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INDIA

INCORPORATION GUIDE

BUSINESS SET UP GUIDE
FOR FOREIGN INVESTORS

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1. BUSINESS FORMS

1.1. INDIAN COMPANY FORMS

Business forms available in India are

- **Limited Liability Partnership (LLP)**
- **Limited Company**
- **Sole Proprietorship**
- **Partnership**

LLPs and Limited Companies are incorporated business forms.
Proprietorship and Partnership are unincorporated business forms.

1.1.1. Limited Liability Partnership (LLP)

Limited Liability Partnerships (LLPs) are incorporated business forms. It is a Body Corporate having the features of a Partnership Firm and a Company. The management of LLP is defined by LLP agreement and partners have the freedom to regulate affairs of the LLP. Minimum two persons are required to form a LLP and there is no restriction regarding maximum number of members.

1.1.2. Limited Company

It is the oldest form of incorporated business in India. A company is a legal entity that is separate from its owners, the shareholders. No member of a company is personally liable for the debts, obligations or acts of the company, except under special circumstances such as the number of members falls below the required minimum number. This type of business organizations are incorporated under the Companies Act, 1956 by respective Registrar of Companies (ROC) in each state of India.

In India two type of companies are available for registration:

- Private Limited Company
- Public Limited Company

A **Private Limited Company** is a Company limited by shares in which there can be:

- The minimum number of shareholders is 2
- The maximum number of shareholders is 50
- No invitation can be made to the public for subscription of shares or debentures
- It cannot make or accept deposits from Public
- There are restriction on the transfer of shares.
- The liability of each shareholder is limited to the extent of the unpaid amount of the shares face value and the premium thereon in respect of the shares held by him.
- The minimum paid up capital at the time of incorporation has to be Indian Rupees 1,00,000.
- There is no upper limit on having the authorized capital and the paid up capital. It can be increased any time, by payment of additional stamp duty and registration fee.

1.2. FOREIGN COMPANY FORMS

Besides of the ordinary Indian Company Forms stated at point 1.1, Foreign Companies are allowed to set up their operations in India also through the following business entities:

- **Liaison Office/Representative Office**
- **Project Office**
- **Branch Office**

Such offices can undertake any permitted activities. Companies have to register themselves with Registrar of Companies (ROC) within 30 days of setting up a place of business in India.

- Liaison Office/Representative Office

- Project Office
- Branch Office

Such offices can undertake any permitted activities. Companies have to register themselves with Registrar of Companies (ROC) within 30 days of setting up a place of business in India.

1.2.1. Liaison office/ Representative office

Liaison office acts as a channel of communication between the principal place of business or head office and entities in India. Liaison office cannot undertake any commercial activity directly or indirectly and cannot, therefore, earn any income in India. Its role is limited to collecting information about possible market opportunities and providing information about the company and its products to prospective Indian customers. It can promote export/import from/to India and also facilitate technical/financial collaboration between parent company and companies in India.
The approval for establishing a liaison office in India is granted by the Reserve Bank of India (RBI).

1.2.2. Project Office

Foreign Companies planning to execute specific projects in India can set up temporary project/site offices in India. RBI has now granted general permission to foreign entities to establish Project Offices subject to specified conditions. Such offices cannot undertake or carry on any activity other than the activity relating and incidental to execution of the project. Project Offices may remit outside India the surplus of the project on its completion, general permission for which has been granted by the RBI.

1.2.3. Branch Office

Foreign companies engaged in manufacturing and trading activities abroad are allowed to set up Branch Offices in India for the following purposes:

- Export/Import of goods
- Rendering professional or consultancy services
- Carrying out research work, in which the parent company is engaged.
- Promoting technical or financial collaborations between Indian companies and parent or overseas group company.
- Representing the parent company in India and acting as buying/selling agents in India.
- Rendering services in Information Technology and development of software in India.
- Rendering technical support to the products supplied by the parent/ group companies.
- Foreign Airline/Shipping Company.

A branch office is not allowed to carry out manufacturing activities on its own but is permitted to subcontract these to an Indian manufacturer. Branch Offices established with the approval of RBI, may remit outside India profit of the branch, net of applicable Indian taxes and subject to RBI guidelines Permission for setting up branch offices is granted by the Reserve Bank of India (RBI).

1.2.4. Branch Office on "Stand Alone Basis"

Such Branch Offices would be isolated and restricted to the Special Economic zone (SEZ) alone and no business activity/transaction will be allowed outside the SEZs in India, which include branches/subsidiaries of its parent office in India. No approval shall be necessary from RBI for a company to establish a branch/unit in SEZs to undertake manufacturing and service activities subject to specified conditions.

2. ENTRY STRATEGIES FOR FOREIGN INVESTORS

A foreign company planning to set up business operations in India has the following options:

- Acting as an Indian Company
- Acting as a Foreign Company

2.1. ENTERING AS AN INDIAN COMPANY

A foreign company can commence operations in India by incorporating a company under the Companies Act, 1956 through:

- **Joint Ventures**
  or
- **Wholly Owned Subsidiaries**

2.1.1. Joint Venture With An Indian Partner

Foreign Companies can set up their operations in India by forging strategic alliances with Indian partners.

Joint Venture may entail the following advantages for a foreign investor:

- Established distribution/ marketing set up of the Indian partner
- Available financial resource of the Indian partners
- Established contacts of the Indian partners which help smoothen the process of setting up of operations

2.1.2. Wholly Owned Subsidiary Company (Subsidiary)

Foreign companies can also to set up wholly owned subsidiary in sectors where 100% foreign direct investment is permitted under the FDI policy.

Foreign equity in such Indian companies can be up to 100% depending on the requirements of the investor, subject to equity caps in respect of the area of activities under the Foreign Direct Investment (FDI) policy.

The wholly-owned subsidiary may be either of the following business entities:

- **Private Limited Company**
- **Public Limited Company**
- **Unlimited Company**
- **Sole Proprietorship**

2.1.2.1. Private Limited Company as a Subsidiary

A Private Limited Company is the most popular form of business entity used for Foreign Investors in India.

A subsidiary once incorporated under the provisions of the Companies Act is treated exactly like a domestic company.

If Indian company is subsidiary of foreign company then minimum authorized capital must be Rs. 500,000.00 instead of Indian Rupees 1,00,000 as requested for a non-subsidiary company.

A limited company has following advantages:

- Members' (the directors and shareholders) financial liability is limited to the amount of money they have paid for shares.
- The management structure is clearly defined, which makes it easy to appoint, retire or remove directors.
- There is no requirement to appoint any local director in Indian company and all the directors can be foreign citizens.
- If extra capital is needed, it can be raised by selling more shares privately.

- It is simple to admit more members.
- The death, bankruptcy or withdrawal of capital by one member does not affect the company's ability to trade.
- The disposal of the whole or part of the business is easily arranged.

A limited company has following disadvantages:

- Requirement to register the company with the registrar of companies and provide annual returns and audited statement of accounts. All details of the company are available for public inspection so there can be no secrecy. There are penalties for failing to make returns.
- Can be more expensive to set up.
- May need professional help to form.
- As a director, you are treated as an employee and must pay tax.
- The advantages of limited liability status are increasingly being undermined by banks, finance house, landlords and suppliers who require personal guarantees from the directors before they will do business.

2.2. ENTERING AS A FOREIGN COMPANY

Foreign Companies can set up their operations in India through

- Liaison Office/Representative Office
- Project Office
- Branch Office

3. INCORPORATION STEPS

3.1. COMPANY/LLP PROCEDURES & REQUIREMENTS

Procedures required to incorporate a Company are as follow:

Nature of Procedure in India	Approx. Duration (days)
Filing the proposed name of company for approval to the Registrar of Companies (ROC); Get the Memorandum and Articles of Association vetted by the ROC and printed	7
Make an application to the Superintendent of Stamps or an authorized bank requesting for stamping of the Memorandum of Association and Articles of Association.	1
Present the required documents along with the registration fee to the Registrar of Companies to get the certificate of incorporation	9
Obtain a company seal	3
Visit the UTI Investors Services Limited to obtain a Permanent Account Number	7
Obtain a Tax Account Number for income taxes deducted at source from the Assessing Office in the Income Tax Department	7*
Register under Shops and Establishment Act	2*
Register for value added tax (VAT) before the Sales Tax Officer of the ward in which the company is located	12*
Register for Profession tax	2*
Register with Employees' Provident Fund Organization	2*
Register with ESIC (medical insurance)	1*
Filing for Government Approval before RBI/FIPB for Foreigners and NRI's	15*
Totals:	35

For registration and incorporation, an application has to be filed with Registrar of Companies (ROC). Once a company has been duly registered and incorporated as an Indian company, it is subject to Indian laws and regulations as applicable to other domestic Indian companies.

First of all an application in Form No. 1A needs to be filed with the Registrar of Companies (ROC) online through Digital Signature of one of the proposed director. The details to be furnished in the said application are as follows:

- Alternative names for the proposed company. (The name can be coined names from the objects of the proposed company or the name of the directors, etc. but should definitely be indicative of the main object of the company. Justification for the name needs to be specified along with the application)
- Names and addresses of the promoters (Minimum 7 for a public company while 2 for private company).
- Authorized Capital of the proposed company.
- Main objects of the proposed company.
- Names of other group companies.

On submitting the application, the ROC scrutinizes the same and sends the approval / objections in about 3-4 days to the applicant through e-mail.

The following documents are required to be executed before they are submitted to the ROC:

- **MOA and AOA -** These are required to be signed by the promoters in their own handwriting in presence of a witness stating their full name, father's name, residential address, occupation and number of shares subscribed for, etc.

  The Memorandum of Association states the main, ancillary / subsidiary and other objects of the proposed company. The Article of Association contains the rules and procedures for the routine conduct of the proposed company. It also states the authorized share capital of the proposed company and the names of its first / permanent directors. After that Memorandum of Association and Article of Association are required to be stamped.

  A stamp duty is required to be paid on Memorandum of Association and Article of Association. The stamp duty depends on the authorized share capital.
- **Form No. 1 -** This is a declaration to be executed on a non-judicial stamp paper by one of the directors of the proposed company or other specified persons such as Attorneys or Chartered Accountant stating that all the requirements of the incorporation have been complied with.
- **Form No. 18 -** This is a form to be filed by one of the directors of the company informing the ROC the registered office of the proposed company.
- **Form No. 29 -** This is a consent obtained from all the proposed directors of the proposed company to act as directors of the proposed company. (Not required in case of private company).
- **Form No. 32 -** This is a form stating the fact of appointment of the proposed directors on the board of directors from the date of incorporation of the proposed company and is signed by one of the proposed directors.
- Power of Attorney signed by all the subscribers of MOA authorizing one of the subscribers or any other person to act on their behalf for the purpose of incorporation and accepting the certificate of incorporation. Investors who are not stationed in India can give Power of Attorney to a person to appear before ROC to complete the necessary formalities after getting MOA, AOA, Power of attorney and other allied documents notarized by notary public and attested by Indian Embassy/Consulate situated in foreign country.
- Filing fees as may be applicable.

After the documents are filed, the ROC calls the attorney for scrutiny and making the corrections in the MOA and AOA filed. On complying with the same, the certificate of incorporation is issued.

On receipt of the certificate of incorporation, the public company has to complete certain other legal formalities such as a statutory meeting (within 6 months), statutory report, etc. On completion of the said formalities and on filing of the statutory report with the ROC the ROC issues the certificate of commencement of business to the company. Thereafter, the Public Company can start the business operations.

The Private Company on the contrary can start its business immediately on incorporation.

Once the company is incorporated in India, foreign investor has to either intimate Reserve Bank of India (RBI) of the foreign equity or take approval of Foreign Investment Promotion Board (FIPB). Intimation to RBI or approval from FIPB is dependent upon sector in which foreign investor intends to do business.

That’s because of a WOS or a JVC in India will be subject to the exchange control regulations and the FDI policy of the Government of India.

There are certain sectors/activities listed out in the exchange control regulations where automatic approval of RBI for investment is not available. In such cases, an application is required to be made to the Foreign Investment Promotion Board (FIPB)/Secretariat for Industrial Assistance (SIA) for its approval for such investment. The exchange control regulations also list out other activities where automatic approval of RBI is available for investment, subject to certain limits specified therein. Any proposed investment in excess of the limits specified therein will again require approval of FIPB/SIA. The list of industries in respect of which the automatic route of RBI is available and in respect of which approval of FIPB/SIA is required is set out in greater detail subsequently.

Synthetically the approval of the investment can be obtained in two ways:

a. Automatic Approval - by the country's Central Bank, the Reserve Bank of India (RBI)

Automatic Approval through Reserve Bank of India is available for all items/activities except a few as given in the Press Note No.4(2006series)

No prior approval required. The company is only required to report to RBI within 30 days of receipt of foreign equity/allotment of shares.

b Foreign Investment Promotion Board (FIPB) approval - required for all other proposals not eligible for Automatic Approval.

3.2. OTHER PROCEDURES & REQUIREMENTS

Besides of the basic incorporation steps other procedures & requirements must be fulfilled.

3.2.1. Other Procedures

Permanent Account Number (PAN).

This is a unique number issued by Income Tax department to Company/LLP for tax filing. This number is mandatory for doing business in incorporated business.

TAN (Tax Account Number)

This number is issued by Income tax department for filing of Tax Deducted at Source (TDS). Many of the transactions requires deduction of tax at source and this number is required for proper compliance.

Service Tax Registration

If the company/LLP provides taxable services, collection of services tax is compulsory. Such service provider shall register and obtain Service Tax Registration.

Value Added Tax

Value Added Tax and Central Sales tax registration is compulsory for Companies/LLPs dealing in taxable goods. It is a state matter and if Companies/LLPs deals locally in different states, separate registrations are required for each state.

Import Export Code

Import and Export Code number is compulsory for companies/LLPs planning for import and export of goods.

Shops & Establishment Registration

A statement containing the employer's and manager's name and the establishment's name (if any), postal address, and category must be sent to the local shop inspector with the applicable fees. New Business Forms shall register within 30 days from the date on which the it commences its operation.

Professional Tax

Every employer (Company/LLP) shall register with prescribed authorities and pay professional tax on yearly basis. Employee registration is also required in some cases and professional tax needs to be paid to local government.

3.2.2. Other Requirements

Accounts & Auditors

Every company is required to appoint an auditor each year at its AGM. An auditor must be qualified by virtue of the Institute of Chartered Accountants of India Act 1949 and completely independent of the company. Audited accounts of the company serve as tool for various stakeholders like creditors, bankers, investors and revenue authorities.

Public Filings

The names and personal particulars of the directors and secretary, register of charges, share capital, registered office address etc. must be filed with the Companies Registry for public inspection upon incorporation and if there is any change thereafter.

Annual Meetings

An annual general meeting (AGM) must be held once in every financial year and not more than 6 months after the end of financial year. However, a company need not hold its first AGM until 18 months of its incorporation.

Fees and duties

A WOS or JVC in India will be required to pay the same registration fees as any other company in India. The fees vary according to the amount of the nominal share capital of the company. The fees vary according to the amount of the nominal share capital of the company. The table of fees is set out in Sch X of the Companies Act.

4. TAXATION

4.1. COMMON TAX REGULATION IN INDIA

Indian Tax System is composed by the following main taxes.

Individual Income Tax Rates		
Taxable Income		Tax Rate
Over	Not Over	
0	Rs. 160,000 [1]	0%
Rs. 160,001	Rs. 300,000	10%
Rs. 300,001	Rs. 500,000	20%
Rs. 500,001	above	30% [2]

1. Rs. 190,000 for women and Rs. 240,000 for seniors.

2. An education cess of 3% is applicable.

3. (a) Tax exemption on interest in Non-Resident (external) Account and on interest payable by a scheduled bank to Non-Resident Indians (NRI's). (b) Tax exemption on the interest payable by a scheduled bank to a non-resident or a person who is not ordinarily resident on deposits in foreign currency where the acceptance of such deposits by the bank is approved by the RBI. .

Domestic Corporate & LLP Income Taxes Rates		
	Tax Rate	Effective Tax Rate with surcharge & ed. cess
Domestic Corporations / Private Limited Companies	30%	33.99% [1]
Domestic Corporations / Public Limited Companies	30%	33.99% [1]
Limited Liability Partnership (LLP's)	30%	30.9% [2]

1. A surcharge of 10% of the income tax is levied, if the taxable income exceeds Rs. 1 million. Educational Cess (3% on tax) is also added.

2. An Educational Cess is added to the basic tax rates. Surcharge is not applicable to LLP In India tax an LLP is required to pay income tax on 40% of its income; since an LLP is allowed to pay the balance of 60% as remunerations to it partners. Partners of an LLP are required to pay tax on the amount paid to them. Besides, LLP's are not required to pay dividend distribution tax or Minimum Alternate Tax (MAT).

Foreign Corporate Income Tax Rates		
	Withholding Tax Rate for non-treaty foreign companies	Withholding Tax Rates for the Companies Doing Business in India under a Tax Treaty
Dividends	20%	Depending on Country [1]
Interest Income	20%	Depending on Country [1]
Royalties	30%	Depending on Country [1]
Technical Services	30%	Depending on Country [1]
Other income	55%	55%

1. India has entered into tax treaties with a number of countries including Australia, Austria, Bangladesh, Belgium, Brazil, Belarus, Bulgaria, Canada, China, Cyprus, Czechoslovakia, Denmark, Finland, France, Germany, Greece, Hungary, Indonesia, Israel, Italy, Japan, Jordan, Kazakhstan, Kenya, Libya, Malta, Malaysia, Mauritius, Mongolia, Namibia, Nepal, Netherlands, New Zealand, Norway, Oman, Philippines, Poland , Qatar , Romania, Singapore, South Africa , South Korea , Spain , Sri Lanka , Sweden, Switzerland, Syria, Tanzania, Thailand, Trinidad & Tobago, Turkmenistan, Turkey , U.A.E. , U.A.R., U.K., U.S.A., Russian Federation, Uzbekistan, Vietnam and Zambia.

These treaties endeavour to avoid double taxation and attract know- how and technology. In many treaties the withholding tax on royalties and fees for technical services emanating from India is lower than the general tax rate. A careful planning and corporate structuring can reduce the tax obligations considerably. The following treaties have been successfully used by international investors to reduce their tax obligations in India and in their home countries:

(a) India - U.S.A. Tax Treaty

The Indo-U.S. tax treaty considerably reduces the withholding tax in India for royalties, fees for technical services, and for interest paid to the US banks and financial institutions. The withholding tax on dividends arising out of India is 15%, if the parent company owns at least 10% of the voting stock. The withholding tax on royalties and technical services fees is at the rate of 15%. The capital gains is taxed at a rate of 20%. The withholding tax on rental of equipment and interest paid to U.S. banks and financial institutions is at the rate of 10%. All these rates are lower than the regular withholding tax rates.

(b) India - Mauritius Tax Treaty

The withholding tax rates for dividends and capital gains can be reduced further by a careful corporate structuring and tax planning. The Indo-Mauritius tax treaty offers reduced withholding taxes for companies incorporated in the island country of Mauritius. Recently some U.S. companies have invested in India through offshore subsidiaries incorporated in Mauritius. For companies incorporated in Mauritius there is no withholding tax on capital gains in India and the withholding tax on dividends is only 5%. The companies incorporated in Mauritius, at present, can opt not to pay any tax in Mauritius.

Wealth Tax		
Net Taxable Wealth		Tax Rate
Over	Not Over	
0	Rs.1,500,000	0
Rs.1,500,000	above	1%

Wealth tax is levied on non-productive assets whose value exceeds Rs.1.5 million. Productive assets like shares, debentures, bank deposits and investments in mutual funds are exempt from wealth tax. The non-productive assets include residential houses, jewellery, bullion, motor cars, aircraft, urban land, etc. Foreign nationals are exempt from wealth tax on non-Indian assets. In arriving at the net taxable wealth, any debt incurred in acquiring specified assets is deductible.

Fringe Benefit Tax Rates		
	Taxable Percentage	Effective Tax Rates
Medical reimbursements	20%	6.8%
Telephone bills	20%	6.8%
Employee Stock Options (*Difference between market value and purchase price on vesting date*)	100%	33.99%

From April 1, 2007 , Employees Stock Option Plan (ESOP) or Sweat Equity has also been brought within ambit of fringe benefit tax. Section 115WB(1)(d) specifies that any ESOP will attract Fringe Benefit Tax, and the benefit is equal to the difference between the price paid and the fair market value of the share, as determined by the Board. Tax is levied on the date of vesting of such options. "Fair Market Value" is not yet defined by the Income Tax Department.

Fringe Benefit Tax is a tax payable by companies against benefits that are seen by employees but cannot be attributed to them individually. This tax is paid as 33.99% of the benefit, which is only a percentage of the actual amount paid.

Tax on cash withdrawal from banks
Withdrawn in the 2008 Budget. 0.1% tax used to be levied on cash withdrawals of over Rs 25,000 from banks on a day.

Gift Tax		
Net Taxable Gift		Tax Rate
Over	Not Over	
0	Rs.30,000	0
Rs.30,000	above	30%
Gifts to dependent relatives at the time of marriage are exempt up to Rs.100,000. Foreign nationals are exempt from gift tax on non-Indian assets.		

4.2. SPECIAL CASES & INCENTIVES

Corporate Income Tax Special Rates

Revenue accruing to foreign companies (including royalty and technical services fees) from providing services concerning the exploration or production of petroleum or natural gas is subject to a maximum tax on a deemed profit of 10% of gross revenue.

Foreign companies engaged in the execution of turnkey power project contracts approved by the government and financed by international programs are subject to a maximum tax on a deemed profit of 10% of gross revenue.

Non-Export Incentives

India offers a wide range of concessions to investors to provide incentives for economic and industrial growth and development. India's tax rates may not be one of the lowest in the world, but a careful tax planning keeping in mind the tax holidays and the following general tax incentives reduce the taxes considerably:

- No corporate taxes are levied for a period of five years for projects set up for domestic power generation and transmission and also for projects in Electric Hardware Technology Park Schemes.
- Deduction of preliminary and preoperative expenses incurred in setting up a project
- Complete tax exemption on profits from exports of goods
- Full or partial exemption of foreign exchange earnings on construction projects, hotel and tourism related services, royalties, commission, etc.
- Liberal depreciation allowances
- Deduction of capital research and development expenditures
- New industrial undertakings may deduct 25% of their gross total income for eight years

Export Incentives

The New Export-Import Policy of 1992 provides substantial tax incentives for investments in Export Oriented Units ("EOU's") and industries located in the Export Processing Zones ("EPZ's"). Automatic approvals are given by the Secretariat for Industrial Approval for setting up 100% Export Oriented Units ("EOU’s"). Incentives and facilities available under the EOU’s scheme include concessional rent for lease of industrial plots, preferential power allocation and supply, exemption from import duty for capital goods and raw materials for power sector industries as well as for trading companies primarily engaged in export activity.

There are six EPZ's or free trade zones located in different parts of the country. These zones are designed to provide internationally competitive infrastructure facilities and duty-free and low cost environment. Various monetary and non-monetary incentives are granted which include import duty exemption, complete tax holiday, decentralized "single window clearance," etc.

Twenty-five percent of goods manufactured in EPZ's are permitted to be sold in the domestic market. No excise duty is payable on such items and customs duties on imported components is 50% of normal rates. Major exporters are allowed to operate bank accounts abroad to facilitate trade. Companies that sell in the domestic market as well as international markets may deduct export earnings from their tax liabilities.

Exporters and other foreign exchange earners have been permitted to retain 25% of their foreign exchange earnings in foreign currency. For 100% Export Oriented Units and units in Export Processing Zones, Electronic Hardware Technology Parks, retention up to 50% is allowed.

Other incentives include:

- Duty-free imports of raw materials and components.
- Tax holiday for a period of 5 continuous years in the first 8 years from the year of commencement of production.
- Exemption from taxes on export earnings even after the period of tax holiday.
- Exemption from central and state taxes on production and sale.
- Permission to install machinery on lease.
- Freedom to borrow self-liquidating foreign currency loans at the prime rate of interest.
- Inter-unit transfers of finished goods among exporting units.
- Decentralized single-window clearance of proposals concerning units in Export Processing Zones.
- EOU/EPZ units may export through Export Houses, Trading Houses and Star Trading houses.