 3 to 4 weeks	Approximately 3 to 4 weeks
Advantages	▪ Newly incorporated manufacturing companies eligible to opt for a concessional corporate tax rate of 15% (excluding surcharge and cess) {refer Chapter 2 for details} ▪ Shares are freely transferable for public companies and transfers for private companies are subject to restrictions contained in charter documents ▪ Greater transparency as all major decisions require consent of directors/ members ▪ Generally preferred contractor/ vendor/investment vehicle	▪ No Limit on the number of partners ▪ Less stringent compliances- no mandatory meetings and no requirement of maintaining registers ▪ Flexibility in management and operations as per the LLP Agreement
Disadvantages	▪ Higher compliance requirements – quarterly board meetings, stringent compliances including maintaining registers, statutory filings and mandatory external audit ▪ Related party transactions are regulated by Companies Act, 2013	▪ Liability of partners may exceed the capital contributions in case of unauthorized acts, fraud and negligence ▪ Transfer of partners' share is subjected to LLP Agreement
Tax status	Treated as a separate taxable unit with an option to avail incentivized rates	Treated as a separate taxable unit (not pass through)
Implications under FEMA	Investment can be made without any approval in sectors where 100% FDI is permitted and where there are no FDI linked conditions	Investment can be made without any approval in sectors where 100% FDI is permitted and where there are no FDI linked conditions

Other forms of setting up business operations in India (amongst others) include Branch Office (**BO**), Project Office (**PO**), Liaison Office (**LO**).

CORPORATE TAX

The recently announced reduced corporate tax regime of 15% for newly incorporated manufacturing companies has made India a sought after investment destination. The general rate of corporate tax (given below) is highly competitive when compared to other jurisdictions in the region:

Particulars		Base tax rate*
Domestic Company	Optional tax rate for newly incorporated manufacturing companies	15%
	Optional tax rate for existing companies	22%
	Normal tax rate for companies (Subject to turnover threshold)	25% to 30%
Others	Limited Liability Partnership	30%
	Foreign Companies (operating through BO, PO, LO, etc)	40%

**said tax rate to be increased by surcharge and cess as applicable*

Considering India's wide tax treaty network with major global jurisdictions, a well-planned investment structure by businesses routed through select jurisdictions can trigger benefits such as lower withholding tax on passive income, grant of foreign tax credits, etc.

In the alternate, the normal withholding tax on income in the hands of foreign parent/group as illustrated below shall apply:

Nature of payment/ income	Withholding tax rate*(%)
Dividend income	20
Interest on foreign currency loan not covered by specified categories as above	20
Royalty and technical fees	10
Other income	40

**said tax rate to be increased by surcharge and cess as applicable*

- Sale of assets, including shares is subject to capital gains.
- The nature of capital gains (Short Term or Long Term) is determined based on the period of holding. Tax rates as prescribed under the Income Tax Act (**ITA**) are applicable to such LTCG and STCG, except in cases where favorable rate is provided in the relevant tax treaty.

Key Tax Incentives Offered by India

Indian corporate tax law also provides for incentives in the form of reduced tax rates or enhanced deductions to encourage:

Research and development activities

Employment generation

INDIRECT TAXES

The Indirect taxes landscape of India has been radically altered post the introduction of the countrywide Goods and Services Tax (**GST**), which has been in effect since July 2017. GST has overcome multiple limitations of various erstwhile indirect tax levies, which it subsumed. The earlier structure was considered as inefficient owing to multiplicity of taxes, tax cascading, voluminous compliances etc. GST has been a key contributor in India's increasing ranking in the World Bank's *Ease of Doing Business* report.

With the introduction of GST, the Indirect tax regime in India has also adopted the globally renowned concept of '*Supply*' as the event of taxation.

Considering the federal structure of the nation, every transaction of supply (for the purposes of levy of GST) needs to be classified into
- intra-state (within the State) or
- inter-state (across two or more States)

Further, with a view to providing a level playing field to Indian businesses, import of goods into the country is also subject to GST in addition to basic customs duty (BCD- a trade barrier).

Customs and GST[1] therefore constitute the principal indirect tax levies within the country.

An overview of India's indirect tax structure applicable on different types of transactions is given below:

Transaction type	Taxes applicable*	Levied by
Import of goods	BCD# + Integrated Goods and Service Tax (IGST)	Central Government
Import of services	B2B- IGST (reverse charge)	Central Government
	B2C- Generally exempted	
Intra- state transaction of goods/services	CGST + SGST	Respective State Government
Inter- state transaction of goods/services	IGST	Central Government
Exports of goods and services	Zero-rated (with refund of ITC/ drawback of BCD)	Central Government

** Certain cesses may be levied in addition/# Levied under the Customs Act, 1962*

[1] Petroleum products and alcohol for human consumption are leviable to Excise duty and State VAT and excluded from GST

Other salient features of the Indirect tax framework are:

Particulars	GST	Customs
Rates	▪ A five-rate structure (0%, 5%, 12%, 18% and 28%) ▪ Essentials are included in the 0% tax slab, most goods and services in the 18% bracket, and specified luxury goods or services and 'sin' goods in the 28% slab ▪ In addition, luxury goods and sin goods are also liable to a Compensation Cess	▪ Qua imports-WTO bound rates, with a peak rate of 12.5% ▪ For enhancing domestic manufacturing in India, a higher rate of BCD, ranging upto 70%, levied on certain items ▪ Exports generally do not have to pay Customs duty, other than for products notified in public interest
Person liable to pay	▪ Generally, a supplier of goods or services is liable to collect GST from the recipient and deposit in the Government treasury ▪ In certain cases however, such as sponsorship services, import of services etc., a reverse charge mechanism applies, where the recipient is required to self-charge	▪ Importer of goods is liable to pay applicable Customs duties and undertake necessary compliances, including filing of bill of entry
Valuation	▪ GST is generally payable on the transaction value of the underlying supply, with specific additions and permissible deductions ▪ However, in cases of transaction between related entities and individual State-wide registrations of the same entity, the value is generally benchmarked on the fair market value	Being a WCO signatory, the valuation rules are guided by the GATT framework, with a special regime for related party transaction
Input tax credit (ITC)	GST seeks to provide a seamless flow of credit across goods and services. However, there are some exceptions to this general rule where the eligibility of ITC is restricted. Some of these include specified construction activities and employee- related expenditure. BCD however remains a non-creditable tax.	

Related party transactions are globally monitored due to their potential of facilitating wrongful shifting of value between entities. Different legislations in India provide for a framework to monitor such transactions between related parties, from various perspectives, including their being at arm's length. The different legislations which require compliance vis-à-vis such transactions are:

Income Tax Act	Customs	GST
Arm's length price is required to be established in relation to global transactions between associated entities, as per the prescribed guidelines	It needs to be established with cogent evidence that the relationship has not influenced the price	The value should represent open market value, to be derived from similarly placed supplies between unrelated entities

Pricing compliant with these legislations, supported by meticulous documentation of the transactions involved, holds the key to avoiding litigation. Key legislative tools which can be employed to achieve certainty are:

Income Tax Act:

- Advance pricing agreement- Between a taxpayer and tax authority or between the tax authorities of two jurisdictions, determining the pricing of taxpayer's international transactions with its associated enterprises
- Mutual agreement procedure- Mechanism laid down in tax treaties to ensure that taxation is in accordance with the tax treaty, which may also be invoked for transfer pricing, depending upon the tax treaty involved

Customs: Obtaining a Special Valuation Branch (SVB) order to secure pricing adopted under a certain agreement, till the time the underlying terms and other factors remain identical

GST: Obtaining an advance ruling to demonstrate that the pricing adopted or to be adopted is benchmarked around the open market value

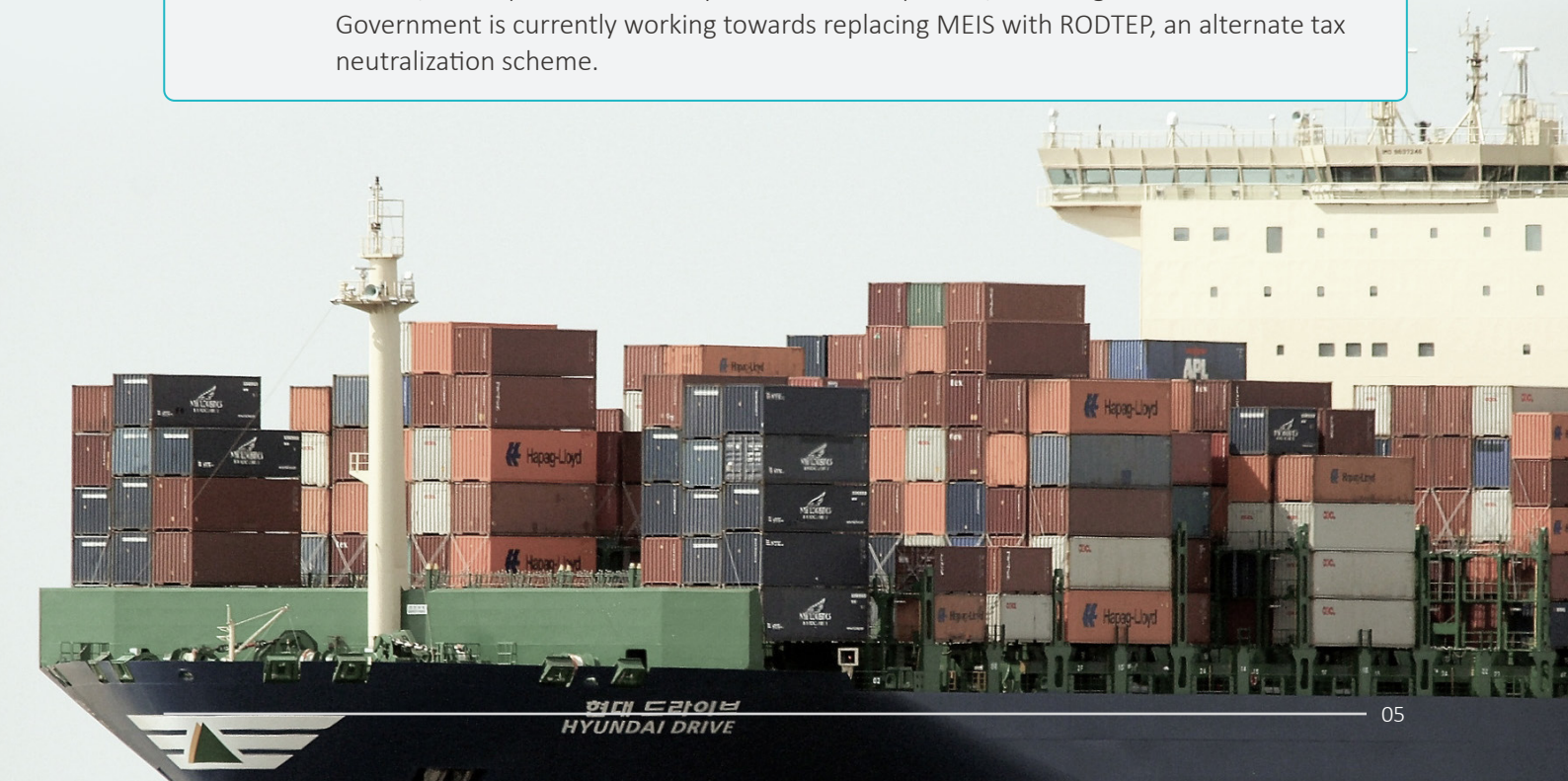
FOREIGN TRADE REGULATIONS AND EXPORT INCENTIVES

Imports and exports are regulated by the Foreign Trade (Development and Regulation) Act, 1992 (FTDR Act) which ***inter alia*** arms the Government with powers to regulate cross border trade and formulate a foreign trade policy (**FTP**).

While imports are mostly free, they are required to be compliant with domestic laws in matters of environmental safety and health norms and should also comply with other prescribed requirements e.g. BIS requirements, regulations dealing with hazardous waste, e-waste, etc.

Exports also are generally permitted freely, but certain restrictions are cast on export of dual use items. For example, items falling into the category of special chemicals, organisms, materials, equipment and technologies (**SCOMET**) can be exported only pursuant to the fulfilment of certain conditions. For instance, such items must comply with the Weapons of Mass Destruction and their Delivery System (Prohibition of Unlawful Activities) Act 2005.

Like every other nation, India also encourages exports. Incentives to businesses engaged in exports are formulated under the FTP. Such incentives are in the form of duty credit schemes or duty remission schemes in relation to both inputs or capital goods used for the purposes of exports. The Government also has formulated various schemes under the FTP, which provide monetary incentives to exporters, including SEIS and MEIS. The Government is currently working towards replacing MEIS with RODTEP, an alternate tax neutralization scheme.



INVESTMENT LINKED STATE INCENTIVES

Socio Economic Development

State governments, in India, encourages setting up of new business or expansion of an existing business as investments entails potential of economic development and employment generation in the region.

Economic & Tax Incentives

States have rolled out various economic and tax stimuli measures in the nature of provision of land at subsidized rates or other subsidies, in their bid to attract green field investments as well as expansions.

Enhances Project Feasibility & Returns

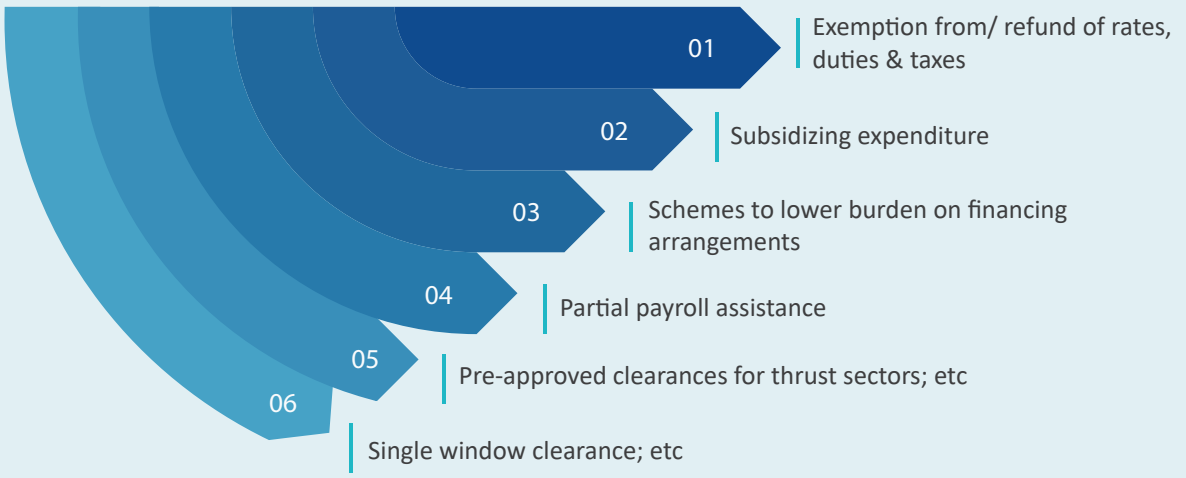
Several precedents demonstrate that incentives impacted the project commissioning timelines as well as returns positively.

Linkage to Fixed Capital Investment

The incentives are directly proportional to the fixed capital likely to be deployed as well as location of the project. Range ~10-100% of fixed capital investment.

Customization

Ability of large projects to negotiate incentive packages with the state. The customization tool could also be potentially used to seek immunity from an adverse policy action in future.



Pre-Investment Assessment

A pre-investment assessment of state incentives and policies could, therefore, meaningfully lower the project costs and help investors identify the right state for setting up the kind of business/ project they wish to set up.

FOREIGN EXCHANGE CONTROL REGULATIONS

01

Investment Opportunity in India

Consistently attracting an annual FDI of more than USD 40 billion, over the past five years, India is considered as one of the most attractive investment destinations in the world. Advantages include:

- An inherently large domestic market with a growing middle-class population that carries a significant buying capacity
- Availability of one of the largest skilled/semi skilled work forces in the age group of 25-45 years, at a comparatively economical cost
- One of the fastest developing economies with a GDP growth rate in the range of 5-8%.

02

Foreign Exchange Management Act, 1999

India's foreign exchange policies have largely been quite conservative and highly regulated. Investments in India by non-residents are regulated under the Foreign Exchange Management Act, 1999 (**FEMA**) and various regulations, press notes, circulars, directions and notifications issued thereunder from time to time. While routine foreign currency transactions are regulated by the Reserve Bank of India, policy framework *qua* foreign investments are generally formulated by the Department for Promotion of Industries and Internal Trade.

03

Foreign Direct Investments

As per relevant regulations, 100 % Foreign Direct Investments (**FDI**) is permitted or upto a certain extent is permitted either under the automatic route or an approval route depending on the sector involved. Generally, 100% FDI has been permitted under the automatic route, i.e. without any government approval but subject to certain reporting requirements, in the manufacturing sector (including contract manufacturing).

04

Simplification of reporting process

Foreign Investment Reporting Process has been simplified by introduction of Foreign Investments Reporting and Management System, an online application aimed at affording ease doing business.

05

Policy reforms by Indian Government

Recently, the Government of India announced **some policy and other reforms to fast-track investments in India:**

- **Investment Clearances:** Empowered Group of Secretaries (EGoS) would be formed with the responsibility to fast track investment clearances.
- **Incentive schemes for New Champion Sectors:** Incentive schemes will be announced for promotion of 'New Champion Sectors' such as Solar PV manufacturing, advanced cell battery storage among others.
- **Affordable Industrial Space:** The Central Government will create land banks to boost industrial development. The scheme will be implemented by States.
- **Increase in FDI limit**

Defence Sector increased from **49% to 75%**	**Insurance intermediaries increased to 100%** subject to applicable conditions	**Coal and lignite** mining sector and related activities **increased to 100%**

FEMA also regulates other foreign exchange fund options in the nature of External Commercial Borrowings, Foreign Currency Convertible Bonds, etc.

INDIAN IMMIGRATION AND LABOR LAWS

India believes in the concept of *"Atithi Devo Bhava"* the translation of which is *"Guest is God"*. In keeping with this philosophy, Indian legislations dealing with employment, especially those of foreign individuals, while being effectively regulated and compliance driven, ensure the comfort and convenience of foreign nationals. With global work force/expats increasingly coming to work in India, the Indian Government has ensured that its laws are updated especially in relation to social security, tax, immigration policies and other allied aspects. Some interesting features are detailed below:

01

FRRO registration

All foreigners visiting India on an appropriate work visa are allowed to engage in gainful employment. A foreigner with a valid visa for more than 180 days is also required to be registered with the Foreigners Regional Registration Officer (**FRRO**)/Foreigners Registration Officer (**FRO**) within 14 days of his arrival.

02

Social security law applicable to international workers

With effect from 2008, foreign nationals working in India called as "international workers" are covered within the ambit of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (**EPF Act**), which deals with social security contributions by employers and employees. An international worker is eligible to exemption from social security contributions in India under the EPF Act provided the following conditions are satisfied:

- The international worker is a national of a country with which India has a reciprocal Social Security Agreement SSA[2] continues to contribute to the social security of his/her home country; and a certificate of coverage (**COC**) is obtained by the international worker from his country of origin and submitted to the Employees' Provident Fund Organization.
- The international worker is contributing to a social security program of his country of origin or residence, with whom India has entered into a bilateral comprehensive economic agreement prior to October 1, 2008, on satisfaction of specified conditions.

03

Factors determining applicability of labor laws

Other labor and employee related laws in India are legislated and administered by Center or State depending on their coverage and are highly heterogeneous and complex. The applicability of such laws to an organization is determined by various factors such as number of employees/workers, nature of activities conducted, wages/salaries drawn by employees/workers. These laws cover various aspects relating to conditions of employment, health and safety, trade unions, industrial and labor disputes and other related matters.

04

Relaxations/reforms by Indian Government

The government has very recently introduced reforms/relaxations for ease of doing business:

- The Transgender Persons (Protection of Rights) Act, 2019 which prohibits discrimination against a transgender person has come into effect.
- Some State Governments have passed orders granting exemptions in respect of provisions pertaining to hours of work etc.

05

Proposed Codes for consolidation of labor laws

In a bid to consolidate and further simplify the existing structure of labor laws in India, the Government of India has proposed four new codes : Code on Wages, 2019, Occupational Safety Health and Working Conditions Code, 2019, the Industrial Relations Code, 2019 and the Code on Social Security, 2019, in an effort to consolidate various legislations in this arena.

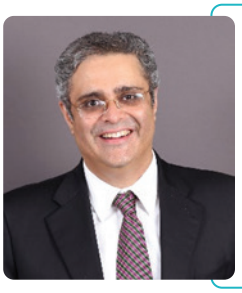
[2] *Currently, India has operating SSAs with 18 countries.*

ECONOMIC LAWS PRACTICE

Established in 2001 with the aim of bringing together a diverse set of professionals to deliver effective solutions for clients, Economic Laws Practice (ELP) is today a leading full-service law firm in India with more than 200 professionals – lawyers, chartered accountants, cost accountants, company secretaries, sector experts and economists – assisting clients on transactional, advisory, litigation, regulatory and tax matters.

ELP was recently featured as among the top 10 law firms in India in the RSG India Report 2019 and several of our practices are rated as Tier 1 by leading agencies in India and globally. ELP has an extensive client base across multiple industry sectors with clients from Fortune 500 companies, public sector undertakings, multinationals, Indian corporate power houses and startups. We work closely with leading global law firms in the United Kingdom, the United States, the Middle East and Asia-Pacific region, giving us the ability to provide real-time support on cross-border concerns. ELP is the India representative for the Taxand global network- the world's largest network of independent tax organizations (Taxand represents leading tax firms across 50 global jurisdictions) allowing us to offer a wider portfolio of services to our global clients.

ELP is actively engaged and collaborates with governments, regulators, legislators, businesses and industry associations to achieve positive and sustainable long-term conditions.



Globally, companies are looking to reconfigure their supply and value chain networks to reduce dependencies and make them more formidable against black-swan events. India is a robust economy with rule of law. Add to this a thriving domestic market and India makes a compelling destination for every global company.

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The adoption of GST has singularly been one of the most bold and welcome tax reforms taken by the government, especially given India's size and complexity . In addition to this, the government's move to reduce the corporate tax rate (by 10 to 12 percentage points) and simultaneously work towards a more efficient tax resolution system are all geared towards making India a more attractive investment destination.

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The Government of India is proactively working towards introducing regulatory and tax reforms, for creating a business friendly environment. Major FDI reforms, increased transparency, employer friendly labour laws and enhanced infrastructure expenditure have been key focus areas. This combined with a consumption friendly demographic make India – the perfect destination for setting up manufacturing operations.

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OUR AWARDS AND RECOGNITIONS

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- International & Cross-Border Capabilities

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