Adil K. Kotwal
and
Sunil P. Hansraj

Partners of
Chandabhoy & Jassoobhoy
Chartered Accountants
Mumbai, India

Special Consultants to Tax Management

Adil K. Kotwal, B.Com, F.C.A., Bachelor of Commerce, University of Bombay (1978), Fellow of the Institute of Chartered Accountants of India. He joined the firm in 1978 and is currently the Managing Partner and partner responsible for the firm's corporate finance and management consultancy and advisory practice. He has served as visiting faculty with the University of Bombay teaching Accountancy and Taxation.

Sunil P. Hansraj, B.Com, F.C.A., University of Bombay (1988), Fellow of the Institute of Chartered Accountants of India. He joined the firm in 1988 and is the partner responsible for the firm's practice relating to international taxation and advisory services to foreign clients investing in India.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Portfolio Description

Leonard L. Silverstein, Esq.
Advisory Board Chairman
Technical Director

Gerald H. Sherman, Esq.
Deputy Technical Director

Patricia R. Lesser, Esq.
Deputy Technical Director
for Foreign Country Taxation

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Portfolio Description

PORTFOLIO DESCRIPTION

Tax Management Portfolio, *Business Operations in India*, No. 966-4th, analyzes India's Companies Act, foreign investment policies, foreign exchange management, anti-competition legislation, Income Tax Act, the liberal tax concessions granted for new investments and industrial undertakings, the special concessions for foreign enterprises and the provisions for the computation of the taxable income of nonresidents. Some indirect taxes such as excise and customs (import) duty, sales tax, value added tax and stamp duty are also discussed. Other topics explained in detail are foreign technology agreements, policies for setting up a 100% export-oriented unit and the legislation for troubled industrial companies.

The Worksheets feature a checklist of transactions, guidelines and government policies having corporate and tax significance.

This Portfolio may be cited as Kotwal and Hansraj, 966-4th T.M., *Business Operations in India.*

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Portfolio Description

Table of Abbreviations

ADR	**American Depository Receipt**
BIFR	**Board for Industrial and Financial Reconstruction**
CA	**Companies Act, 1956, as amended**
CBDT	**Central Board Of Direct Taxes**
CCI	**Competition Commission of India**
CEA	**Central Excise and Salt Act, 1944**
CEGAT	**Customs, Excise and Gold Appellate Tribunal**
CVD	**Countervailing Duty**
DIPP	**Department of Investment Policy and Promotion**
DPIN	**Designated Partner Identification Number**
ECBs	**External Commercial Borrowings**
EEFC	**Exchange Earners' Foreign Currency**
EHTP	**Electronic Hardware and Technology Park**
EOU	**Export Oriented Undertaking**
EPZ	**Export Processing Zone**
FCCB	**Foreign Currency Convertible Bonds**
FCEBs	**Foreign Currency Exchangeable Bonds**
FDI	**Foreign Direct Investment**
FEMA	**Foreign Exchange Management Act**
FII	**Foreign Institutional Investors**
FIPB	**Foreign Investment Promotion Board**
FTZ	**Free Trade Zone**
GDR	**Global Depository Receipts**
HSN	**Harmonized System of Nomenclature**
HUF	**Hindu Undivided Family**
ICAI	**Institute of Chartered Accountants of India**
IDR	**Indian Depository Receipt**
IMF	**International Monetary Fund**
ITA	**Income Tax Act, 1961**
JV	**Joint Venture**
LIBOR	**London Interbank Offered Rate**
LLP	**Limited Liability Partnership**
MRTP	**Monopolies and Restrictive Trade Practices**
NCLT	**National Company Law Appellate Tribunal**
NOR	**Not Ordinarily Resident**
NRI	**Non-Resident Indian**
OCB	**Overseas Corporate Body**
OTCEI	**Over The Counter Exchange of India**
PAN	**Permanent Account Number**
PE	**Permanent Establishment**
RBI	**Reserve Bank of India**
SEBI	**Securities and Exchange Board of India**
SEZ	**Special Economic Zone**
SIA	**Secretariat of Industrial Assistance**
SPV	**Special Purpose Vehicle**
STP	**Software Technology Park**
TDRs	**Transferable Development Rights**
ULIP	**Unit Linked Insurance Plan**
VAT	**Value Added Tax**
WOS	**Wholly-Owned Subsidiary**
WTO	**World Trade Organization**

KEY FACTS

Area	**1,269,219 square miles**
Capital	**New Delhi**
Climate	**Tropical monsoon climate, with numerous climatic zones.**
Population	**1,028 million** * * www.censusindia.gov.in/Census_Data_2001
Languages	**22 languages,** ** **of which Hindi is the official language and English is the associate official language.** ** As set forth in the Constitution.
Workforce/Education	**64.8% literacy rate, with great regional variation.**
Unemployment	
GDP	
GDP Growth (Decline)	
Inflation	
Balance of Payments Surplus (Deficit)	
Currency	**Rupee (Rs.), subdivided into 100 paise.**
Membership of economic groups/ organizations	
Major industries	
Infrastructure	**Largest railway system in Asia and fourth largest in the world; extensive air service; 12 major ports; well-developed modern means of communication.**
Websites:	• **http://www.sebi.gov.in** • **www.sezindia.nic.in** • **www.rbi.org.in** • **www.finmin.nic.in** • **Authority for Advance Rulings (www.aar.gov.in)**

A. Geography

India is the largest country in South Asia and the seventh largest in the world. The neighboring countries to the north are China (PRC), Nepal and Bhutan; to the east, Bangladesh and Burma; and to the west, Pakistan and Afghanistan. To the south the country tapers off into the Indian Ocean. The Palk Strait separates the island country of Sri Lanka from the southeast coast of India.

India is a subcontinent flanked by the Himalayas to the north, the Arabian Sea to the west, the Bay of Bengal to the east and the Indian Ocean to the south. It has a land frontier of 9,445 miles (15,200 kilometers) and a coastline of 4,670.5 miles (7516.5 kilometers). The Andaman and Nicobar Islands in the Bay of Bengal and Lakshadweep Islands in the Arabian Sea are part of the territory of India.

B. Climate

India has a tropical monsoon climate. Because of India's size and wide variations in altitude, there are a number of climatic zones in the country. The great Himalayan mountain barrier stops the northern winter from blanketing India and thus keeps it pleasant in winter, except for Kashmir and the hill stations in the Himalayas, where the temperature in winter drops to 5°F.

Rainfall in India is unevenly distributed. Areas such as the west coast, and Bengal and Assam in the east get the heaviest rainfall, more than 75 inches a year. Rajasthan and the high Ladakh plateau of Kashmir receive less than four inches a year. At the other extreme, Mawsynram in Assam in the northeast gets rainfall of over 467 inches, the highest rainfall in the world.

The seasons recognized by the Indian Meteorological Department are the cold weather season (December to March); the hot weather season (April and May); the rainy season (June to September); and the season of retreating southwest monsoons (October and November).

C. Population

India is the second most populous country in the world. Nearly 27.78% of India's population lives in urban areas; 72.22% lives in rural areas. The country has more than 35 cities with a population of more than 1 million (Census Data, 2001).

D. Transportation

India has an excellent network of roads and a railway network of about 39,435 miles (64,465 kilometers). The railways play a crucial role in India's development.

India has 12 major and 187 minor/administrative ports. The major ports handle 90% of all India's port traffic.

India is well served by air transport. Air India is the country's international carrier. The world's airlines fly to and through India and several domestic carriers provide extensive air services within the country, with some domestic carriers also servicing international sectors.

E. Communications

India has an excellent network of post offices, telegraph offices, telephone, telex, and facsimile facilities. E-mail and Internet is available for internal and external communications.

F. Political Structure

India is the largest democracy in the world and has adopted a parliamentary system of government with two legislative houses. The country is a union of 28 states, six union territories and one National Capital Territory, Delhi. The central government in New Delhi has exclusive jurisdiction over all matters of national interest, such as defense, communications, banking and currency, international trade and foreign affairs. The state governments have primary responsibility for matters such as law and order, education, health and agriculture.

The central government comprises a council of ministers headed by a Prime Minister. The Prime Minister is the head of the party commanding a majority in the Parliament. Parliamentary elections are generally held once every five years.

The Right to Information Act 2005 establishes the right of citizens to access information under the control of public authorities, promotes transparency and accountability in the working of every public authority, and establishes a central information commission and state information commissions.

G. Judiciary

India has a well-established, independent judicial system. The Supreme Court of India, the highest court of appeal in New Delhi, and High Courts in the states, along with subsidiary district courts, enforce the rule of law and ensure the fundamental rights of citizens, which are guaranteed by the constitution.

H. Banking

The country's banking system is controlled by the Reserve Bank of India. The functions of the Reserve Bank are divided into two separate departments:

(i) The issue department, which looks after the issue of currency; and

(ii) The banking department, which regulates and supervises Indian banking.

The commercial banking system is fully developed and consists of about 300 commercial banks, almost all of which undertake foreign exchange transactions. Many cooperative banks and foreign banks have fully operational branches in the major cities.

I. Quality of Life

India has an ancient culture with a rich tradition and history dating back several thousand years. It is a totally nonsectarian society where all the religions of the world may be practiced.

The educational system is of a fairly high standard and consists of public and private schools, universities, and institutions of higher learning, providing academic and vocational training and opportunities for participation in sports and extra-curricular activities.

India boasts a host of tourist attractions — from historical monuments like the world-famous Taj Mahal to the beach resorts in the south. The Himalayas offer a unique experience of scenic beauty and sports. Excellent accommodation and transport facilities are available at tourist centers.

A. The Indian Economy

1. Introduction

Until 1947, the Indian economy was characterized by subsistence agriculture and a few organized industries. Since then, India has achieved considerable economic development through a planned program that fixed strict priorities for the limited available resources. This was effected by a series of five-year plans that have transformed the Indian economy and given India a strong impetus toward becoming a leading industrial nation.

India has a mixed economy in which both the public and the private sectors play an important role. The public sector plays an active part in creating infrastructure and building core industries that require substantial investment. The government has a set program for divesting of its ownership in several large public sector companies with a view to

increasing the professionalism of their management. The entrepreneurial talent of the private sector has taken advantage of the country's infrastructure to develop industries that manufacture a wide variety of articles.

Rapid industrialization has required the importation of large quantities of capital goods, technology and finance. To pay for these imports, it has been imperative for India to enter the highly competitive international export market. Exports, therefore, have priority in government economic policy.

India manufactures a wide range of sophisticated products such as machinery, chemicals, precision tools, electronic components and nuclear energy. This has been made possible by the government's industrial policy, which has given India a solid industrial base. As a result, India has flourishing exports in the engineering goods sector and has completed a number of projects on a turnkey basis.

India has emerged as a world leader in information technology as a result of its large pool of skilled information technology professionals. India also has a large pool of trained engineers, technicians, artisans and professionals, which has assisted the country's rapid industrialization.

2. Economic Factors

A foreign investor wishing to carry on business in India will find tremendous opportunities — India is ready for rapid industrialization and government policy welcomes foreign participation in almost all fields. India by itself is one of the largest markets in the world.

Over the years, India has needed sophisticated technology, raw materials and capital goods to develop industry and infrastructure for its ambitious expansion program in oil and gas exploration, coal mining, electricity generation and alternative energy sources, ship building, port expansion and transportation. India is undergoing a revolution in its telecommunications industry and in computer technology, as regards both hardware and software.

India has gone through more than a decade of economic reforms. Continuity in the economic liberalization process and the political consensus that economic change necessitates has set India on the path of growth.

India's foreign currency assets have been increasing steadily. Foreign currency reserves (including valuation changes) as of October 30, 2009 were US$ 284.4 billion. In recent years, India's balance of payments has been characterized by surplus in both the current and capital accounts. The steady accumulation of reserves, made possible by a strong balance of payment position in recent years, has made India as the sixth largest reserve holder in the world. These reserves provide India with an opportunity to engage in further trade reforms.

Continuing liberalization in India's foreign direct investment (FDI) policy and the simplification of procedures are contributing immensely to attracting increased FDI in India. The fact that the Government now conducts an annual review of the FDI policy and procedures has given foreign investors added confidence that their concerns are being addressed on an ongoing basis.

FDI equity inflow during the financial year 2008-09 of nearly US$ 27.31 billion represents growth of 11% over the inflow received in the previous year. This was the highest FDI equity inflow into the country in any financial year since the commencement of economic reforms. During the first quarter of calendar year 2009, the FDI inflow was US$ 6.16 billion, as compared to US$ 11.90 billion for the corresponding quarter in 2008. The cumulative FDI equity inflows in India during the period August 1991 to March 2009 were US$ 108.86 billion.

3. India as an Investment Location

There are a number of good reasons for investing in India including:

(i) A stable democratic environment after more than 50 years of independence;

(ii) A large market with a middle class population of 250-350 million that has increasing purchasing power, as reflected in the remarkable increase in the purchase of consumer durables in recent years;

(iii) Access to regional international markets through India's membership of regional integration frameworks such as the South Asian Association for Regional Cooperation;

(iv) The fact that foreign investment is welcomed in almost all sectors barring those of strategic concern such as defense and atomic energy;

(v) The fact that India's foreign investment policy is among the most liberal and attractive of those of the emerging economies. Policy-based initiatives are constantly being launched by the Government in specific sectors such as telecoms, ports, airports, etc.;

(vi) The suitability of the Indian economy for small and medium-sized companies, which are now finding it difficult to operate in the saturated western markets;

(vii) India's emergence as an across the board, low-cost base, to which multinationals may relocate. More than 100 Fortune-500 companies now have a presence in India;

(viii) A large and diversified infrastructure spread across the country;

(ix) An emphasis on technology, innovation and development of the knowledge base;

(x) Substantial manufacturing capacity, spanning almost all kinds of manufacturing activities;

(xi) A developed banking system — a commercial banking network of over 71,000 branches, supported by a number of national and state level financial institutions;

(xii) A vibrant capital market comprising 23 stock exchanges with over 10,000 listed companies;

(xiii) The introduction of futures trading in selective commodities on three national exchanges and 21 regional exchanges;

(xiv) Increasing investment by Private Equity Funds over the last two years;

(xv) Legal protection for intellectual property rights;

(xvi) An import regime in conformity with World Trade Organization (WTO) commitments — quantitative restrictions on the importation of goods into India only in the case of certain items on grounds of national security, defense and health;

(xvii) The increased role of private and foreign investment in the Indian economy;

(xviii) The competitiveness of the rates of direct and indirect tax;

(xix) Special investment and tax incentive for export in certain sectors such as power, electronics, software, business process outsourcing and food processing;

(xx) Full convertibility of the rupee on current account and progressive liberalization of convertibility on capital account;

(xxi) The availability of skilled manpower and professional managers;

(xxii) The fact that English is the preferred business language;

(xxiii) A well-developed insurance and financial services sector;

(xxiv) Well-developed accountancy, legal, actuarial and consultancy professions; and

(xxv) A well-established legal system with an independent judiciary.

B. Foreign Investment

1. Foreign Investment Policy

The Indian Government's approach to foreign investment has undergone a major change over the last two decades. The central government's liberalization and economic reforms program aims at rapid and substantial growth, and integration with the global economy in a harmonized manner. Industrial policy reforms have removed almost all industrial licensing requirements and restrictions on investments and expansion, and facilitated access to foreign technology and foreign direct investment.

All industrial undertakings are exempt from industrial licenses to manufacture, except for industries reserved for the public sector (see the Worksheets) and industries retained under compulsory licensing (see the Worksheets).

a. Foreign Direct Investment

Government policy guidelines for foreign investment in India are reviewed on an ongoing basis in line with industrial and financial changes. Regulations have been structured to identify industrial sectors (with or without sectoral caps) for investment, to minimize procedural formalities and to introduce an "Automatic Route" for foreign investors, allowing them to make investments merely by informing the Reserve Bank of India (RBI). Changes in the sectoral policy/sectoral equity cap are made through press releases issued by the Secretariat of Industrial Assistance (SIA), Department of Investment Policy and Promotion (DIPP). All press releases are available at the DIPP website (www.dipp.gov.in).

The central government encourages FDI, i.e., investment by foreign entities and nonresident Indians, to complement and supplement domestic investment.

Note: **In September 2003, the Government "de-recognized" Overseas Corporate Bodies (OCBs) as an eligible, special "class of investor" under various routes/schemes. Under the Foreign Exchange Management Regulations, this has resulted in the withholding of all special facilities available to OCBs, including the following: (i) an OCB is not permitted to make any fresh investment under an FDI scheme, except to the extent permitted to any foreign investor; (ii) an OCB is not permitted to make a fresh investment in shares or convertible debentures on a nonrepatriation basis; (iii) fresh investment in government dated securities, treasury bills, units of domestic mutual funds, units of money market mutual funds, or National Saving Certificates on a repatriation or a nonrepatriation basis is prohibited; (iv) a person resident outside India and an OCB are not permitted to transfer shares or convertible debentures to another OCB, whether the transfer is by way of sale or by way of gift; (v) fresh investment on a rights basis in equity/preference shares and convertible debentures is prohibited; (vi) a person resident in India is not permitted to borrow from an OCB in foreign currency; (vii) an Indian Company is not permitted to borrow in the form of nonconvertible debentures on either a repatriation or a nonrepatriation basis; and (viii) a person resident in India is not permitted to borrow from an OCB on a nonrepatriation basis. OCBs are permitted to hold existing investments in shares or debentures whether on a repatriation or a nonrepatriation basis, until they are sold or redeemed.**

FDI may be made by a person resident outside India (other than a citizen of Pakistan) or by an entity incorporated outside India (other than an entity incorporated in Pakistan) with respect to most activities using the Automatic Route, in which case no prior regulatory approval is needed. In the case of other items or activities or investments by citizens of Bangladesh or by an entity incorporated in Bangladesh, FDI requires central government approval, which is accorded at the recommendation of the Foreign Investment Promotion Board (FIPB).

The terms and conditions governing FDI are contained in Schedule I to the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 notified by the RBI in pursuance of the Foreign Exchange Management Act, 1999 (FEMA). The terms and conditions are described in (1), below.

(1) Automatic Route of Reserve Bank of India for Issue of Shares by an Indian Company

(a) General

An Indian company that is not engaged in any activity, or in the manufacturing of an item included in the List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or Items for which FDI is Prohibited (see the Worksheets) may issue shares (equity or fully and mandatorily convertible preference shares) or fully and mandatorily convertible debentures, subject to pricing guidelines/valuation norms, to a person resident outside India, up to the extent specified for the relevant sector in the Sector Specific Guidelines for Foreign Direct Investment (see the Worksheets) in accordance with the entry route specified therein and subject to compliance with the provisions of the FDI Policy as notified by the SIA in the Ministry of Commerce and Industry. The shares or convertible debentures must not be issued by the Indian company with a view to acquiring existing shares of any Indian company.

Note: **A company that proposes to embark on an expansion program to undertake activities or manufacture items included in the Sector Specific Guidelines for Foreign Direct Investment (see the Worksheets) may issue shares or debentures out of fresh capital proposed to be issued by it for purposes of financing the expansion program, to the extent indicated in the Guidelines, subject to compliance with the provisions therein.**

Note: **Issue of other types of preference shares, such as nonconvertible, optionally convertible or partially convertible shares, are considered debt and, consequently, the guidelines relating to External Commercial Borrowings (ECBs) will apply. Since these instruments are denominated in rupees, the rupee interest rate will be based on the swap equivalent of the London Interbank Offered Rate (LIBOR) plus the spread permissible for ECBs with corresponding maturity. As far as debentures are concerned, only those that are fully and mandatorily convertible into equity within a specified time will be considered equity under the FDI policy.**

Erstwhile OCBs that are incorporated outside India and are not under adverse notice of the RBI may make fresh investments under the FDI rules as incorporated nonresident entities, with the prior approval of the FIPB if the investment are made via the Approval Route, and with the prior approval of the RBI if the investments are made via the Automatic Route.

(b) Foreign Investment in Small Scale Industrial Units

A company that is a small scale industrial unit and is not engaged in any activity or in the manufacture of prohibited items included in the List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or Items for which FDI is Prohibited (see the Worksheets) may issue shares or convertible debentures to persons resident outside India, to the extent of 24% of its paid-up capital.

Such a company or unit may issue shares in excess of 24% of its paid-up capital if:

(i) It has given up its small-scale status;

(ii) It is not engaged or does not propose to engage in the manufacture of items reserved for the small scale sector; and

(iii) It complies with the ceilings specified in the List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or

Items for which FDI is Prohibited (see the Worksheets).

Note: **The company or unit would be reckoned to have given up its small scale status if the investment in plant and machinery exceeds the limits prescribed under the Micro, Small and Medium Enterprises Development Act, 2006.**

(c) Foreign Investment in a Small Scale Industrial Export Oriented Unit, or a Unit in a Free Trade Zone or Export Processing Zone, or in a Software Technology Park or Electronic Hardware Technology Park

A small scale industrial unit that is an Export Oriented Unit or a small scale industrial unit in a Free Trade Zone or Export Processing Zone, or in a Software Technology Park or an Electronic Hardware Technology Park may issue shares or fully and mandatorily convertible debentures/preference shares to a person resident outside India in excess of 24% provided it complies with the ceilings specified in the List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or Items for which FDI is Prohibited (see the Worksheets).

(d) Conversion of External Commercial Borrowing/ Lump-Sum Fee, Etc.

Indian companies have been granted general permission for the conversion of ECBs into shares/preference shares, subject to the following conditions and reporting requirements:

(i) The activity of the company is covered under the Automatic Route for foreign direct investment or the company has obtained Government approval for foreign equity in the company;

(ii) After the conversion of the ECB into equity, the foreign equity is within the sectoral cap, if any;

(iii) The pricing of the shares complies with Securities Exchange Board of India (SEBI) regulations or the guidelines of the erstwhile Controller of Capital Issues [1] in the case of listed or unlisted companies respectively; and

(iv) The company complies with the requirements prescribed under any other statute or regulation in force.

---

[1] The Controller of Capital Issues was empowered as the sanctioning authority for any reorganization of the capital structure of public limited companies. The office is now defunct. However, the Reserve Bank of India (RBI), the Ministry of Corporate Affairs and the Securities Exchange Board of India (SEBI) follow the guidelines issued by the Controller of Capital Issues for pricing shares. The office is therefore referred to as the "*erstwhile* Controller of Capital Issues."

The conversion facility is available for ECBs availed of under either the Automatic or the Approval Route and is applicable to ECBs, whether or not due for payment, as well as secured or unsecured loans availed of from nonresident collaborators.

General permission is also available for the issue of shares or preference shares against lump-sum technical know-how fees or royalties, under the Automatic Route or the Approval Route, subject to pricing guidelines set by the SEBI/Controller of Capital Issues and compliance with applicable tax laws.

Units in Special Economic Zones (SEZs) are permitted to issue equity shares to nonresidents against the import of capital goods subject to valuation performed by a committee consisting of the Development Commissioner and the appropriate customs officials. Details of the issue of shares against the conversion of ECBs must be reported to the relevant regional office of the RBI. The SEZ unit issuing equity is also required to report on the particulars of the shares issued.

(e) Foreign Investment in Asset Reconstruction Companies

Asset Reconstruction Companies (ARCs) that are registered with the RBI may issue up to 49% of their paid-up capital to a person resident outside India with FIPB approval. The Automatic Route is not available for such investments. Further, such investments may only be in the nature of FDI and investments made by Foreign Institutional Investors (FIIs) are not permitted. However, FIIs registered with the SEBI may invest in Security Receipts (SRs) issued by registered ARCs. FIIs may invest up to 49% of each tranche of SRs issued, subject to the condition that the investment made by a single FII may not, in a tranche of SRs, exceed 10% of the issue.

(f) Investment in Infrastructure Companies in the Securities Market

FDI is permitted in infrastructure companies in the securities market, namely stock exchanges, depositories and clearing corporations, in compliance with regulations issued in this regard by the SEBI, subject to the following:

(i) Aggregate foreign investment of up to 49% of the paid-up capital is permitted, with a separate FDI cap of 26% and an FII cap of 23%;

(ii) FDI is permitted only with the specific prior approval of the FIPB; and

(iii) FIIs may invest only through purchases on the secondary market.

(g) Investment in Credit Information Companies

Foreign investment in Credit Information Companies is permitted in compliance with the Credit Information Companies (Regulations) Act, 2005, subject to the following:

(i) Aggregate foreign investment of up to 49% of the paid up capital is permitted, with a separate FDI cap of 25% and an FII cap of 24%;

(ii) FDI up to 49% is allowed only with the prior approval of the FIPB and regulatory clearance from the RBI;

(iii) Investment by FIIs registered with the SEBI is permitted only through purchases on the secondary market to the extent of 24%; and

(iv) No FII may individually hold, directly or indirectly, more than 10% of the equity of a Credit Information Company.

(h) Investment in Commodity Exchanges

Foreign investment in Commodity Exchanges is permitted subject to the following conditions:

(i) Aggregate foreign investment of up to 49% of the paid up capital is permitted, with a separate FDI cap of 26% and an FII cap of 23%;

(ii) FDI is allowed with the specific prior approval of the FIPB;

(iii) The FII purchase of equity in Commodity Exchanges is restricted to the secondary markets; and

(iv) Foreign investment in Commodity Exchanges is also subject to compliance with the regulations issued, in this regard, by the Forward Market Commission.

(i) Investment in Public Sector (Nationalized) Banks

FDI and foreign portfolio investment in nationalized banks is subject to overall statutory limits of 20% as provided under Section 3 (2D) of the Banking Companies (Acquisition & Transfer of Undertakings) Acts. The same ceiling would also apply in respect of such investments in the State Bank of India and its associate banks.

(2) Issue of Shares by a Company Requiring Government Approval

An Indian company may issue shares to a person resident outside India in accordance with the regulations only with the prior approval of the FIPB in the following circumstances:

(i) The company is engaged or proposes to engage in any permitted activity specified in the List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or Items for which FDI is Prohibited (see the Worksheets) that specifically requires approval;

(ii) The activity falls under the FIPB route as stipulated in the Sector Specific Guidelines for Foreign Direct Investment (see the Worksheets);

(iii) The company proposes to issue shares to a person resident outside India against consideration other than inward remittance, i.e., against royalties or lump sum fees due for payment; and

(iv) The company proposes to issue shares against ECBs (excluding deemed ECBs) received in convertible foreign currency.

Specifically, a person who is a citizen of Bangladesh or an entity incorporated in Bangladesh requires the prior approval of the FIPB to purchase shares and convertible debentures of an Indian company.

The FIPB was set up as a fast track mechanism to encourage and facilitate foreign investment in large projects in India. The FIPB also grants composite approvals involving foreign technical collaborations and the setting up of Export Oriented Undertakings (EOUs) involving foreign investment/technical collaboration.

The FIPB considers proposals for approval that do not qualify for the Automatic Route. Applications to the FIPB for the approval of foreign investment must include the following information:

(i) Whether the applicant has any previous financial/technical collaboration or trademark agreement in India in the same field as that for which approval is sought or an allied field; and

(ii) If so, details thereof and the justification for proposing the new venture/technical collaboration (including trademarks).

Indian companies obtaining foreign investment approval through the FIPB route do not require any further clearance from the RBI for purposes of receiving inward remittances and issuing shares to foreign investors. Such companies are, however, required to notify the relevant RBI Regional Office of the receipt of inward remittances within 30 days of such receipt and to file the required documents with the relevant RBI Regional Offices within 30 days after issuing shares to foreign investors.

(3) Guidelines for the Calculation of Foreign Investment

The Government of India has issued separate guidelines (Press Note 2 (2009 series) and Press Note 4 (2009 series)) for the calculation of total foreign investment, i.e., the aggregate of direct and indirect foreign investment in Indian companies (see the Worksheets).

b. Other Modes of Foreign Direct Investment

(1) Issue of Shares by International Offering Through American Depository Receipts and/or Global Depository Receipts

An Indian company may issue its rupee denominated shares to a person resident outside India, being a depository for purposes of issuing Global Depository Receipts (GDRs) and/or American Depository Receipts (ADRs), subject to the following conditions:

(i) The company has approval from the Ministry of Finance to issue such ADRs and/or GDRs or is eligible to issue ADRs/GDRs in terms of the relevant scheme in force or notification issued by the Ministry of Finance;

(ii) The company is not otherwise ineligible to issue shares to persons resident outside India; and

(iii) The ADRs/GDRs are issued in accordance with the Scheme for Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the central government.

The Indian company must furnish the RBI with full details of such an issue, in the form specified (see the Worksheets), within 30 days from the date of closing of the issue. The Indian company must also furnish to the RBI a quarterly return, in the form specified (see the Worksheets), within 15 days of the close of the calendar quarter. The quarterly return must be submitted until the entire amount raised through GDRs/ADRs is either repatriated to India or utilized abroad as per the RBI guidelines.

GDRs/ADRs are issued based on the ratio worked out by the Indian company in consultation with the Lead Manager for the issue. The proceeds must be retained abroad until actually required in India. Pending the repatriation or utilization of foreign exchange resources, the Indian company may invest the foreign currency funds in:

(i) Deposits or Certificates of Deposit or other instruments offered by banks rated by Standard and Poor, Fitch, IBCA or Moody's, etc., no lower than the rating stipulated by the RBI for the purpose;

(ii) Deposits with a branch outside India of an authorized dealer in India; and

(iii) Treasury bills and other monetary instruments with a maturity or unexpired maturity of one year or less.

A registered broker in India may purchase shares of an Indian company on behalf of a person resident outside India for purposes of converting the shares into ADRs/GDRs, subject to the following conditions:

(i) The shares are purchased on a recognized stock exchange;

(ii) The Indian company has issued ADRs/GDRs;

(iii) The shares are purchased with the permission of the Custodian of the ADRs/GDRs of the Indian company concerned and are deposited with the Custodian;

(iv) The number of shares so purchased does not exceed ADRs/GDRs converted into underlying shares and is subject to sectoral caps as applicable; and

(v) The nonresident investor, broker, Custodian and overseas depository comply with the provisions of the Scheme for Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt

Mechanism) Scheme, 1993 and guidelines issued thereunder by the central government.

An Indian company may sponsor an issue of ADRs/GDRs with an overseas depository against shares held by its shareholders at a price to be determined under the provisions of the Scheme for Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued thereunder by the central government and the reporting requirements as directed by the RBI.

A company may issue GDRs/ADRs if it is eligible to issue shares to a person outside India under the FDI policy. However, an Indian listed company that is not eligible to raise funds from the Indian capital market, including a company that has been restrained from accessing the securities market by the SEBI, will not be eligible to issue GDRs/ADRs. Unlisted companies that have not accessed the ADR/GDR route for raising capital in the international market would require prior or simultaneous listing in the domestic market, while seeking to issue such overseas instruments. Unlisted companies that have already issued ADRs/GDRs in the international market are required to list in the domestic market on making a profit or within three years of such issue, whichever is earlier.

There are no end use restrictions on capital raised through the ADR/GDR route, except for a ban on deployment/investment of such funds in real estate or the stock exchange. The proceeds from the issue may be utilized for the first stage acquisition of shares in the disinvestment of public sector undertakings or enterprises (PSUs or PSEs) and also the mandatory second stage offer to the public. There is no monetary limit on how much an Indian company may raise through ADRs/GDRs.

The voting rights of shares issued in terms of the scheme stated above are as per the provisions of the Companies Act, 1956.

A limited two-way fungibility scheme has been put into place by the central government for ADRs/GDRs, under which a stock broker in India that is registered with the SEBI may purchase shares of an Indian company from the market for conversion into ADRs/GDRs based on instructions from an overseas investor. The reissuance of ADRs/GDRs is permitted to the extent of ADRs/GDRs that have been redeemed into underlying shares and sold in the market.

An Indian company may also sponsor an issue of ADRs/GDRs. Under this mechanism, the company offers its resident shareholders the option of submitting their shares back to the company so that, based such shares, ADRs/GDRs may be issued abroad. The proceeds of the ADR/GDR issue are remitted back to India and distributed among the resident investors who offered their rupee denominated shares for conversion. These proceeds may be kept in Resident Foreign Currency (Domestic) accounts in India by the resident shareholders who tendered such shares for conversion into ADRs/GDRs.

(2) Investment via Rights Issues

An Indian company may offer a person resident outside India, equity or preference shares or convertible debentures on a rights basis, subject to the following conditions:

(i) The offer on a rights basis does not result in an increase in the percentage of foreign equity already approved, or permissible under the existing FDI Scheme;

(ii) The existing nonresident shareholders may apply for the issue of additional shares, and the investee company may allot the same, subject to the condition that the overall issue of shares to nonresidents in the total paid-up capital does not exceed the sectoral cap;

(iii) The existing shares or debentures against which shares or debentures are issued by the company on a rights basis were acquired and are held by the persons resident outside India in accordance with the existing regulations; and

(iv) The offer on a rights basis to persons resident outside India is at a price no lower than that at which the offer is made to resident shareholders.

The rights shares or debentures purchased by the person resident outside India are subject to the same conditions, including restrictions regarding the ability to repatriate, as are applicable to the original shares against which the rights shares or debentures are issued when:

(i) The amount of consideration for the purchase of rights shares or debentures is paid by way of inward remittance in foreign exchange through normal banking channels or by debit to an Non-resident External (NRE) or Foreign Currency Non-resident (FCNR) account, when the shares or debentures are issued on a repatriation basis; and

(ii) With respect to the shares or debentures issued on a nonrepatriation basis, the amount of consideration may also be paid by debit to an Non-resident Ordinary (NRO), Non-resident Special Rupee (NRSR) or Non-resident Non-repatriable (NRNR) account.

(3) Acquisition of Bonus Shares

An Indian company may issue bonus shares to its nonresident shareholders, subject to the following conditions:

(i) The shares against which the bonus shares are issued by the company (hereinafter referred to as "the original shares") were acquired or held by the nonresident shareholder in accordance with the rules and regulations applicable to such an acquisition; and

(ii) The bonus shares acquired by the nonresident shareholder are subject to the same conditions, including restrictions with regard to the ability to repatriate, as are applicable to the original shares.

(4) Issue and Acquisition of Shares After Merger, Demerger or Amalgamation of Indian Companies

Where a scheme of merger or amalgamation of two or more Indian companies or a reconstruction by way of demerger or otherwise of an Indian company has been approved by a Court in India, the transferee company or the new company may issue shares to the shareholders of a transferor company resident outside India, subject to the following conditions:

(i) The percentage shareholding of persons resident outside India in the transferee or new company does not exceed the percentage specified in the approval granted by the central government or the RBI, or the sectoral cap (see the Sector Specific Guidelines for Foreign Direct Investment in the Worksheets)). However, where the percentage is likely to exceed the percentage specified in the approval or the regulations, the transferor company or the transferee or new company may, after obtaining approval from the central government, apply to the RBI for its approval under the regulations;

(ii) The transferor company or the transferee or new company does not engage in any prohibited activity (see the List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or Items for which FDI is Prohibited in the Worksheets)); and

(iii) The transferee or the new company files a report within 30 days with the RBI giving full details of the shares held by persons resident outside India in the transferor and the transferee or the new company before and after the merger, amalgamation or reconstruction, and also furnishes a confirmation that all the terms and conditions stipulated in the scheme approved by the Court have been complied with (see (6), below).

(5) Issue of Shares Under Employees Stock Options Scheme to Persons Resident Outside India

An Indian company may issue shares under an Employees' Stock Options Scheme, by whatever name called, to its employees or employees of its joint venture or wholly-owned subsidiary abroad who are resident outside India, directly or through a trust, subject to the following conditions:

(i) The scheme has been drawn up in terms of the regulations issued under the Securities and Exchange Board of India Act, 1992; and

(ii) The face value of the shares to be allotted under the scheme to the nonresident employees does not exceed 5% of the paid-up capital of the issuing company.

The trust and the issuing company must ensure that the value of shares held by persons resident outside India under the scheme does not exceed the limit specified above.

Unlisted companies may issue shares under an Employee Stock Ownership Plan (ESOP) scheme to employees, as referred to above, after complying with the provisions of the Companies Act, 1956.

ESOPs may not be issued to citizens of Pakistan. ESOPs may be issued to citizens of Bangladesh, with the prior approval of the FIPB.

The issuing company must furnish the RBI, within 30 days from the date of issue of shares under the scheme, a report containing the following particulars and documents:

(i) The names of persons to whom shares are issued under the scheme and the number of shares issued to each of them; and

(ii) A certificate from the company secretary of the issuing company to the effect that the value of the shares issued under the scheme does not exceed 5% of the paid-up capital of the issuing company and that the shares are issued in compliance with the regulations issued by the SEBI in this respect.

(6) Reporting and Issue of Shares

Indian companies are required to report, in advance reporting form, details of the receipt of consideration for the issue of shares or convertible debentures through an authorized dealer, along with the required documents not later than 30 days from the date of receipt.

Equity instruments should be issued within 180 days from the date of receipt of the inward remittance. If equity instruments are not issued within 180 days, the amount of consideration so received should be refunded immediately to the nonresident investor by outward remittance through normal banking channels. Noncompliance with the above provision would be a violation of FEMA and could attract penal provisions. In exceptional cases, a refund of the amount of consideration outstanding after a period of 180 days from the date of receipt may be considered by the RBI on the merits of the case.

After the issue of shares or debentures (including bonus and right shares) and shares under ESOP, the Indian company must file Form FC-GPR (see the Worksheets) not later than 30 days from the date of issue. The following documents must be attached to the Form:

(i) A certificate from the company secretary of the company certifying that:

- **All requirements of the Companies Act have been complied with;**
- **The terms and conditions of the Government approval, if any, have been complied with;**
- **The company is eligible to issue shares under the relevant regulations; and**
- **The company has all the original certificates issued by the authorized dealers in India evidencing receipt of the consideration amount.**

(ii) A certificate from the statutory auditors or a chartered accountant indicating the manner of arriving at the price of the shares issued.

The issue of bonus or rights shares or stock options to persons resident outside India directly or on amalgamation or merger with an existing Indian company, as well as the issue of shares on the conversion of ECBs, royalties, lump sum technical know-how fees or the import of capital goods by units in SEZs must be reported on form FC-GPR.

(7) Pricing

The price of shares issued to a person resident outside India under the FDI Scheme must be determined based on the SEBI guidelines in the case of listed companies. In the case of unlisted companies, shares are to be valued as per the RBI guidelines issued from time to time.

The pricing of ADRs/GDRs (including sponsored ADRs/GDRs) must be determined under the provisions of the Scheme for Issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued by the government of India and the reporting requirements of the RBI.

c. Investments by Nonresident Indians

Investment by nonresident Indians (NRIs) is treated as FDI and considered to be essentially on a par with investment by other nonresidents.

Some of the important schemes for investment by NRIs are described in (1) and (2), below.

(1) Purchase/Sale of Shares and/or Convertible Debentures by a Nonresident Indian on a Stock Exchange in India on a Repatriation and/or Non-Repatriation Basis Under the Portfolio Investment Scheme

An NRI may purchase or sell shares and/or convertible debentures of a listed Indian company, through a registered broker on a recognized stock exchange, subject to the following conditions:

(i) An NRI may purchase and sell shares or convertible debentures under the Portfolio Investment Scheme through a branch designated by an authorized dealer for the purpose and duly approved by the RBI;

(ii) The paid-up value of shares of the Indian company purchased by each NRI, both on a repatriation and on a nonrepatriation basis, may not exceed 5% of the paid-up value of the shares issued by the company concerned;

(iii) The paid-up value of each series of convertible debentures purchased by each NRI, both on a repatriation and on a nonrepatriation basis, may not exceed 5% of the paid-up value of each series of convertible debentures issued by the company concerned;

(iv) The aggregate paid-up value of the shares of any company purchased by all NRIs may not exceed 10% of the paid-up capital of the company and, in the case of the purchase of convertible debentures, the aggregate paid-up value of each series of debentures purchased by all NRIs may not exceed 10% of the paid-up value of each series of convertible debentures. However, the aggregate ceiling of 10% referred to in this clause may be raised to 24% if a special resolution to that effect is passed by the general body of the Indian company concerned;

(v) The NRI investor must take delivery of the shares purchased and make delivery of the shares sold, i.e.

short selling is not permitted; and

(vi) Payment for the purchase of shares and/or debentures must be made by inward remittance in foreign exchange through normal banking channels or out of funds held in an NRE or FCNR account maintained in India if the shares are purchased on a repatriation basis and by inward remittance or out of funds held in an NRE, FCNR, NRO, NRNR or NRSR account of the NRI concerned maintained in India where the shares or debentures are purchased on a nonrepatriation basis.

Shares purchased by NRIs on the stock exchange under the Portfolio Investment Scheme may not be transferred by way of sale under private arrangement or by way of gift (except by NRIs to their relatives as defined in Section 6 of Companies Act, 1956 or to a charitable trust duly registered under the laws in India) to a person resident in India or outside India without the prior approval of the RBI.

NRIs are allowed to invest in Exchange Traded Derivative Contracts approved by the SEBI out of rupee funds held in India on a nonrepatriation basis, subject to the limits prescribed by the SEBI.

(a) Report to the Reserve Bank of India

The link office of the designated branch of an authorized dealer referred to above must furnish the Chief General Manager, RBI, Exchange Control Department, Central Office, Mumbai, a report on a daily basis on Portfolio Investment Scheme transactions undertaken by it. The report must be furnished on line, on floppy disk or in hard copy in a format supplied by the RBI.

(b) Remittance/Credit of Sale/Maturity Proceeds of Shares and/or Debentures

The net sale or maturity proceeds (after payment of taxes) of shares and/or debentures of an Indian company purchased by an NRI under this scheme may be allowed by the designated branch of an authorized dealer referred to above:

(i) To be credited to the NRO account of the NRI investor where the payment for the purchase of shares and/or debentures sold was made out of funds held in an NRO account or where the shares and/or debentures were purchased on a nonrepatriation basis; or

(ii) At the NRI investor's option, to be remitted abroad or credited to the NRE, FCNR or NRO account of the NRI, where the shares and/or debentures were purchased on a repatriation basis.

(2) Purchase and Sale of Shares/Convertible Debentures by a Nonresident Indian, on a Non-Repatriation Basis

Investment in the shares or convertible debentures of an Indian company may not be made under this scheme if the company concerned is:

(i) A chit fund; [2]

(ii) A *nidhi* company; [3] or

(iii) Engaged in agricultural or plantation activities or real estate business or the construction of farm houses, or dealing in Transferable Development Rights (TDRs).

---

[2] "Chit fund company" means a company managing, conducting or supervising, as foreman, agent or in any other capacity, chits. "Chit" as per the Chit Funds Act, 1982 means a transaction by or under which a person enters into an agreement with a specified number of persons that every one of them shall subscribe a certain sum of money (or a certain quantity of grain instead) by way of periodic installments over a definite period and that each such subscriber shall, in his turn, as determined by lot or by auction or by tender or in such other manner as may be specified in the chit agreement, be entitled to the prize amount.

[3] "Nidhi company" means a mutual benefit society, formed for the benefit of its members.

Note: **For this purpose, real estate business does not include the development of townships, or the construction of residential or commercial premises, roads, bridges, etc.**

Subject to the restrictions set out above, an NRI may without any limit, purchase on a nonrepatriation basis, shares or convertible debentures of an Indian company issued by public issue, private placement or a rights issue, subject to the condition that the person to whom the shares are being transferred has obtained prior permission from the central government to acquire the shares if he has a previous venture or tie-up in India through investment in shares or debentures, a technical collaboration, a trade mark agreement or investment, by whatever name called, in the same field as, or an allied field to, that in which the Indian company whose shares are being transferred is engaged, subject to exceptions.

The amount of the consideration for the purchase of shares or convertible debentures of an Indian company on a

nonrepatriation basis must be paid by way of inward remittance through the normal banking channels from abroad or out of funds held in an NRE, FCNR, NRO, NRSR or NRNR account maintained with an authorized dealer or, as the case may be, with an authorized bank in India. However, in the case of an NRI resident in Nepal or Bhutan, the amount of consideration for the purchase of shares or convertible debentures of an Indian company on a nonrepatriation basis must be paid only by way of inward remittance in foreign exchange through normal banking channels.

The sale or maturity proceeds (net of applicable taxes) of shares or convertible debentures purchased under this scheme will be credited only to the NRSR account where the purchase consideration was paid out of funds held in the NRSR account and to the NRO or NRSR account, at the option of the seller, where the purchase consideration was paid out of inward remittance or funds held in an NRE, FCNR, NRO or NRNR account.

Neither the amount invested in shares or convertible debentures under this scheme nor the capital appreciation thereon may be repatriated abroad.

d. Investment by Foreign Institutional Investors

An FII registered with the SEBI may purchase shares and convertible debentures of an Indian company under the Portfolio Investment Scheme.

Such a purchase of shares or convertible debentures must be made through a registered broker on a recognized stock exchange in India.

The consideration for the purchase of the shares or debentures must be paid out of inward remittance from abroad through normal banking channels or out of funds held in an account maintained with the designated branch of an authorized dealer in India, in accordance with the Regulations.

The total holding of each FII or SEBI-approved sub-account of an FII may not exceed 10% of the total paid-up equity capital or 10% of the paid-up value of each series of convertible debentures issued by an Indian company and the total holdings of all FIIs or sub-accounts of FIIs, in aggregate, may not exceed 24% of paid-up equity capital or the paid-up value of each series of convertible debentures. However, the 24% limit may be increased up to the sectoral cap or statutory ceiling, as applicable, by the Indian company concerned by the passing of a resolution by its board of directors followed by the passing of a special resolution to that effect by its general body.

Note: **In arriving at the ceiling on holdings of FIIs, shares or convertible debentures acquired through both the primary and the secondary market will be included. However, the ceiling will not include investment made by FIIs through offshore funds, GDRs and Euro-convertible bonds.**

A registered FII is permitted to purchase shares or convertible debentures of an Indian company through offer or private placement, subject to the ceilings specified above and the Indian company is permitted to issue such shares, subject to the following:

(i) In the case of a public offer, the price of the shares to be issued is not less than the price at which the shares are issued to residents; and

(ii) In the case of issue by private placement, the price is not less than the price arrived at in terms of the SEBI guidelines or guidelines issued by the erstwhile Controller of Capital Issues, as applicable. Purchases may also be made of compulsorily and mandatorily convertible debentures, rights renunciations or units of domestic mutual fund schemes.

FIIs are not permitted to invest in the equity issued by ARCs. Nor are FIIs allowed to invest in a company that is engaged, or proposes to engage, in any of the following activities:

(i) The business of a chit fund;

(ii) A *nidhi* company;

(iii) Agricultural or plantation activities;

(iv) Real estate business or the construction of farm houses; or

(v) Trading in TDRs.

Note: **"Real estate business," as referred to above, does not include the construction of housing or commercial premises, educational institutions, recreational facilities, city and regional level infrastructure, and townships.**

FIIs are allowed to trade in all exchange traded derivatives contracts on recognized stock exchanges in India, subject to position limits prescribed by the SEBI. FIIs are allowed to offer cash and foreign securities with AAA rating as collateral to recognized stock exchanges in India for their transactions in the derivatives segment. In the case of the cash segment, FIIs are allowed to offer Government Securities (subject to overall limits specified from time to time by the SEBI), along with cash and foreign sovereign securities with an AAA rating, as collateral to recognized stock exchanges in India. However, the cross-margining of Government Securities, which are placed as margins by the FIIs for their transactions in the cash segment of the market, are not allowed between the cash and the derivative

segments of the market. Authorized dealers may also offer forward cover to an FII with the Indian rupee as one of the currencies and hedge the market value of their entire investment in India as of a particular date. Rebooking of cancelled forward contracts is permitted, up to a limit of 2% of the market value of the entire investment of the FII in India.

An FII may open a Foreign Currency Account and/or a Special Nonresident Rupee Account with a designated branch of an authorized dealer for routing the receipt of and payment for a transaction relating to the purchase and sale of shares or convertible debentures under this scheme, subject to the following conditions:

(i) The account must be funded by inward remittance through normal banking channels or by the credit of the sale proceeds (net of taxes) of the shares or convertible debentures sold on the stock exchange.

(ii) The funds in the account must be utilized for the purchase of shares or convertible debentures in accordance with the provisions of the scheme or for remittance outside India.

(iii) Funds from a Foreign Currency Account of a registered FII may be transferred to a special nonresident rupee account of the same FII and vice versa.

Registered FIIs and sub-accounts of FIIs are permitted to short sell, lend and borrow equity shares of Indian companies subject to any conditions laid down in that behalf by the RBI, the SEBI and other regulatory agencies, and in particular the following:

(i) The FII participation in the short selling as well as borrowing or lending of equity shares is subject to the current FDI policy, and short selling will not be permitted with respect to equity shares that are on the ban or caution list of the RBI;

(ii) The borrowing of equity shares is only for purposes of delivery into short sale; and

(iii) The margin or collateral must be maintained by the FII in cash. No interest must be paid on such collateral.

The designated branch of an authorized dealer may allow the remittance of net sale proceeds (after payment of taxes) or credit the net amount of the sale proceeds of shares or convertible debentures to the Foreign Currency Account or a Nonresident Rupee Account of the FII concerned.

An FII may invest in a particular share issue of an Indian company either under the FDI Scheme or the Portfolio Investment Scheme. Authorized dealers have to ensure that the FIIs that purchase the shares by debit to the special rupee accounts report these details separately in the specified form.

An Indian company that has issued shares to FIIs under the FDI Scheme (for which payment has been received directly into the Indian company's account) and the Portfolio Investment Scheme (for which payment has been received from the FIIs' account maintained with an authorized dealer in India) should report these figures separately.

A daily statement with respect to all transactions (except derivative trades) must be submitted by the custodian bank in floppy or soft copy directly to the RBI to monitor the overall ceiling, sectoral cap or statutory ceiling.

e. Investment by Asset Management Companies/ Portfolio Managers

A domestic asset management company or portfolio manager registered with the SEBI as an FII for managing the fund of a sub-account may make an investment under the scheme on behalf of the following:

(i) A person resident outside India who is a citizen of a foreign state; or

(ii) A body corporate registered outside India, subject to the condition that the investment is made out of funds raised or collected or brought from outside through normal banking channels.

Investments may not exceed 5% of the total paid-up equity capital or 5% of the paid-up value of each series of convertible debentures issued by an Indian company, and may also not exceed the overall ceiling specified above in the case of investments by FIIs.

f. Purchase and Sale of Securities Other Than Shares or Convertible Debentures of an Indian Company by a Person Resident Outside India

(1) Permission for a Foreign Institutional Investor

A registered FII may purchase, on a repatriation basis, dated Government securities or treasury bills, listed nonconvertible debentures or bonds, commercial paper issued by an Indian company, units of domestic mutual funds and security receipts issued by an ARC, either directly from the issuer of such securities or through a registered stock broker on a recognized stock exchange in India, subject to the following condition: The total holding by a single FII in each tranche of the scheme of security receipts issued by an ARC may not exceed 10% of the issue and the total

holdings of all FIIs, in aggregate, may not exceed 49% of the paid-up value of each tranche of the scheme of security receipts issued by ARCs.

(2) Permission for a Nonresident Indian

An NRI may, without limit, purchase on a repatriation basis:

(i) Government dated securities (other than bearer securities) or treasury bills or units of domestic mutual funds;

(ii) Bonds issued by a PSU in India; and

(iii) Shares in public sector enterprises being disinvested by the Government of India, provided the purchase is in accordance with the terms and conditions stipulated in the notice inviting bids.

An NRI may, without limit, purchase the following on a nonrepatriation basis:

(i) Dated Government securities (other than bearer securities), or treasury bills; and

(ii) Units of domestic mutual funds, units of money market mutual funds in India or National Plans or Savings Certificates.

(3) Permission for a Multilateral Development Bank

A multilateral development bank specifically permitted by the Government of India to float rupee bonds in India may purchase Government dated securities.

(4) Permission for a Foreign Central Bank to Purchase Government Securities

A foreign central bank may purchase and sell dated government securities or treasury bills in the secondary market subject to the conditions set by the RBI.

A person resident outside India, being the central bank of any country under the law in force in that country, may purchase and sell dated Government securities or treasury bills subject to conditions stipulated by the RBI.

(5) Foreign Investment in Instruments Issued by Banks

FIIs are permitted to invest in the following securities issued by banks in India:

(i) Up to 49% in each issue of perpetual debt instruments, with the limit for an individual FII being 10% of the issue;

(ii) Debt capital instruments within the limits specified by the SEBI for investment in corporate debt. FII investments in such instruments raised in Indian rupees will be outside the limit prescribed by the SEBI for investment in corporate debt instruments. However, investment by FIIs in these instruments will be subject to a limit of US$ 500 million.

Note: **FIIs may offer the above securities as permitted by the RBI, as collateral, to a recognized stock exchange for transactions in exchange traded derivative contracts.**

NRIs are permitted to invest in the following securities issued by banks in India:

(i) Up to 24% in each issue of perpetual debt instruments, with the limit for an investment by a single NRI being 5% of the issue; and

(ii) Debt capital instruments, in terms of the policy for investments by NRIs in other debt instruments.

(6) Method of Payment of Purchase Consideration

An FII that purchases securities as outlined above must make the payment for the purchase of the securities either by inward remittance through normal banking channels or out of funds held in a foreign currency account or nonresident rupee account maintained by the FII with a designated branch of an authorized dealer with the approval of the RBI.

An NRI who purchases securities as outlined above on a repatriation basis must make payment either by inward remittance through normal banking channels or out of funds held in his NRE or FCNR account.

An NRI who purchases securities as outlined above on a nonrepatriation basis must make payment either by inward remittance through normal banking channels or out of funds held in his NRE, FCNR, NRO, NRSR or NRNR account.

A multilateral development bank that purchases government dated securities as outlined above must make payment either by inward remittance through normal banking channels or out of funds held in the account opened with the specific approval of the RBI.

(7) Permission for Sale of Securities

A person resident outside India who has purchased securities as described above may:

(i) Sell such securities through a registered stock broker on a recognized stock exchange;

(ii) Tender units of mutual funds to the issuer for repurchase or for the payment of maturity proceeds; or

(iii) Tender government securities or treasury bills to the RBI for the payment of maturity proceeds.

(8) Remittance/Credit of Sale/Maturity Proceeds

(i) In the case of a registered FII that has sold securities in the manner outlined above, the designated branch of the authorized dealer may allow the remittance of net sale or maturity proceeds (after payment of taxes) or credit the net amount of sale or maturity proceeds of such securities to the foreign currency account or nonresident rupee account of the FII investor, maintained as described above.

(ii) In the case of an NRI who has sold securities, the net sale or maturity proceeds (after payment of taxes) of such securities, may be:

- **Credited only to an NRSR account of the NRI investor where the payment for the purchase of the securities sold was made out of funds held in the NRSR account;**
- **Credited, at the NRI investor's option, to his NRO or NRSR account, where the payment for the purchase of the securities sold was made out of funds held in the NRO account; or**
- **Remitted abroad or, at the NRI investor's option, credited to his NRE, FCNR, NRO, NRSR or NRNR account, where the securities were purchased on a repatriation basis as outlined above and the payment for the purchase of the securities sold was made by inward remittance through normal banking channels or out of funds held in an NRE or FCNR account.**

(iii) In the case of the sale of government dated securities by a multilateral development bank, the net maturity proceeds (after payment of taxes) may be remitted abroad or credited to a fund account opened with the prior permission of the RBI.

g. Investment in Indian Venture Capital Undertakings by Registered Foreign Venture Capital Investors

A registered foreign venture capital investor (FVCI) may, through the SEBI, apply to the RBI for permission to invest in an Indian venture capital undertaking (IVCU) or in an Indian venture capital fund (IVCF) registered with the SEBI, or in a scheme floated by such IVCFs. Permission may be granted by the RBI, subject to such terms and conditions as may be considered necessary.

An FVCI may purchase equity, equity-linked instruments, debt, debt instruments or debentures of an IVCU or IVCF through an initial public offer or private placement, or in units of schemes or funds set up by an IVCF.

The amount of consideration for investment in IVCFs/IVCUs must be paid out of inward remittance from abroad through normal banking channels or out of funds held in an account maintained with the designated branch of an authorized dealer in India.

The purchase or sale of shares, debentures and units may be effected at a price that is mutually acceptable to the buyer and the seller.

Note: **An IVCU is defined as a company incorporated in India whose shares are not listed on a recognized stock exchange in India and that is not engaged in an activity specified in the negative list issued by the SEBI. An IVCF is defined as a fund established in the form of a trust or a company, including a body corporate, and registered under the Securities and Exchange Board of India (Venture Capital Fund) Regulations, 1996 that has a dedicated pool of capital raised in a manner specified under the Regulations and that invests in IVCUs in accordance with the Regulations.**

(1) Maintenance of Account by a Registered Foreign Venture Capital Investor for Investment in Indian Venture Capital Undertakings/Venture Capital Funds or Schemes/Funds Set Up by Indian Venture Capital Funds

The RBI may, on application, permit an FVCI that has obtained "in principle" registration from the SEBI to open a foreign currency account and/or a rupee account with a designated branch of an authorized dealer for the following permissible transactions:

(i) Crediting inward remittance received through normal banking channels or the sale proceeds (net of taxes) of investments.

(ii) Making investments in accordance with the provisions of (i).

(iii) Transferring funds from the foreign currency account of the FVCI to its own rupee account.

(iv) Remitting funds from the foreign currency or rupee account, subject to the payment of applicable taxes.

(v) Meeting the local expenses of the FVCI.

(2) Forward Cover

An authorized dealer may offer forward cover to an FVCI to the extent of total inward remittance. If the FVCI has made any remittance by liquidating some investments, the original cost of the investments will be deducted from the eligible cover.

(3) Valuation of Investments

An FVCI may acquire, by purchase or otherwise, or sell shares or convertible debentures, units or any other investment held by it in IVCUs or IVCFs or schemes or funds set up by IVCFs at a price that is mutually acceptable to the buyer and the seller/issuer. An FVCI may also receive the proceeds arising on the liquidation of IVCFs or schemes or funds set up by IVCFs.

(4) Adherence to Securities Exchange Board of India Guidelines

FVCIs must abide by the relevant regulations and guidelines issued by the SEBI.

h. Investment in Partnership Firm/Proprietary Concern

(1) Investment in a Firm or Proprietary Concern in India by a Person Resident Outside India

An NRI or a person of Indian origin (PIO) resident outside India may invest by way of contribution to the capital of a firm or proprietary concern in India on a nonrepatriation basis, subject to the following conditions:

(i) The amount is invested by inward remittance or out of an NRE, FCNR or NRO account maintained with an authorized dealer;

(ii) The firm or proprietary concern is not engaged in any agricultural or plantation or real estate business (i.e., dealing in land and real property with a view to earning profit or income) or the print media sector; and

(iii) The amount invested is not eligible for repatriation outside India.

(2) Investment in Sole Proprietorship Concern/ Partnership Firm with Repatriation Benefits

An NRI or a PIO may seek prior permission of the RBI for investment in sole proprietorship concerns or partnership firms with repatriation benefits.

(3) Investment by a Nonresident Other Than a Nonresident Indian/Person of Indian Origin

A person resident outside India other than an NRI or a PIO may apply for prior approval from the RBI for making an investment by way of contribution to the capital of a firm or proprietorship concern or any association of persons in India.

(4) Restrictions

An NRI or a PIO is not allowed to invest in a firm or proprietorship concern engaged in any agricultural or plantation activity or real estate business (i.e., dealing in land and real property with a view to earning profit or income) or engaged in the print media.

i. Prior Permission of Reserve Bank in Certain Cases for Transfer of Security

(1) Transfer by Way of Gift or Sale by a Person Resident in India

A person resident in India who proposes to transfer any security by way of gift to a person resident outside India, not being an erstwhile OCB, must make an application to the RBI for its approval.

The RBI may grant its approval on being satisfied that the following conditions are fulfilled:

(i) The donee is eligible to hold the security under the existing regulations;

(ii) The gift does not exceed 5% of the paid-up capital of the Indian company, each series of debentures or each mutual fund scheme;

(iii) The applicable sectoral cap or FDI limit in the Indian company is not breached;

(iv) The donor and the donee are relatives, as defined in Section 6 of the Companies Act, 1956;

(v) The value of the security to be transferred by the donor together with any security transferred to any person residing outside India as a gift in the calendar year does not exceed the rupee equivalent of US$ 25,000; and

(vi) Such other conditions as are considered necessary in the public interest by the RBI.

The application for approval in this context must contain the following information and documents:

(i) The name and address of the donor and the donee;

(ii) The relationship between the donor and the donee;

(iii) The reasons for the making of the gift;

(iv) In the case of government dated securities and treasury bills and bonds, a certificate issued by a chartered accountant with respect to the market value of the securities;

(v) In the case of units of domestic mutual funds and units of money market mutual funds, a certificate from the issuer with respect to the net asset value of the securities;

(vi) In the case of shares and debentures, a certificate from a chartered accountant with respect to the value of the securities according to the guidelines issued by the SEBI or the erstwhile Controller of Capital Issues with regard to listed companies and unlisted companies, respectively; and

(vii) A certificate from the Indian company concerned certifying that the proposed transfer of shares or convertible debentures, by way of gift, from the resident to the nonresident will not breach the applicable sectoral cap or FDI limit in the company and that the proposed number of shares or convertible debentures to be held by the nonresident transferee will not exceed 5% of the paid-up capital of the company.

A person resident in India who proposes to transfer to a person resident outside India, not being an erstwhile OCB, any shares or convertible debentures of an Indian company whose activities fall within the categories set out in the Sector Specific Guidelines for Foreign Direct Investment, other than items Nos. 1, 2 and 3 (see the Worksheets), and subject to the sectoral limits specified therein, may transfer such shares or debentures without the prior approval of the government and the RBI if the transfer is by way of sale, subject to the following:

(i) The Indian company whose shares or convertible debentures are proposed to be transferred is not engaged in rendering any financial service;

(ii) The transfer does not fall within the purview of the provisions of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997; and

(iii) The parties concerned adhere to such pricing guidelines, documentation and reporting requirements for such transfers as may be specified by the RBI.

A person resident in India who proposes to transfer any security by way of sale must make an application to the RBI for approval in the following instances:

(i) The activity of the Indian company whose securities are being transferred falls outside the Automatic Route and the approval of the FIPB has been obtained for the transfer;

(ii) The activity of the Indian company whose securities are being transferred falls within the financial services sector;

(iii) The transfer falls within the purview of the provisions of the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997; or

(iv) The transfer is to take place at a price that falls outside the pricing guidelines specified by Reserve Bank.

Note: **For purposes of these regulations, "financial services" means services rendered by a banking or nonbanking company regulated by the RBI, an insurance company regulated by the Insurance Regulatory and Development Authority (IRDA) and any other company regulated by any other financial regulator.**

(2) Transfer by Way of Sale Not Covered by the Regulations by a Person Resident Outside India

A person resident outside India may transfer shares or convertible debentures of an Indian company, without the

prior permission of the RBI, by way of sale to a person resident in India, subject to adherence to such pricing guidelines, documentation and reporting requirements for such transfers as may be specified by the RBI.

(3) Remittance of Sale Proceeds

An authorized dealer may allow the remittance of sale proceeds of a security (net of applicable taxes) to the seller resident outside India, subject to the following conditions:

(i) The security was held by the seller on a repatriation basis;

(ii) Either the security has been sold on a recognized stock exchange in India through a stock broker at the ruling market price as determined on the floor of the exchange, or the RBI's approval has been obtained in other cases for the sale of the security and remittance of the sale proceeds thereof; and

(iii) A no objection or tax clearance certificate from the income tax authority has been produced.

j. Foreign Technology Agreements

The acquisition of foreign technology is encouraged through foreign technology collaboration agreements in order to promote the technological capacity and competitiveness of Indian industry. The induction of know-how through such collaboration is permitted via the Automatic route. The terms of payment under foreign technology collaboration include technical know-how fees, payments for design and drawing, payments for engineering services and royalties. The payment of royalties includes payment for the use of a trademark and the brand name of the foreign collaborator. Payments for hiring foreign technicians, the deputation of Indian technicians abroad and the testing of indigenous raw material, products and technology in foreign countries, are governed by separate procedures and rules of the RBI relating to current account transactions.

2. Exchange Control

a. Foreign Exchange Management Act, 1999

The FEMA was enacted with the objective of facilitating external trade and payments, and promoting the orderly development and maintenance of foreign exchange markets in India. It extends to the whole of India, and also applies to all branches, offices and agencies located outside India that are owned or controlled by a person resident in India. The RBI supervises compliance with the FEMA by specifying regulations and issuing directions. The central government is empowered to make rules under Section 46 of the FEMA.

b. Residential Status

The FEMA regulates transactions between residents and nonresidents. Determining the residential status of a person under the FEMA is of the utmost importance because the applicability or otherwise of the provisions of the FEMA depends on a person's residential status.

The term "resident of India" refers to a "person." A "person" includes:

(i) An individual;

(ii) A Hindu Undivided Family (HUF);

(iii) A company;

(iv) A firm;

(v) An association of persons (AOP) or a body of individuals (BOI), whether incorporated or not;

(vi) Any artificial juridical person not falling within any of subparagraphs (i) to (v); and

(vii) Any agency, office or branch owned or controlled by such person. [4]

[4] Foreign Exchange Management Act, 1999 (FEMA), Sec. 2(u).

"A person resident in India" means:

(i) A person residing in India for more than 182 days during the course of the preceding financial year but not including:

(a) A person who has gone out of India or who stays outside India, in either case:

- For purposes of, or on taking up, employment outside India;
- For purposes of carrying on a business or vocation outside India; or

• For any other purpose, in such circumstances as would indicate an intention to stay outside India for an indefinite period; or

(b) A person that has come to or stays in India, in either case, otherwise than:

• For purposes of, or on taking up, employment in India;

• For purposes of carrying on a business or vocation in India; or

• For any other purpose, in such circumstances as would indicate an intention to stay in India for an indefinite period.

(ii) Any person or body corporate registered or incorporated in India.

(iii) An office, branch or agency in India owned or controlled by a person resident outside India.

(iv) An office, branch or agency outside India owned or controlled by a person resident in India. [5]

---

[5] FEMA, Sec. 2(v).

A person resident outside India is defined as a person that is not resident in India. [6]

---

[6] FEMA, Sec. 2(w).

---

c. Capital Account Transactions

"Capital account transaction" means a transaction that alters the assets and liabilities, including contingent liabilities outside India of persons resident in India or assets or liabilities in India of persons resident outside India, and includes transactions specifically referred to in the FEMA. [7]

---

[7] FEMA, Secs. 2(e) and 6(3).

The RBI may, in consultation with the central government, specify:

(i) Any class or classes of capital account transactions that are permissible; and

(ii) The limit up to which foreign exchange will be admissible in the case of such transactions.

However, the RBI is not permitted to impose any restriction on the drawing of foreign exchange for payments due on account of the amortization of loans or for the depreciation of direct investments in the ordinary course of business. [8]

---

[8] FEMA, Sec. 6(2).

The RBI may, by regulations, prohibit, restrict or regulate the following: [9]

---

[9] FEMA, Sec. 6(3).

(i) The transfer or issue of any foreign security by a person resident in India;

(ii) The transfer or issue of any security by a person resident outside India;

(iii) The transfer or issue of any security or foreign security by any branch, office or agency in India of a person resident outside India;

(iv) Any borrowing or lending in foreign exchange in whatever form or by whatever name called;

(v) Any borrowing or lending in rupees in whatever form or by whatever name called between a person resident in India and a person resident outside India;

(vi) Deposits between persons resident in India and persons resident outside India;

(vii) The export, import or holding of currency or currency notes;

(viii) The transfer of real property outside India, other than by way of a lease not exceeding five years, by

a person resident in India;

(ix) The acquisition or transfer of real property in India, other than by way of a lease not exceeding five years, by a person resident outside India; and

(x) The giving of a guarantee or surety with respect to any debt, obligation or other liability incurred:

- **By a person resident in India and owed to a person resident outside India; or**
- **By a person resident outside India.**

A person resident in India may hold, own, transfer or invest in foreign currency, foreign securities or any real property situated outside India if such currency, securities or property was (were) acquired, held or owned by the person when he was resident outside India or was (were) inherited from a person resident outside India. [10]

[10] FEMA, Sec. 6(4).

A person resident outside India may hold, own, transfer or invest in Indian currency or securities, or any real property situated in India if such currency, securities or property was (were) acquired, held or owned by the person when he was resident in India or was (were) inherited from a person who was resident in India. [11]

[11] FEMA, Sec. 6(5).

The RBI may, by regulation, prohibit, restrict or regulate the establishment in India of a branch, office or other place of business by a person resident outside India for carrying on any activity relating to the branch, office or other place of business. [12]

[12] FEMA, Sec. 6(6).

The RBI has made detailed regulations governing different types of permissible capital account transactions. The regulations lay down substantive law governing such transactions. [13]

[13] Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000.

d. Current Account Transactions

A current account transaction means a transaction other than a capital account transaction and, without prejudice to the generality of the foregoing, includes:

(i) Payments due in connection with foreign trade, other current business, or services, and short-term banking and credit facilities in the ordinary course of business;

(ii) Payments due as interest on a loan and as net income from investments;

(iii) Remittances for the living expenses of a parent, a spouse or a child residing abroad; and

(iv) Expenses in connection with the foreign travel, education or medical care of a parent, a spouse or a child. [14]

[14] FEMA, Sec. 2(j).

Any person may sell or draw foreign exchange to or from an authorized dealer if the sale or drawing is a current account transaction, subject to rules made by the central government to that effect. [15]

[15] FEMA, Sec. 5.

The central government has drawn up rules under which current account transactions have been broadly classified as: [16]

[16] Foreign Exchange Management (Current Account Transactions) Rules, 2000.

(i) Transactions that are prohibited;

(ii) Transactions that require the prior approval of the Government of India; or

(iii) Transactions exceeding certain monetary limits, which require the prior approval of the RBI.

Nothing contained in (ii) or (iii) applies to the withdrawal of funds made out of funds held in the Exchange Earners' Foreign Currency (EEFC) account of the remitter.

e. Foreign Companies

(1) Branch Office

Companies incorporated outside India and engaged in manufacturing and trading activities are allowed to set up a branch office in India with the specific approval of the RBI. A branch office of a foreign company is permitted to represent its parent or group company and to carry on the following activities:

(i) The exporting and importing of goods;

(ii) The rendering of professional or consultancy services;

(iii) The carrying out of research work, in which the parent company is engaged;

(iv) The promotion of technical or financial collaboration between Indian companies and a parent or overseas group of companies;

(v) The representation of a parent company in India and acting as a buying or selling agent in India;

(vi) The rendering of information technology services and the development of software in India;

(vii) The rendering of technical support in relation to the products supplied by a parent company or group companies; and

(viii) The activities of a foreign airline/shipping company.

Normally, the branch office should be engaged in the activity in which the parent company is engaged.

A branch office in India is not allowed to carry on retail trading activities of any nature. Nor is a branch office is allowed to carry on manufacturing or processing activities in India, whether directly or indirectly.

Branch offices are permitted to acquire property for their own use and to carry on the permitted or incidental activities, but not in order to lease or rent out the property. Entities from Afghanistan, Bangladesh, China (PRC), Iran, Pakistan and Sri Lanka are not allowed to acquire real property in India even for purposes of a branch office. Such entities are, however, allowed to lease such property for a period not exceeding five years.

Profits earned by branch offices are freely remittable from India, subject to the payment of applicable taxes.

Branch offices are required to submit Annual Activity Certificates from Chartered Accountants as at the end of March 31, on or before April 30, to the designated authorized dealer (for onward submission to the RBI) and copies to the Directorate General of Income Tax (International Taxation).

The RBI has given general permission to foreign companies to establish branches or units in SEZs to undertake manufacturing and service activities. The general permission is subject to the following conditions:

(i) Such units function in those sectors where 100% FDI is permitted;

(ii) Such units comply with Part XI of the Companies Act, 1956 (Sections 592 to 602); and

(iii) Such units function on a stand-alone basis.

In the event of the winding-up of business, in order to remit the winding-up proceeds, the branch office must approach the authorized dealer with the required documents.

(2) Liaison Office

A "liaison office" is a place of business that functions as a channel of communication between the principal place of business or head office (by whatever name called) and entities in India, but that does not undertake any business, commercial, trading or industrial activity, whether directly or indirectly, and may not earn any income in India. A liaison office must maintain itself out of inward remittances received from abroad through normal banking channels. The role of a liaison office is, therefore, limited to collecting information about possible market opportunities and providing information about the company and its products to prospective Indian customers. Permission to set up such an office is initially granted for a period of three years and the authorized dealer may extend this for a period of three years from the date of the original approval/extension granted by the RBI. However, the extension is subject to the fulfillment of certain conditions by the applicant.

A liaison office established in India by a foreign company is permitted to carry on the following activities:

(i) Representing in India a parent company or group companies;

(ii) Promoting exports or imports from or to India;

(iii) Promoting technical or financial collaboration between parent or group companies and companies in India; and

(iv) Acting as a communication channel between a parent company and Indian companies.

Liaison offices are required to submit Annual Activity Certificates from Chartered Accountants as at the end of March 31, on or before April 30, to the designated authorized dealer (for onward submission to the RBI) and copies to the Directorate General of Income Tax (International Taxation).

(3) Project Office

A project office is a place of business that represents the interests of a foreign company executing a project in India but does not include a liaison office.

A project office may be established in India by a person resident outside India to execute a project in India under a contract with an Indian company if:

(i) The project is funded directly by inward remittance from abroad;

(ii) The project is funded by a bilateral or multilateral international financing agency (for example, the World Bank or the International Monetary Fund (IMF));

(iii) The project has been cleared by an appropriate authority; or

(iv) The company or entity in India awarding the contract has been granted a term loan for the project by a public financial institution or bank in India.

The approval may be granted subject to such terms and conditions as may be considered necessary by the RBI.

(4) Procedure

An application for establishing a branch office, liaison office or project office must be made to the RBI (see the Worksheets). In the cases of a branch and a liaison office, the necessary documents for application are to be routed via a designated authorized dealer. However, foreign banks and insurance companies must apply directly to the Department of Banking Operations and Development (DBOD), Reserve Bank, Central Office and the Insurance Regulatory and Development Authority (IRDA), respectively. Approval of the RBI is not required for establishing a branch/unit in a Special Economic Zone for undertaking manufacturing and service activities, subject to compliance with certain specified conditions.

The profits of a branch or the surplus of a project office on its completion may be remitted outside India, subject to compliance with the requisite procedure. [17]

---

[17] **Foreign Exchange Management (Establishment in India of Branch or Office or other place of Business) Regulations, 2000.**

---

(5) Eligibility Criteria for Establishment of Branch/ Liaison Office in India

An application from a foreign entity to establish a branch/liaison office in India is considered based on the following two criteria:

(i) Basic criteria:

• Where RBI approval is required: the principal business of the foreign entity falls within a sector in which 100% FDI is permissible under the Automatic Route; or

• Where Government approval is required: the principal business of the foreign entity falls within a sector in which 100% FDI is not permissible under the Automatic Route. Applications from entities falling under this category are considered by the RBI, in consultation with the Government of India, Ministry of Finance.

(ii) Additional criteria:

• A branch office: (a) should have been in a profitable position during the immediately preceding five financial years in the home country; and (b) should have a net worth of not less than US$ 100,000 or its equivalent.

• A liaison office: (a) should have been in a profitable position during the immediately preceding three financial years in the home country; and (b) should have a net worth of not less than US$ 50,000 or its equivalent.

Applicants that do not satisfy the eligibility criteria and are subsidiaries of other companies may submit a Letter of Comfort from their parent company as per the prescribed format, subject to the condition that the parent company satisfies the eligibility criteria as prescribed.

Note: **Net worth is defined as the total of paid-up capital and free reserves, less intangible assets as per the latest audited balance sheet or account statement certified by a certified public accountant or any registered accounts practitioner by whatever name called.**

(6) Unique Identification Number

To provide a uniform framework, a Unique Identification Number (UIN) will be allotted to existing, as well as new, branch and liaison offices.

f. Exports

The export of goods or services (in physical or any other form) from India requires a declaration by the exporter to the RBI or to such other authority in such form and in such manner as may be specified, providing material particulars. The declaration must include the amount representing the full export value of the goods in the overseas market or, if the full export value is not ascertainable at the time of export, the value that the exporter, having regard to the prevailing market conditions, expects to receive on the sale of the goods in a market outside India. Where no specified form applies to a service export, such service may be exported without the furnishing of a declaration. However, in such cases, the regulations relating to realization and repatriation of the export proceeds to India, will apply.

The exporter must also furnish the RBI such other information as may be required by the RBI for purposes of ensuring the realization of the export proceeds.

The RBI may, for purposes of ensuring that the full export value of the goods, or such reduced value as the RBI may determine, having regard to the prevailing market conditions, is received without any delay, direct any exporter to comply with such requirements.

The RBI has also issued a list of exports for which no declaration is required. For example, trade samples of goods and publicity material supplied free of charge do not need to be declared.

The FEMA also deals with the realization and repatriation of foreign exchange. It imposes a duty on every person resident in India to whom any foreign exchange is due or has accrued to take all reasonable steps to realize and repatriate the foreign exchange to India within the time and in the manner specified by the RBI.

If it is not possible to realize and repatriate the export proceeds within the prescribed time frame, an application should be made to the RBI through the authorized dealer. The RBI may extend the period for realization and repatriation, and may impose conditions.

An exporter may receive an advance payment (with or without interest) from an overseas buyer, when:

(i) The shipment of goods is made within one year of the receipt of the advance payment;

(ii) The rate of interest on the advance payment does not exceed LIBOR plus 100 basis points; and

(iii) The documents covering the shipment are routed through the authorized dealer through whom the advance payment is received.

Where the exporter is unable to ship the goods within one year, the advance payment may be refunded with the approval of the RBI.

Where the export of goods or services is to be made on deferred payment terms or in execution of a turnkey or civil construction contract, the exporter must submit the proposal for the prior approval of the approving authority for consideration in accordance with the guidelines of the RBI.

An exporter of goods or services may retain the permitted portion of foreign exchange earned by him with an authorized dealer in foreign currency in an account known as the EEFC account, up to a specified percentage of receipts.

g. Real Property

(1) Acquisition and Transfer of Real Property Outside India

The FEMA prohibits a person resident in India from acquiring holding, owning, possessing or transferring any real property situated outside India. The prohibition does not apply to a lease of real property situated outside India if the lease period is not more than five years.

(i) The prohibition does not apply if:

- **The real property was acquired, held or owned by a person when he was resident outside India; or**
- **The real property is inherited from a person who was resident outside India.**

(ii) The regulations exempt the holding of property by a person resident in India if:

- **The person resident in India is a foreign national; or**
- **The property was acquired on or before July 8, 1947, and continues to be held by the person with the permission of the RBI.**

(iii) The RBI has granted general permission to a person resident in India to acquire property outside India if the property is acquired:

- **By way of gift or inherited from a person referred to in (i), or if the property is acquired by the resident person on or before July 8, 1947, and continues to be held by the person with the permission of the RBI; or**
- **By way of purchase out of foreign exchange held in a Resident Foreign Currency (RFC) account maintained by the resident person.**

(iv) A person resident in India is permitted to transfer real property, acquired by him as described above in (iii), by way of gift to a relative who is resident in India. For this purpose, "relative" in relation to an individual means the husband or wife, brother or sister or any lineal ascendant or descendant of that individual.

A company incorporated in India having overseas offices, may acquire real property outside India for its business and for the residential purposes of its staff, in accordance with the directions issued by the RBI.

(2) Acquisition and Transfer of Real Property in India

A person resident outside India who is a citizen of India (i.e., an NRI) is permitted to acquire or transfer any real property situated in India subject to such conditions as may be considered necessary by the RBI.

All persons, whether resident in India or outside India, who are citizens of Afghanistan, Bangladesh, Bhutan, China (PRC), Iran, Nepal, Pakistan or Sri Lanka, require prior permission from the RBI to acquire or transfer any real property in India.

These restrictions do not apply to leases of real property, if the lease period is not more than five years.

The RBI has granted general permission to a person resident outside India to hold, own or transfer any real property situated in India if the property was acquired, held or owned by the person when the person was resident in India or inherited from a person who was resident in India.

An Indian citizen resident outside India is permitted:

(i) To acquire real property in India, not being agricultural land or a plantation or farm house, only by way of purchase out of funds:

- **Received in India through normal banking channels by way of inward remittance from any place outside India; or**
- **Held in any nonresident account maintained in accordance with the provisions of the FEMA and the**

regulations made by the RBI under the FEMA.

The purchase price for acquiring the real property may not be paid either by traveler's checks or foreign currency notes or by any other mode than that stated above.

(ii) To transfer real property, not being agricultural land or a plantation or farm house, to a person who is:

- **A person resident in India;**
- **A citizen of India resident outside India; or**
- **A PIO resident outside India.**

(iii) To transfer agricultural land or a plantation or a farm house acquired by way of inheritance only to Indian citizens permanently residing in India.

"Person of Indian origin" (PIO) means an individual (not being a citizen of Afghanistan, Bangladesh, Bhutan, China (PRC), Iran, Nepal, Pakistan or Sri Lanka):

(i) Who at any time has held an Indian passport; or

(ii) Whose father or mother or grandfather or grandmother was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955 (57 of 1955). [18]

---

[18] **Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, Sec. 2(c).**

A PIO is permitted to:

(i) Acquire any real property, not being agricultural land or a plantation or a farm house in India, by way of:

- **Purchase out of funds received in India through normal banking channels by way of inward remittance from any place outside India; or**
- **Purchase out of funds held in any nonresident account maintained in accordance with the provisions of the FEMA and the regulations made by the RBI under the FEMA.**

The purchase price for acquiring the real property may not paid either by traveler's checks or foreign currency notes or by any other mode other than stated above.

- **By way of gift from a person resident in India or a person resident outside India who is citizen of India, or a PIO.**

(ii) Acquire any real property in India by way of inheritance from:

- **A person resident in India; or**
- **A person resident outside India who acquired the property in accordance with the provisions of the foreign exchange law at the time of acquisition or the regulations under that law.**

(iii) Transfer any real property in India, not being agricultural land or a plantation or farm house, by way of:

- **Sale or gift to a person who is resident in India;**
- **Gift to a person resident outside India who is citizen of India; or**
- **Gift to a PIO.**

(iv) Transfer agricultural land or a plantation or farm house in India acquired by way of inheritance by way of gift or sale to a person resident in India who is a citizen of India.

(v) Transfer residential or commercial property in India by way of gift to:

- **A person resident in India;**
- **A person resident outside India who is a citizen of India; or**

- **A PIO resident outside India.**

NRIs or PIOs may rent out their real property in India. As the income from such rental would be received on current account, the rental income may be freely repatriated outside India.

A person resident outside India or a foreign company that has established in India, in accordance with the Foreign Exchange Management (Establishment in India of Branch or Office or other Place of Business) Regulations, 2000, a branch, office or other place of business for carrying on in India any activity, excluding a liaison office, is, subject to exceptions, granted general permission to:

(i) Acquire any real property in India that is necessary for or incidental to the carrying on of such activity; and

(ii) Transfer by way of mortgage to an authorized dealer as a security for any borrowing, real property acquired in accordance with (i).

The person or entity concerned is required to file a declaration with the RBI within 90 days of such acquisition.

Where real property, other than agricultural land, a farm house or plantation property in India is sold by a person resident outside India who is a citizen of India or a PIO, the authorized dealer may allow the sale proceeds to be repatriated outside India, provided the following conditions are satisfied:

(i) The real property was acquired by the seller in accordance with the provisions of the foreign exchange law or its regulations.

(ii) The amount to be repatriated does not exceed:

- **The amount paid for the acquisition of the real property in foreign exchange received through normal banking channels or out of funds held in an FCNR account; or**

- **The foreign currency equivalent, as of the date of payment, of the amount paid where payment was made out of funds held in an NRE account for the acquisition of the property.**

(iii) In the case of residential property, only the sale proceeds with respect to no more than two such properties may be repatriated.

In the case of the sale of real property purchased out of rupee funds, authorized dealers may allow the repatriation of funds out of balances held by a person resident outside India who is a citizen of India or a PIO in his NRO account up to US$ 1 million per financial year, subject to an undertaking given by the remitter and a certificate from the chartered accountant.

No citizen of Afghanistan, Bangladesh, Bhutan, China (PRC), Iran, Nepal, Pakistan or Sri Lanka may acquire or transfer real property in India, other than by way of a lease not exceeding five years, without the prior permission of the RBI. [19]

---

[19] Foreign Exchange Management (Acquisition and Transfer of Immovable Property in India) Regulations, 2000.

Foreign nationals of non-Indian origin resident outside India are not permitted to acquire any real property in India unless such property is acquired by way of inheritance from a person who was resident in India. Foreign nationals of non-Indian origin who have acquired real property in India by way of inheritance or purchase with the specific approval of the RBI may not transfer such property without the prior permission of the RBI.

h. Remittance of Dividends and Interest

The remittance of dividends and interest relating to investments made with repatriation rights is freely permitted. Indian companies intending to remit dividends or interest to nonresidents should apply to their authorized dealers. Authorized dealers allow remittances after verifying that they are not prohibited by the terms of the RBI permission and that the appropriate withholding tax has been paid.

i. Other Provisions

Authorized dealers (comprising all schedule banks, i.e., banks under Schedule I to the Reserve Bank of India Act, 1932), licensed money changers and offshore banking units are the only persons authorized under the FEMA to effect transactions in foreign exchange and foreign securities. [20]

---

[20] FEMA, Sec. 10.

C. Outward Investment from India

1. Direct Investment Outside India

a. Permission for Direct Investment in Certain Cases

A company incorporated in India or a body created under an Act of Parliament or a partnership firm registered under the Partnership Act, 1932 or any other entity notified by the RBI (an Indian party) may make direct investment in a joint venture (JV) or wholly-owned subsidiary (WOS) outside India, subject to the following conditions:

(i) The total financial commitment of the Indian party in JVs/WOSs does not exceed 400% of the net worth of the Indian party as of the date of the last audited balance sheet.

Note: **For purposes of determining "total financial commitment" within the limit of 400% of net worth, the following are taken into account:**

- **Remittance by market purchases, namely in freely convertible currencies; in the case of Bhutan, investment made in freely convertible currencies or equivalent Indian rupees; in the case of Nepal, investment made only in Indian rupees;**
- **Capitalization of export proceeds and other dues and entitlements as specified inj, below;**
- **100% of the value of guarantees issued by the Indian party to or on behalf of the JV company or WOS. The guarantee may not be open ended;**
- **Investment in agricultural operations through overseas offices or directly;**
- **ECB in conformity with other parameters of the ECB guidelines;**
- **Utilization of proceeds of foreign currency funds raised through ADR/GDR issues;**
- **Exchange of ADRs/GDRs issued in accordance with the guidelines issued by the central government; and**
- **Swaps of shares.**

(ii) The direct investment is made in an overseas JV or WOS engaged in a *bona fide* business activity.

(iii) The Indian party is not on the RBI's exporters caution list or list of defaulters with respect to the banking system circulated by the RBI or under investigation by any investigation or enforcement agency or regulatory body.

(iv) The Indian party has submitted the annual performance report up to date on Form APR (see the Worksheets) with respect to all its overseas investments.

(v) The Indian party routes all transactions relating to the investment in the JV/WOS through only one branch of an authorized dealer to be designated by it.

Note: **The Indian party may designate different branches of authorized dealers for different JVs/WOSs outside India.**

The following investments are not permitted without the prior approval of the RBI:

(i) Investments in real estate business; and

(ii) Investments in banking business.

Note 1: **"Real estate business" means buying and selling real estate or trading in Transferable Development Rights (TDRs) but does not include the development of townships, or the construction of residential or commercial premises, roads or bridges.**

Note 2: **Investments in Pakistan are not permitted.**

Investments may be funded out of one or more of the following sources, namely:

(i) Withdrawal of foreign exchange from a bank in India;

(ii) Balances held in the EEFC account of the Indian party maintained with an authorized dealer in accordance with the Foreign Exchange Management (Foreign Currency Accounts by a Person Resident in India) Regulations, 2000.

The ceiling of 400% mentioned above does not apply where the investment is funded from the source in (ii). The Indian party is required to make an application to an authorized dealer (bank) with the prescribed enclosures and documents.

An Indian party may, subject to certain conditions, extend a loan or a guarantee to or on behalf of the JV/WOS abroad, within the permissible financial commitment, provided the Indian party has made an investment by way of contribution to the equity capital of the JV/WOS.

An Indian party may make a direct investment without any limit in any foreign security, out of the proceeds of its international offering of shares through the mechanism of ADRs/GDRs, subject to certain conditions.

For purposes of investment by way of remittance from India in an existing company outside India, a valuation of the shares of the company outside India must be made:

(i) Where the investment is more than US$ 5 million, by a Category I merchant banker registered with the SEBI, or an investment banker or merchant banker outside India registered with the appropriate regulatory authority in the host country; and

(ii) In all other cases, by a chartered accountant or a certified public accountant.

For purposes of investment by way of the acquisition of shares of an existing company outside India where the consideration is to be paid fully or partly by the issue of the Indian party's shares, the valuation of shares of the company outside India must in all cases be carried out by a Category I merchant banker registered with the SEBI or an investment banker or merchant banker outside India registered with the appropriate regulatory authority in the host country. FIPB approval is required in such cases.

Investment in a JV/WOS abroad by an Indian party through the medium of a Special Purpose Vehicle (SPV) is also permitted under the Automatic Route subject to the conditions that the Indian party is not included in the RBI's caution list or under investigation by the Enforcement Directorate or included in the list of defaulters. Indian parties whose names appear in the defaulters' list require the prior approval of the RBI for such an investment. Setting up an SPV under the Automatic Route is permitted only for purposes of investment in JVs/WOSs overseas.

b. General Permission for Investment in Agricultural Operations Overseas Directly or Through Overseas Offices

A person resident in India, being a company incorporated in India or a partnership firm registered under the Indian Partnership Act, 1932, may undertake agricultural operations overseas including the purchase of land incidental to such activity either directly or through overseas offices, subject to the following conditions:

(i) The Indian party is otherwise eligible to make the investment (as specified in a, above) and such investment is within the overall limits, as specified; and

(ii) For purposes of investment under this regulation by the acquisition of land overseas, the valuation of the land is certified by a certified appraiser registered with the appropriate authority in the host country.

c. General Permission for Investment in the Equity of a Company Registered Overseas

A listed Indian company may invest in:

(i) The shares of an overseas company listed on a recognized stock exchange; and

(ii) Rated bonds or fixed income securities issued by such an overseas company and rated no lower than investment grade by accredited or registered credit rating agencies, subject to the following conditions:

- **In the case of investment by a listed Indian company, the investment does not exceed 50% of its net worth as of the date of its last audited balance sheet; and**
- **Every transaction relating to the purchase and sale of the shares of the overseas company or the bonds or securities is routed through the designated branch of an authorized dealer in India.**

Resident individuals are permitted to invest in equity and in rated bonds or fixed income securities of overseas companies as permitted in terms of the limits and conditions specified under the Liberalised Remittance Scheme.

d. Investment by Mutual Funds

Mutual funds registered with the SEBI may invest, within specified limits, in the ADR/GDR issues of Indian and

foreign companies, shares or rated bonds or fixed income securities of an overseas company listed on a recognized stock exchange, investment grade rated foreign debt securities, money market instruments, repos in the form of investment government securities, short term deposits, specified derivatives traded on recognized overseas stock exchanges, or exchange traded funds and overseas mutual funds that make nominal investments in unlisted overseas securities or in such other securities as may be stipulated by the RBI.

Domestic VCFs registered with the SEBI may invest, within specified limits, in equity and equity linked investments of offshore VCUs.

Every transaction relating to the purchase and sale of foreign securities by mutual funds must be routed through the designated branch of an authorized dealer in India.

e. Investment in the Financial Services Sector

An Indian party may make an investment in an entity outside India engaged in financial services activities, subject to the regulations discussed in a, above and the following additional conditions:

(i) It has earned a net profit during the preceding three financial years from the financial services activities.

(ii) It is registered with the regulatory authority in India for conducting the financial services activities.

(iii) It has obtained approval from the concerned regulatory authorities both in India and abroad, for venturing into such financial sector activities.

(iv) It has met the prudential norms relating to capital adequacy as prescribed by the relevant regulatory authority in India.

Any additional investment by an existing JV/WOS or its step-down company in the financial services sector may be made only after the conditions stipulated above are complied with.

Unregulated entities in the financial sector in India may invest in nonfinancial sector activities, subject to fulfilling the conditions set out in a, above. Trading in commodities exchanges and setting up JVs/WOSs will be reckoned to be financial services activities and will require clearance from the Forward Markets Commission.

f. Approval of the Reserve Bank in Certain Cases

An Indian party that does not satisfy the eligibility norms set out above may apply to the RBI for approval.

Application for direct investment in a JV/WOS outside India, or by way of exchange for shares of a foreign company, must be made on Form ODI (see the Worksheets).

An application made on Form ODI:

(i) For purposes of investment by way of remittance from India in an existing company outside India, must be accompanied by a valuation of the shares of the company outside India, made:

- **Where the investment is more than US$ 5 million, by a Category I merchant banker registered with the SEBI or an investment banker or merchant banker registered with the appropriate regulatory authority in the host country; and**
- **In all other cases, by a chartered accountant or a certified public accountant.**

(ii) For purposes of investment by way of the acquisition of shares of an existing company outside India where the consideration is to be paid fully or partly by the issue of the Indian party's shares, must be accompanied by a valuation carried out by a Category I merchant banker registered with the SEBI or an investment banker or merchant banker registered with the appropriate regulatory authority in the host country.

The RBI may, *inter alia*, take into account the following factors in considering the application as above:

(i) The *prima facie* viability of the JV/WOS outside India;

(ii) The contribution to external trade and other benefits that will accrue to India through the investment;

(iii) The financial position and business track record of the Indian party and the foreign entity; and

(iv) The expertise and experience of the Indian party in a line of activity that is the same as, or related to, that of the JV or WOS outside India.

g. Investment in Unincorporated Entities Overseas in the Oil Sector

An Indian company is permitted under the Automatic Route to invest in unincorporated entities overseas in the oil sector up to 400% of its net worth, subject to the approval of the competent authority, if it is approved by Board resolution. Investment in excess of 400% of the net worth of an Indian company requires the prior approval of the RBI.

h. Investment in the Energy and Natural Resources Sector

The RBI will consider applications for investment by an Indian company in a JV/WOS overseas in the energy and natural resources sectors (for example, oil, gas, coal and mineral ores) in excess of 400% of the net worth of the Indian company as of the date of its last audited balance sheet.

i. Consortium with Other International Operators

Indian companies are allowed to participate in a consortium with other international operators to construct and maintain submarine cable systems on a co-ownership basis under the Automatic Route. Authorized dealers may allow remittances by an Indian company for overseas direct investment after ensuring that the Indian company has obtained necessary license from the Department of Telecommunication, Ministry of Telecommunication and Information Technology, Government of India, to establish, install, operate and maintain international long distance services, also by obtaining a certified copy of the board resolution approving such investment.

j. Unique Identification Number

The RBI will allot a unique identification number for each JV or WOS outside India, which the Indian party must quote in all its communications and reports to the RBI and the authorized dealer.

k. Investment by Capitalization

An Indian party may make a direct investment outside India in accordance with the regulations discussed above by way of capitalization in full or in part of the amount due to the Indian party from the foreign entity towards:

> **(i) Payment for the export of plant, machinery, equipment and other goods or software to the foreign entity; or**
>
> **(ii) Fees, royalties, commissions or other entitlements due to the Indian party from the foreign entity for the supply of technical know-how, consultancy, managerial or other services.**

Where the export proceeds have remained unrealized beyond the period prescribed for realization and fees, royalties, commissions or other entitlements of the Indian party have remained unrealized from the date on which such payment is due, such proceeds may not be capitalized without the prior permission of the RBI.

An Indian software exporter may receive, in the form of shares, up to 25% of the value of exports to an overseas software start-up company without entering into a JV agreement, by filing an application with the RBI through the authorized dealer.

l. Export of Goods Towards Equity — Procedure

An Indian party exporting goods, software or plant and machinery from India towards an equity contribution in a JV or WOS outside India must declare it on form GR, SDF or SOFTEX, which must be superscribed "Exports against equity participation in the JV/WOS abroad" and also quote the identification number, if such a number has already been allotted by the RBI.

The Indian party must, within 15 days of effecting the shipment of the goods, submit to the RBI a custom certified copy of the invoice through the branch of an authorized dealer designated by it.

An Indian party capitalizing exports as described above must, within six months from the date of export or such further time as may be allowed by the RBI, submit to the RBI, copy (ies) of the share certificate(s) or any document issued by the JV or WOS outside India to the satisfaction of the RBI evidencing the investment from the Indian party, together with the duplicate of the GR, SDF or SOFTEX form, through the branch of an authorized dealer designated by it.

m. Post-Investment Changes/Additional Investment in Existing Joint Venture/Wholly Owned Subsidiary

A JV/WOS set up by an Indian party may diversify its activities, set up a step-down subsidiary or alter the shareholding pattern in the overseas entity, subject to the condition that the Indian party reports to the RBI the details of such decisions taken by the JV/WOS within 30 days of the approval of those decisions by the competent authority concerned for the JV/WOS in the host country, and includes the same in the annual performance report filed annually with the RBI.

n. Acquisition of a Foreign Company Through Bidding or Tender Procedure

On being approached by an Indian party that is eligible to make an investment outside India, an authorized dealer may allow remittances towards earnest money deposit or issue a bid bond guarantee on its behalf for participation in a bidding or tender procedure for the acquisition of a company incorporated outside India.

On the Indian party winning the bid:

(i) The authorized dealer may allow further remittances towards acquisition of the foreign company, subject to the ceilings specified above; and

(ii) The Indian party must submit a report to the RBI on Form ODI (see the Worksheets), through the authorized dealer concerned, within 30 days of effecting the final remittance.

For participation in a bidding or tender procedure for the acquisition of a company incorporated outside India that does not fall within the provisions above, the RBI may, on the submission of an application on Form ODI (see the Worksheets), allow the remittance of foreign exchange towards earnest money deposit or permit the authorized dealer in India to issue a bid bond guarantee, subject to such terms and conditions as the RBI may stipulate.

If the Indian party is successful in the bid, but the terms and conditions of the acquisition of the company outside India:

(i) Are not in conformity with the provisions of the regulations, as set out above, or different from those for which approval was obtained, the Indian party must submit an application on Form ODI (see the Worksheets) to the RBI for obtaining approval for the FDI in the manner specified in g, above; or

(ii) Are in conformity with the provisions of the regulations, as set out above, or the same as those for which approval was obtained, the Indian party must submit a report to the RBI, giving details of the remittances made, within 30 days of effecting the final remittance.

o. Obligations of the Indian Party

An Indian party that has acquired a foreign security as discussed above must:

(i) Obtain share certificates or any other document as evidence of investment in the foreign entity to the satisfaction of the RBI within six months, or such further period as the RBI may permit;

(ii) Repatriate to India all dues receivable from the foreign entity, such as dividends, royalties, technical fees etc., within 60 days of their falling due, or such further period as the RBI may permit. Special rules apply in the case of investments in securities in Bhutan; and

(iii) Submit to the RBI every year within 60 days from the date of expiry of the statutory period, as prescribed by the respective laws of the host country for the finalization of the audited accounts of the JV/WOS outside India or such further period as may be allowed by the RBI, an annual performance report on Form APR (see the Worksheets) with respect to each JV or WOS outside India set up or acquired by the Indian party and such other reports or documents as may be stipulated by the RBI.

Note: **An individual partner must hold shares for and on behalf of the firm in an overseas JV/WOS in the individual's name if the host country regulations or operational requirements mandate such holdings, subject to the condition that the entire funding for the investment is done by the firm.**

p. Transfer by Way of Sale of Shares of a Joint Venture/Wholly Owned Subsidiary Outside India

An Indian party may transfer by way of sale to another Indian party who complies with the provisions set out above, or to a person resident outside India, any share or security held by him in a JV/WOS outside India, without the prior approval of the RBI in the cases set out below:

(i) In cases where the JV/WOS is listed on the overseas stock exchange;

(ii) In cases where the Indian promoter is listed on a stock exchange in India and has a net worth of not less than Rs.1 billion; and

(iii) Where the Indian promoter is an unlisted company and the investment in the overseas venture does not exceed US$ 10 million, subject to the following conditions:

- **The sale does not result in any write off of the investment made;**
- **The sale is effected through a stock exchange on which the shares of the overseas JV/WOS are listed;**
- **If the shares are not listed on a stock exchange, and the shares are disinvested by private arrangement, the share price is not less than the value certified by a chartered accountant or certified public accountant as the fair value of the shares based on the latest audited financial statements of the JV/WOS;**
- **The Indian party does not have any outstanding dues by way of dividend, technical know-how fees,**

royalty, consultancy, commission or other entitlements, and/or export proceeds from the JV/WOS;

• The overseas concern has been in operation for at least one full year and the annual performance report on Form APR (see the Worksheets) together with the audited accounts for that year has been submitted to the RBI; and

• The Indian party is not under investigation by any regulatory authority in India.

The sale proceeds of shares or securities must be repatriated to India immediately on receipt thereof and in any case not later than 90 days from the date of sale of the shares or securities, and documentary evidence to this effect must be submitted to the regional office of the RBI through the designated authorized dealer.

An Indian party that does not satisfy the criteria specified above must apply to the RBI for permission to transfer by way of sale shares of a JV/WOS outside India, which may be granted subject to such conditions as the RBI may consider appropriate. The Indian party is required to submit details of the disinvestment through its bankers, within 30 days of the disinvestment.

q. Transfer by Way of Sale of Shares Involving Write-off

Where the transfer by way of sale of shares or securities referred to in n, above by any Indian party listed on any stock exchange in India is for a price less than the amount invested in the share or the security transferred:

(i) Where the difference between that value and the sale price does not exceed the percentage, approved by the RBI, of the Indian party's actual export realization of the previous year, the Indian party may, to the extent of the difference, write off the capital invested in the overseas JV/WOS; and

(ii) Where the difference is more than the percentage, approved by the RBI, of the Indian party's actual export realization of the previous year, the Indian party must apply to the RBI for permission to write-off the capital invested, which permission may be granted subject to such conditions as the RBI considers appropriate.

r. Pledge of Shares of Joint Ventures and Wholly-Owned Subsidiaries

An Indian party may transfer, by way of pledge, shares held in a JV/WOS outside India as a security for availing itself of any fund-based or nonfund-based facilities for itself or for the JV/WOS from an authorized dealer or a public financial institution in India.

An Indian party may also transfer, by way of pledge, shares held in overseas JV/WOS to an overseas lender, provided the lender is regulated and supervised as a bank and the total financial commitment of the Indian party remains within the limit stipulated by the RBI for overseas investment.

s. Hedging of Overseas Direct Investments

Entities resident in India having overseas direct investments are permitted to hedge the exchange risk arising out of such investments. Banks may enter into forward or option contracts with resident entities that wish to hedge their overseas direct investments (in equity and loans), subject to verification of such exposure. Cancellation of such forward contracts may be permitted by banks and 50% of such cancelled contracts may be allowed to be rebooked.

If a hedge becomes naked in part or full owing to the shrinking of the market value of the overseas direct investment, the hedge may continue to the original maturity. Rollovers on the due date are permitted up to the extent of market value on that date.

2. Investments Abroad by Individuals in India

a. Prior Permission of the Reserve Bank for Direct Investment by a Proprietary Concern in India

Proprietorship concerns and unregistered partnership firms are allowed to set up JVs/WOSs outside India with the prior approval of the RBI, subject to eligibility criteria. An application on Form ODI must be filed with the Chief General Manager, RBI, Foreign Exchange Department.

b. Investment by Individuals

A resident individual may apply to the RBI for permission to acquire shares in a foreign entity offered as consideration for professional services provided to the foreign entity.

After taking into account, *inter alia*, the following factors, the RBI may grant permission, subject to such terms and conditions as are considered necessary:

(i) The credentials and net worth of the individual and the nature of his profession;

(ii) The extent of the individual's forex earnings/balances in his EEFC and/or RFC account;

(iii) The financial and business track record of the foreign entity;

(iv) The potential for forex inflow into the country; and

(v) Other likely benefits to the country.

3. Investment in Foreign Securities Other than by Way of Direct Investment

a. Prohibition on Issue of Foreign Securities by a Person Resident in India

A person resident in India, being an Indian company or a body corporate created by an Act of Parliament:

(i) May issue foreign currency convertible bonds (FCCBs) not exceeding US$ 500 million to a person resident outside India in accordance with and subject to the conditions stipulated in Schedule I to the Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004 (see the Worksheets);

(ii) May issue FCCBs of more than US$ 500 million with the specific approval of the RBI; and

(iii) May issue foreign currency exchangeable bonds (FCEBs) to a person resident outside India in accordance with and subject to certain conditions and with the specific approval of the RBI.

The company or body corporate referred to above issuing the FCCBs must, within 30 days from the date of issue, furnish a report to the RBI providing the following details and documents:

(i) The total amount for which FCCBs have been issued;

(ii) The names of the investors resident outside India and the number of FCCBs issued to each of them; and

(iii) The amount repatriated to India through normal banking channels and/or the amount received by debit to the NRE or FCNR accounts in India of the investors (duly supported by a bank certificate).

b. Permission for the Purchase/Acquisition of Foreign Securities in Certain Cases

A person resident in India, being an individual, may acquire foreign securities:

(i) By way of gift from a person resident outside India;

(ii) Issued by a company incorporated outside India under the Cashless Employees Stock Option Scheme, subject to no remittance from India being involved; and

(iii) By way of inheritance from a person whether resident in or outside India.

A person resident in India, being an individual who is an employee or a director of an Indian office or branch of a foreign company or of a subsidiary in India of a foreign company or of an Indian company in which the foreign equity holding, either directly or indirectly, is not less than 51%, may purchase equity shares offered by the foreign company, under its ESOP scheme.

Note: **For purposes of this provision, "indirectly" refers to the indirect holding of foreign equity through an SPV or a step-down subsidiary.**

Foreign companies are permitted to repurchase shares issued to resident Indians under an ESOP scheme, subject to certain conditions.

All other acquisitions not covered by a general or special permission require approval of the RBI.

An authorized dealer may allow remittance to be made by the person eligible to purchase the shares as described above.

A person resident in India may transfer by way of sale the shares acquired as described above, subject to the proceeds thereof being repatriated immediately on receipt thereof and, in any case, not later than 90 days from the date of sale of the securities.

c. Transfer of a Foreign Security by a Person Resident in India

A person resident in India who has acquired or holds foreign securities in accordance with the provisions of the Act, or rules or regulations made thereunder may transfer them by way of pledge for obtaining any fund-based or nonfund-based facilities in India from an authorized dealer or public financial institution.

d. General Permission for the Acquisition of Foreign Securities as Qualification/Rights Shares

A person resident in India, being an individual, may:

(i) Acquire foreign securities as qualification shares issued by a company incorporated outside India for holding the post of director in the company, subject to the following conditions:

- **The number of shares so acquired is the minimum required to be held for holding the post of director and in any case does not exceed 1% of the paid-up capital of the company; and**
- **Consideration for the acquisition of the shares does not exceed the ceiling stipulated by the RBI;**

(ii) Acquire foreign securities by way of rights shares in a company incorporated outside India, subject to the condition that the rights shares are being issued by virtue of the holding of shares in accordance with the provisions of the law; and

(iii) Where the person is an employee or a director of the Indian promoter company, acquire by way of purchase shares of a JV/WOS outside India of the Indian promoter company, in the field of software, subject to the following conditions:

- **The consideration for the purchase does not exceed the ceiling stipulated by the RBI;**
- **The shares so acquired do not exceed 5% of the paid-up capital of the JV/WOS outside India; and**
- **After the allotment of the shares, the percentage of shares held by the Indian promoter company, together with the shares allotted to its employees, is not less than the percentage of shares held by the Indian promoter company prior to the allotment.**

A person resident in India, being an individual holding qualification or rights shares, as described above, may sell the shares so acquired, without prior approval, provided the sale proceeds are repatriated to India through banking channels and documentary evidence is submitted to the authorized dealer.

An Indian company in the knowledge-based sector may allow its resident employees (including working directors) to purchase foreign securities under the ADR/GDR linked stock option schemes, subject to the issue of employees' stock options by a listed company being governed by the SEBI (Employees Stock Option and Stock Purchase Scheme) Guidelines, 1999 and the issue of employees' stock options by an unlisted company being governed by the guidelines issued by the government of India for the issue of ADR/GDR linked stock options. The consideration for the purchase must not exceed the ceiling stipulated by the RBI.

Note: **For purposes of this provision, "knowledge-based sector" refers to such sectors as have been notified by the Government of India in terms of its Guidelines for the Issue of ADR/GDR Linked Employees' Stock Options by Indian Companies, dated September 15, 2000.**

e. Prior Permission of the Reserve Bank of India in Certain Cases

A person resident in India, being an individual seeking to acquire qualification shares in a company outside India beyond the limits laid down above must apply to the RBI for prior approval.

f. Investment by Mutual Funds

The purchase of foreign securities by mutual funds must be subject to these regulations and such other terms and conditions as may be notified by the SEBI.

D. Industrial Policy

1. General

The Indian Government's industrial policy was first formulated in 1948. This policy, as revised, became the Industrial Policy Resolution of 1956. This resolution classified industries into three categories: one each exclusively for the public and private sectors; and the third where the state was to take the initiative, with the private sector supplementing the effort. In 1973, the licensing policy was revised. Industrial policies have adopted the concept of capacity licensing to regulate industrial growth, though in recent years attempts have been made to liberalize the provisions and gradually move away from this concept.

The Industrial Policy of 1991 marked a radical departure from earlier policies and opened up a new chapter in India's economic history. The policy abolished the system of industrial licensing in all but a small list of strategic industries. The bedrock of the package of measures included in the current policy is to let entrepreneurs make investment decisions based on their own commercial judgment. To achieve the objectives of the strategy for the industrial sector for the 1990s and beyond, the industrial policy made a number of changes to the system of industrial approvals. The industrial policy recognizes that the attainment of technological dynamism and international competitiveness requires that enterprises must be able to respond swiftly to rapidly changing external conditions. The government has changed the role of the industrial policy from one of simply exercising control to one of providing help and guidance by making essential procedures fully transparent and eliminating delays. Government policy and procedures are geared to assisting entrepreneurs in their efforts.

2. Industrial Licensing

Industrial licenses are regulated under the Industries (Development & Regulation) Act (the "IDR Act"). With the progressive liberalization and deregulation of the economy, the industrial licensing requirements have been substantially reduced. Currently, industrial licensing for manufacturing is required only:

(i) For industries retained under compulsory licensing;

(ii) For the manufacture of items reserved for the small scale industry (SSI) sector by non-SSI units; and

(iii) When the proposed location attracts locational restrictions.

a. Industries Reserved for the Public Sector

The following industries are reserved for the public sector:

(i) Atomic energy;

(ii) Industries concerned with substances specified in the schedule to the notification of the Government of India in the Department of Atomic Energy number S.O.212(E), dated March 15, 1995; and

(iii) Railway transport.

b. Industries Subject to Compulsory Licensing

The following industries are subject to compulsory licensing under the IDR Act or appropriate authority:

(i) The distillation and brewing of alcoholic drinks;

(ii) Tobacco cigars and cigarettes and manufactured tobacco substitutes;

(iii) Electronic aerospace and defense equipment;

(iv) Industrial explosives, including detonating fuses, safety fuses, gunpowder, nitrocellulose and matches;

(v) Hazardous chemicals;

(vi) Drugs and pharmaceuticals (according to the modified Drug Policy issued in September, 1994, as modified in 1999).

c. Small-Scale Sector

An industrial undertaking is defined as a small-scale unit if the capital investment in plant and machinery in the manufacturing sector does not exceed INR 50 million (approximately US$1.02 million) and investment in equipment in the service sector does not exceed INR 20 million (approximately US$410,000).

Small scale units may be registered with the Directorate of Industries/District Industries Centre of the State Government. Such units may manufacture any item and are also free from locational restrictions. Twenty-one items in various categories have been reserved for the small-scale sector.

The Government has reserved the following for exclusive manufacture in the small-scale sector:

(i) Wood and wood products;

(ii) Paper products;

(iii) Injection-molded thermo-plastic products;

(iv) Glass and ceramics;

(v) Mechanical engineering, excluding transport equipment.

d. Locational Restrictions

Industrial undertakings are free to select the location of their projects. An industrial license is required if the proposed location is within 25 km of the Standard Urban Area limits of 23 cities with a population of one million or more, as per the 1991 census. These cities are: Greater Mumbai, Kolkata, Delhi, Chennai, Hyderabad, Bangalore, Ahmedabad, Pune, Kanpur, Nagpur, Lucknow, Surat, Jaipur, Kochi, Coimbatore, Vadodara, Indore, Patna, Madurai, Bhopal, Vishakhapatnam, Varanasi and Ludhiana.

The locational restriction does not apply:

(i) If the unit was to be located in an area designated as an "Industrial area" before July 25, 1991; or

(ii) In the case of electronics, computer software and printing and any other industry that may be designated as a nonpolluting industry.

The location of industrial units is subject to applicable locational zoning and land use regulations and environmental regulations.

e. Procedure for Obtaining an Industrial License

Application for an industrial license must be made to the SIA (see the Worksheets). An industrial license is granted by the SIA at the recommendation of the Licensing Committee. Decisions are usually taken within four to six weeks.

f. Policy for Industries Exempt From Licensing

Industrial undertakings exempt from industrial license are required to file only an Industrial Entrepreneur Memorandum (IEM).

g. Carry-On-Business License

By virtue of their natural growth, small-scale units may exceed the investment limit prescribed for small-scale units. In such cases, these units need to obtain a carry-on-business (COB) license based on the best production in the preceding three years. No export obligation is fixed as to the capacity for which the COB license is granted. An application must be made and the requisite fee paid. However, on further expansion of the capacity beyond the capacity included in the COB license, a unit would need to obtain an industrial license.

h. Environmental Clearances

Entrepreneurs are required to obtain statutory clearances relating to pollution control, as may be necessary, for setting up an industrial project for 31 categories of industries specified by the Ministry of Environment and Forests under the Environmental Protection Act, 1986. The list includes petrochemical complexes, petroleum refineries, cement, thermal power plants, bulk drugs, fertilizers, dyes, paper, etc.

However, if the investment in the project is less than INR 1 billion, environmental clearance is not necessary, except in the case of pesticides, bulk drugs and pharmaceuticals, asbestos and asbestos products, integrated paint complexes, mining projects, tourism projects with certain parameters, tarred roads in the Himalayan areas, distilleries, dyes, foundries and electroplating industries.

Setting up industries in certain locations considered fragile (for example, the Aravalli Range, coastal areas, Doon valley and Dahanu) is guided by separate guidelines issued by the Ministry.

E. Monopolies and Restrictive Trade Practices Act, 1969

The Competition Act, 2002, came into effect September 1, 2009. The Monopolies and Restrictive Trade Practices Act, 1969 (MRTP), which it repeals, had become redundant post-July 1991, when the new economic policy was announced and Chapter III of the MRTP Act dealing with restrictions on mergers and acquisitions (M&A) activities was made effectively inoperative. The MRTP Commission will continue to handle all old cases filed prior to September 1, 2009, for a period of two years. It will, however, not entertain any new cases.

However, the provisions relating to M&A transactions (Sections 5 and 6 of the Competition Act, 2002, dealing with the regulation of combinations) are to be notified at a later date.

F. Competition Act, 2002

1. General

The Competition Act, 2002 is intended to ensure fair competition by prohibiting trade practices that have an appreciable adverse effect on competition in markets within India and, for this purpose, provides for the establishment of a quasi-judicial body to be called the Competition Commission of India (CCI).

2. Overall Scheme

The Act prohibits all anti-competitive agreements and abuse of a dominant position and regulates combinations.

a. Anti-Competitive Agreements

Any agreement by an enterprise or association of enterprises or person or association of persons with respect to the production, supply, distribution, storage, acquisition or control of goods or the provision of services that causes or is likely to cause an appreciable adverse effect on competition within India will, subject to certain exceptions, be prohibited.

Any agreement in contravention of the above provisions will be void.

However, the provisions do not apply to any agreement entered into by way of a JV if the agreement increases efficiency in the production, supply, distribution, storage, acquisition or control of goods or the provision of services. [21]

---

[21] Competition Act, 2002, Sec. 3.

---

b. Abuse of a Dominant Position

Abuse of a dominant position is prohibited.

A dominant position means a position of strength, enjoyed by an enterprise, in the relevant market, in India, that enables the enterprise to:

(i) Operate independently of competitive forces prevailing in the relevant market; or

(ii) Affect its competitors or consumers or the relevant market in its favor. [22]

---

[22] Competition Act, 2002, Sec. 4.

---

c. Regulation of Combinations

The acquisition of one or more enterprises by one or more persons or the merger or amalgamation of enterprises will be considered a combination of such enterprises and persons or enterprises, subject to certain conditions and the meeting of prescribed criteria.

No person or enterprise is permitted to enter into a combination that causes or is likely to cause an appreciable adverse effect on competition within the relevant market in India and such a combination will be void.

Any person or enterprise that proposes to enter into a combination must give notice to the Commission disclosing the details of the proposed combination, within the prescribed time limit. [23]

---

[23] Competition Act, 2002, Secs. 5 and 6.

---

3. Competition Commission of India

The "Competition Commission of India" was established on October 14, 2003 by the central government of India, *vide* notification S.O. 1198 (E) dated October 14, 2003. [24]

---

[24] Competition Act, 2002, Sec. 7.

It is the duty of the CCI to eliminate practices having an adverse effect on competition, promote and sustain competition, protect the interests of consumers, and ensure freedom of trade carried on by other participants, in markets in India.

In fulfilling its duties under the Act, the CCI may enter into an arrangement, with the prior approval of the central government, with any agency of any foreign country. [25]

[25] Competition Act, 2002, Sec. 18.

a. Agreements and Abuse of a Dominant Position

(1) Inquiry

The CCI has the power to inquire into alleged instances of anti-competitive agreements or an abuse of a dominant position, either on its own initiative or on:

(i) Receipt of any information from any person or consumer or his association or trade association; or

(ii) A reference made to it by the central government or a State Government or a statutory authority.

In determining whether an agreement has an appreciable adverse effect on competition, the CCI will give due regard to various economic factors. [26]

[26] Competition Act, 2002, Sec. 19.

(2) Reference by Statutory Authority

Where, in the course of proceedings before any statutory authority, an issue is raised by any party that any decision that the statutory authority has taken or proposes to take is or would be contrary to any of the provisions of the Act, then such statutory authority may make a reference with respect to the issue to the CCI.

A statutory authority may not make such a reference to the CCI of its own accord. [27]

[27] Competition Act, 2002, Sec. 21.

(3) Procedure for Inquiry

On receipt of a referral from the central government or a State Government or a statutory authority or based on its own knowledge or information, if the CCI is of the opinion that there exists a *prima facie* case, it may direct the Director General to investigate the matter.

If the report of the Director General finds that any of the provisions of the Act have been contravened and the CCI is of the opinion that further inquiry is needed, then it may inquire into the contravention. [28]

[28] Competition Act, 2002, Sec. 26.

(4) Orders by the Commission After Inquiry into Agreements or Abuse of a Dominant Position

Where after inquiry, the Commission finds that any agreement or action of an enterprise in a dominant position is in contravention of the provisions of the Act, it may impose a penalty or order the cessation of the agreement or abuse of a dominant position. [29]

[29] Competition Act, 2002, Sec. 27.

Where an enterprise enjoys a dominant position, the CCI may direct the division of the enterprise to ensure the enterprise does not abuse its dominant position. [30]

[30] Competition Act, 2002, Sec. 28.

b. Combination

(1) Inquiry into a Combination by the Commission

The CCI may, acting on its own knowledge or information relating to an acquisition or acquiring of control or merger or amalgamation, inquire into whether such a combination has caused or is likely to cause an appreciable adverse effect on competition in India. [31]

[31] Competition Act, 2002, Sec. 29.

(2) Orders of Commission with Respect to Certain Combinations

The CCI may approve a combination that does not, or is not likely to, have an appreciable adverse effect on

competition.

However, if the CCI is of the opinion that a combination has, or is likely to have, an appreciable adverse effect on competition, it may direct that the combination not take effect.

Where the CCI is of the opinion that a combination has, or is likely to have, an appreciable adverse effect on competition but the adverse effect may be eliminated by suitably modifying the combination, it may propose an appropriate modification to the combination to the parties to the combination. [32]

[32] Competition Act, 2002, Sec. 31.

G. Limited Liability Partnership Act 2008

1. Nature

a. Body Corporate

A limited liability partnership (LLP) is a body corporate formed and incorporated under the Limited Liability Partnership Act, 2008 (the "LLP Act"). It is a legal entity separate from its partners and has perpetual succession. Any change in the partners of an LLP will not affect the existence, rights or liabilities of the LLP. The provisions of the Indian Partnership Act, 1932 do not apply to an LLP. [33]

[33] Limited Liability Partnership Act, 2008 ("LLP Act"), Sec. 3.

b. Partners

Any individual or body corporate may be a partner in an LLP. However, an individual will not be capable of becoming a partner in an LLP, if:

(i) He has been found to be of unsound mind by a Court of competent jurisdiction and the finding is in force;

(ii) He is an undischarged insolvent; or

(iii) He has applied to be adjudicated as an insolvent and his application is pending. [34]

[34] LLP Act, Sec. 5.

c. Minimum Number of Partners

Every LLP must have at least two partners. If at any time the number of partners of an LLP is reduced below two and the LLP carries on business for more than six months while the number is so reduced, the person who is the only partner of the LLP during the time that it so carries on business after those six months and has the knowledge of the fact that it is carrying on business with him alone will be liable personally for the obligations of the LLP incurred during that period. [35]

[35] LLP Act, Sec. 7.

d. Designated Partners

Every LLP must have at least two designated partners who are individuals and at least one of them must be resident in India.

However, in the case of an LLP in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners in the LLP or nominees of such bodies corporate must act as designated partners.

Note: "Resident in India" means a person who has stayed in India for a period of not less than 182 days during the immediately preceding year.

Subject to the above provisions:

(i) If the incorporation document:

- **Specifies who are to be designated partners, such persons must be designated partners on incorporation; or**
- **States that each of the partners from time to time is to be a designated partner, every partner must be a designated partner.**

(ii) Any partner may become a designated partner by and in accordance with the LLP agreement and a partner may cease to be a designated partner in accordance with the LLP agreement.

An individual may not become a designated partner in any LLP unless he has given his prior consent to act as such to the LLP.

Every LLP must file with the Registrar the particulars of every individual who has given his consent to act as a designated partner in such form and manner as may be prescribed within 30 days of his appointment.

An individual eligible to be a designated partner must satisfy such conditions and requirements as may be prescribed.

Every designated partner of an LLP must obtain a Designated Partner Identification Number (DPIN) from the central government. [36]

[36] **LLP Act, Sec. 7.**

e. Liabilities of Designated Partners

A designated partner will be:

(i) Responsible for doing all acts, matters and things that are required to be done by the LLP with respect to compliance with the provisions of the LLP Act, including filing any document, return, statement and the like report pursuant to the provisions of the LLP Act and as may be specified in the LLP agreement; and

(ii) Liable to all penalties imposed on the LLP for any contravention of those provisions. [37]

[37] **LLP Act, Sec. 8.**

f. Changes in Designated Partners

An LLP may appoint a designated partner within 30 days of a vacancy arising for any reason and the respective provisions of the LLP Act will apply with respect to the new designated partner.

However, if no designated partner is appointed, or if at any time there is only one designated partner, then each partner will be deemed to be a designated partner. [38]

[38] **LLP Act, Sec. 9.**

g. Punishment for Contravention of Sections 7, 8 and 9

If the LLP contravenes the provisions set out in d, e and f, above, the LLP and each partner will be punishable with a fine, which may not be less than Rs.10,000 but which may reach Rs.500,000. [39]

[39] **LLP Act, Sec. 10.**

2. Incorporation

a. Incorporation Document

For an LLP to be incorporated:

(i) Two or more persons associated for carrying on a lawful business with a view to profit must subscribe their names to an incorporation document;

(ii) The incorporation document must be filed in such manner and with such fees as may be prescribed with the Registrar of the State in which the registered office of the LLP is to be situated.

A statement made either by an advocate, a company secretary, a chartered accountant or a cost accountant who is

engaged in the formation of the LLP and by any one who subscribed his name to the incorporation document that all the requirements of the LLP Act and the rules made thereunder have been complied with, in respect of incorporation and matters precedent and incidental thereto, must be filed along with the incorporation document. [40]

[40] LLP Act, Sec. 11.

b. Incorporation by Registration

Where the set out requirements in a, above are met, the Registrar will retain the incorporation document and will, within a period of 14 days:

(i) Register the incorporation document; and

(ii) Provide a certificate to the effect that the LLP is incorporated by the name specified therein.

The Registrar may accept the statement of the advocate, company secretary, etc., as sufficient evidence that the requirements have been met.

The certificate of incorporation must be signed by the Registrar and authenticated by his official seal.

The certificate is conclusive evidence that the LLP is incorporated by the name specified therein. [41]

[41] LLP Act, Sec. 12.

c. Registered Office of LLP

Every LLP must have a registered office to which all communications and notices may be addressed and at which they will be received.

An LLP may change the place of its registered office by filing a notice of such change with the Registrar in such form and manner and subject to such conditions as may be prescribed and any such change will take effect only on such filing. [42]

[42] LLP Act, Sec. 13.

d. Effect of Registration

On registration, an LLP will, by its name, be capable of:

(i) Suing and being sued;

(ii) Acquiring, owning, holding and developing or disposing of property, whether movable or real, tangible or intangible;

(iii) Having a common seal, if it decides to have one; and

(iv) Doing and suffering such other acts and things as bodies corporate may lawfully do and suffer. [43]

[43] LLP Act, Sec. 14.

e. Name

Every LLP must have either the words "limited liability partnership" or the acronym "LLP" as the last words of its name.

No LLP may be registered by a name that, in the opinion of the central government is:

(i) Undesirable; or

(ii) Identical to or too nearly resembling that of any other partnership firm or LLP or body corporate or a registered trade mark, or a trade mark that is the subject of an application for registration, of any other person under the Trade Marks Act, 1999. [44]

[44] LLP Act, Sec. 15.

f. Reservation of Name

A person may apply, on paying the prescribed fee, to the Registrar for the reservation of a name set out in the application as:

(i) The name of a proposed LLP; or

(ii) The name to which an LLP proposes to change its name.

On receipt of such an application and the prescribed fee, the Registrar may, subject to the rules prescribed by the central government in the matter, if he is satisfied that the name to be reserved is not one that may be rejected on any ground mentioned above, reserve the name for a period of three months from the date of intimation by the Registrar. [45]

---

[45] LLP Act, Sec. 16.

---

g. Change of Name of LLP

If the central government is satisfied that an LLP has been registered (whether through inadvertence or otherwise and whether originally or by a change of name) under a name that:

(i) Is a name mentioned in e, above; or

(ii) Is identical to or too nearly resembles the name of any other LLP or body corporate or other name so as to be likely to be mistaken for it,

the central government may direct the LLP to change its name, and the LLP must comply with the direction within three months after the date of the direction or such longer period as the central government may allow. If the LLP fails to comply with the direction, it may be penalized with a fine ranging from Rs.10,000 to Rs.500,000 and the designated partner of the LLP may be penalized with a fine ranging from Rs.10,000 to Rs.100,000. [46]

---

[46] LLP Act, Sec. 17.

---

h. Application for Direction to Change Name in Certain Circumstances

Any entity that already has a name similar to the name of an LLP that is incorporated subsequently may apply to the Registrar to direct the LLP to change its name, on either of the grounds referred to in g, above. However, the Registrar will not consider any such application, unless the Registrar receives the application within 24 months from the date of registration of the LLP under that name. [47]

---

[47] LLP Act, Sec. 18.

---

i. Change of Registered Name

An LLP may change its registered name by filing with the Registrar a notice of the change and paying the prescribed fees. [48]

---

[48] LLP Act, Sec. 19.

---

3. Partners and Their Relations

a. Eligibility to Be Partners

On the incorporation of an LLP, the persons who subscribed their names to the incorporation document will be its partners; any other person may become a partner of the LLP by and in accordance with the limited liability partnership agreement. [49]

---

[49] LLP Act, Sec. 22.

---

b. Relationship of Partners

The mutual rights and duties of the partners of an LLP, and the mutual rights and duties of an LLP and its partners, will be governed by the LLP agreement between the partners, or between the LLP and its partners.

The LLP agreement and any changes made to it must be filed with the Registrar, together with the prescribed fees.

An agreement made in writing before the incorporation of an LLP between the persons who subscribe their names to

the incorporation document may impose obligations on the LLP, provided all the partners ratify the agreement after the incorporation of the LLP.

In the absence of agreement as to any matter, the provisions relating to the matter set out in the First Schedule of the LLP Act determine the mutual rights and duties of the partners and the mutual rights and duties of the LLP and the partners. [50]

---

[50] **LLP Act, Sec. 23.**

---

c. Cessation of Partnership Interest

A person may cease to be a partner of an LLP in accordance with an agreement with the other partners or, in the absence of agreement with the other partners as to ceasing to be a partner, by giving a notice in writing of not less than 30 days to the other partners of his intention to resign as a partner.

A person will cease to be a partner of an LLP:

(i) On his death or the dissolution of the LLP; or

(ii) If he is declared to be of unsound mind by a competent court; or

(iii) If he has applied to be adjudged an insolvent or declared an insolvent.

A person who has ceased to be a partner of an LLP (i.e., a former partner) will be regarded in relation to any person dealing with the LLP as still being a partner of the LLP unless:

(i) The person has been given notice that the former partner has ceased to be a partner of the LLP; or

(ii) Notice that the former partner has ceased to be a partner of the LLP has been delivered to the Registrar.

Ceasing to be a partner of an LLP does not absolve the partner concerned of an obligation to the LLP or to the other partners or to any other person that he incurred while he was a partner.

Where a partner of an LLP ceases to be a partner (a "former partner"), unless otherwise provided, the former partner or a person who is entitled to the former partner's share in consequence of the death or insolvency of the former partner will be entitled to receive from the LLP:

(i) An amount equal to the capital contribution of the former partner actually made to the LLP; and

(ii) His/her right to share in the accumulated profits of the LLP, after the deduction of accumulated losses of the LLP, determined as at the date the former partner ceased to be a partner.

A former partner or a person entitled to a former partner's share in consequence of the death or insolvency of the former partner will not have any right to interfere in the management of the LLP. [51]

---

[51] **LLP Act, Sec. 24.**

---

d. Registration of Changes in Partners

Every partner must inform the LLP of any change in his name or address within a period of 15 days of such change. If he fails to do so, the partner may be punished with a fine, which may not be less than Rs.2,000 but which may be as much as Rs.25,000.

Where a person becomes or ceases to be a partner of an LLP, the LLP must file a notice with the Registrar within 30 days from the date that person becomes or ceases to be a partner. Where there is any change in the name or address of a partner of an LLP, the LLP must file a notice with the Registrar within 30 days of such change. The relevant notice must be filed with the Registrar along with the relevant fees. If the LLP contravenes the above requirements, the LLP and every designated partner may be punished with a fine, which may not be less than Rs.2,000 but which may be as much as Rs.25,000.

A notice relating to an incoming partner must contain a statement stating his consent to become a partner. The statement must be signed and authenticated by the incoming partner. [52]

---

[52] **LLP Act, Sec. 25.**

---

4. Extent and Limitation of Liability of an LLP and Its Partners

a. Partner as Agent

Every partner of an LLP is, for purposes of the business of the LLP, the agent of the LLP, but not of other partners. [53]

[53] LLP Act, Sec. 26.

b. Extent of Liability of an LLP and its Partners

An LLP is not bound by anything done by a partner in dealing with a person if:

(i) The partner in fact has no authority to act for the LLP in doing a particular act; and

(ii) The person knows that the partner has no such authority or does not know or believe him to be a partner of the LLP.

An obligation of the LLP, whether arising in contract or otherwise, is solely the obligation of the LLP.

An LLP is liable to a person if one of its partners is liable to that person as a result of a wrongful act or omission on the partner's part committed in the course of the business of the LLP or with its authority.

The liabilities of an LLP will be met out of the property of the LLP. [54] A partner is not personally liable, either directly or indirectly, for such obligation solely by reason of being a partner of the LLP.

[54] LLP Act, Sec. 27.

In the above two cases, the personal liability of the partner for his wrongful act or omission is not be affected. A partner of an LLP is personally liable for the wrongful act or omission of any other partner of the LLP. [55]

[55] LLP Act, Sec. 28.

5. Contributions

a. Form of Contribution

The contribution of a partner to an LLP may consist of tangible, movable or real or intangible property or other benefit contributed to the LLP, including money, promissory notes, other agreements to contribute cash or property, and contracts for services performed or to be performed.

The monetary value of the contribution of each partner will be accounted for and disclosed in the accounts of the LLP. [56]

[56] LLP Act, Sec. 32.

b. Obligation to Contribute

The obligation of a partner to contribute money or other property or other benefit or to perform services for an LLP will be as set out in the LLP agreement. [57]

[57] LLP Act, Sec. 33.

6. Financial Disclosures

a. Maintenance of Books of Account, Other Records and Audit, etc.

An LLP must maintain proper books of account, as prescribed, relating to its affairs for each year of its existence on a cash basis or an accrual basis prepared using the double entry system of accounting. The books of account have to be kept at the LLP's registered office for a prescribed period.

Every LLP must, within a period of six months from the end of each financial year, prepare a Statement of Account and Solvency for that financial year as of the last day of that financial year. The statement must be signed by the designated partners of the LLP, filed, within the prescribed time, with the Registrar every year and accompanied by such fees as may be prescribed.

The accounts of an LLP must be audited in accordance with such rules as may be prescribed. However, the central government may, by notification, exempt any class or classes of LLP from such requirements.

Any LLP that fails to comply with the above provisions will be punished with fine, which may not be less than Rs.25,000 but which may be as much as Rs.500,000 and every designated partner of the LLP will be punished with a

fine, which may not be less than Rs.10,000 but which may be as much as Rs.100,000. [58]

[58] LLP Act, Sec. 34.

b. Annual Return

Every LLP must file a duly authenticated annual return with the Registrar within 60 days of the close of its financial year in such form and manner and accompanied by such fee as may be prescribed. If it fails to do so, it will be penalized with a fine, which may not be less than Rs.25,000 but which may be as much as Rs.5 million. Also, the designated partner of the LLP will be punished with fine, which may not be less than Rs.10,000 but which may be as much as Rs.100,000. [59]

[59] LLP Act, Sec. 35.

c. Inspection of Documents Kept by Registrar

The incorporation document, the names of the partners and changes and any changes thereto, the Statement of Account and Solvency and the annual return filed by each LLP with the Registrar must be available for inspection by any person in such manner and on payment of such fee as may be prescribed. [60]

[60] LLP Act, Sec. 36.

7. Conversion

a. Conversion from a Firm into an LLP

A firm may convert into an LLP in accordance with the provisions of the LLP Act and, in particular, the Second Schedule to the LLP Act. [61]

[61] LLP Act, Sec. 55.

b. Conversion from a Private Company into an LLP

A private company may convert into an LLP in accordance with the provisions of the LLP Act and, in particular, the Third Schedule to the LLP Act. [62]

[62] LLP Act, Sec. 56.

c. Conversion from an Unlisted Public Company into an LLP

An unlisted public company may convert into an LLP in accordance with the provisions of the LLP Act and, in particular, the Fourth Schedule to the LLP Act. [63]

[63] LLP Act, Sec. 57.

8. Foreign LLPs

The central government may make rules regarding the establishment by a foreign LLP of a place of business in India and the carrying on of business therein by applying or incorporating, with such modifications, as appear appropriate, the provisions of the Companies Act, 1956 or such regulatory mechanism with such composition as may be prescribed. [64]

[64] LLP Act, Sec. 57.

9. Winding Up and Dissolution

The winding up of an LLP may be either voluntary or by the Tribunal. An LLP so wound up may be dissolved. [65]

[65] LLP Act, Sec. 63.

The central government may make rules regarding the winding up and dissolution of LLPs. [66]

[66] LLP Act, Sec. 65.

A. Business Presence of a Foreign Investor

The most appropriate form of business for foreign investment in India is a limited liability company. Sole proprietorships and partnerships are the other common business forms, but, because of their unlimited liability, are not normally found suitable by overseas investors. A foreign investor may establish a business presence in India in the following ways:

(i) Through a joint venture (JV) company with an Indian partner and/or by making a public offering;

(ii) By incorporating a wholly-owned company with 100% foreign equity;

(iii) Through a liaison office for carrying on liaison work for the normal business activities of an overseas parent company, such as:

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

(iv) Through a project office for the execution of approved projects/contracts; and

(v) In the case of a foreign company engaged in manufacturing and trading activities, the opening of a branch office:

- **To represent the foreign company in India in various matters, for example, by acting as a buying/selling agent;**
- **To undertake export and import trading activities;**
- **To promote possible technical and financial collaboration between an Indian company and a foreign company;**
- **To render professional or consultancy services;**
- **To render services in information technology and the development of software in India;**
- **To render technical support in relation to the products supplied by the parent company/group companies; and**
- **To carry out research work in which the parent is engaged.**

Foreign shipping companies, airlines and banks are permitted to open branches in India on a reciprocal basis.

Foreign investors in all the above cases must obtain permission from the Reserve Bank of India (RBI) and comply with certain provisions of the Indian Companies Act, 1956 (see W, below).

India has had a company law for over a century. In general, the structure of India's company law follows the English law from which it was derived. The Companies Act, 1956, (the "Companies Act"), a comprehensive and modern corporate law, has been amended several times, most recently by the Companies (Amendment) Act, 2000. The Companies Act applies throughout India.

The Companies Act regulates the formation, financing, functioning and winding up of companies. The Companies Act prescribes a regulatory mechanism for all relevant aspects, including the organizational, financial and managerial aspects of companies. In the functioning of the corporate sector, the protection of investors and shareholders is of equal importance to the freedom of companies.

The main objects of the Companies Act are:

(i) To protect the interests of the large number of shareholders, as there is separation between the ownership and the management of a company;

(ii) To safeguard the interests of creditors;

(iii) To aid the development of companies along healthy lines;

(iv) To help in the attainment of the social and economic objectives of the government of India; and

(v) To equip the government with adequate powers of intervention in the affairs of a company in the public interest, as prescribed by law, to protect the interests of all stakeholders.

Synergies exist between the Companies Act and the regulations issued by the Securities Exchange Board of India (SEBI) in common matters relating to governance, management, the issue of securities, investor protection, etc.

Specifically, the Companies Act provides for the following, among other things:

(i) The incorporation of companies and related matters;

(ii) The issue of prospectuses and other matters relating to the issue of shares and debentures and miscellaneous provisions relating thereto;

(iii) The registration of charges;

(iv) Management and administration, and specifically the following matters:

- **Registered office;**
- **Commencement of new businesses;**
- **Registers of members and debenture holders, including foreign registers;**
- **Meetings and proceedings;**
- **Managerial remuneration;**
- **Dividend payments;**
- **Accounts and audits;**
- **Investigation of the affairs of a company; and**
- **The appointment of the Board of Directors, the conduct of Board meetings, the powers of the Board, disclosures of interest, remuneration and compensation, etc.**

(v) Provisions relating to company secretaries and managers;

(vi) The powers of the central government to remove managerial personnel at the recommendation of the Tribunal;

(vii) Arbitration, compromises, arrangements (including amalgamations) and reconstructions;

(viii) Management and the prevention of oppression;

(ix) The revival and rehabilitation of sick industrial companies;

(x) Winding up proceedings;

(xi) The incorporation of "producer companies" and related matters — a producer company is a company engaged in agriculture or any other primary activity or service that promotes the interests of farmers or consumers; and

(xii) Companies incorporated outside India that carry on business in India.

With a view to encouraging companies to adopt good corporate governance practices, leading to more transparent, ethical and fair business conduct, the following provisions have been introduced:

(i) A Director's Responsibility Statement to be included in the Director's Report;

(ii) The constitution of an Audit Committee;

(iii) The debarring of a person from acting as a director of a company if there has been default in the filing of annual returns or accounts, or the repayment of deposits, debentures, interest or dividends;

(iv) The limitation of the number of companies in which a person can be appointed a director to 15; and

(v) Clause 49 of the Listing Agreement with Stock Exchanges, which provides for the promotion and raising of the standards of corporate governance in companies (see I, 1, below).

B. Types of Company

The following three types of companies may be incorporated in India: [67]

[67] Companies Act, 1956, Sec. 12.

(i) Companies limited by shares;

(ii) Companies limited by guarantee; and

(iii) Companies with unlimited liability.

The most appropriate form of business enterprise for foreign investors is a limited liability company. Companies limited by shares may be either private or public companies.

1. Private Company

A private company is a company that has a minimum paid-up capital of Rs.0.1 million and that, by virtue of its articles:

(i) Restricts the right to transfer its shares, if any;

(ii) Limits the number of its members to 50 (excluding employees and ex-employees who are members of the company during their employment or after the cessation of their employment);

(iii) Prohibits the invitation or acceptance of deposits from persons other than its members, directors or their relatives; and

(iv) Prohibits any invitation to the public to subscribe for any of its shares or debentures. [68]

[68] Companies Act, 1956, Sec. 3(1) (iii).

The minimum number of members required for a private company is two.

Where two or more persons hold one or more shares in a company jointly, they will be treated as a single member.

A private company must have at least two directors, collectively referred as the "board of directors" or the "board."

Comment: **One advantage of a private company is that it is exempt from many of the regulatory and restrictive provisions of the Companies Act (see the Worksheets).**

A private company is the ideal form for a foreign investor not wishing to have any participation from the public. A private company may be converted into a public company at any time by following certain simple procedures.

2. Public Company

A public company is defined in the Companies Act as: "a company which

(i) Is not a private company;

(ii) Has a minimum paid up capital of Rs.500,000;

(iii) Is a private company which is a subsidiary of a public company." [69]

[69] Companies Act, 1956, Sec. 3(1)(iv).

A public company must have at least three directors, collectively referred as the "board of directors" or the "board." A public company with a paid-up capital of Rs.50 million or more and 1,000 or more shareholders holding shares with a

nominal value of Rs.20,000 or less may have a director elected by such small shareholders in the manner prescribed in the "Appointment of Small Shareholders' Director" Rules, 2001.

More specifically, a public company is a company that offers its shares to the public. The Companies Act has more comprehensive regulations for public companies with respect to public offerings, management, borrowings, and dealing with members and creditors, because there is greater public participation. A public company requires at least seven members.

Comment: **A foreign investor who is a minority partner would find comfort in participating through public companies, as the Companies Act contains specific provisions for the protection of minority shareholders.**

C. Company Formation

The formation of a company requires:

(i) Approval of the company name from the Registrar of Companies;

(ii) Determination of the state in which the registered office will be situated;

(iii) A memorandum of association specifying the company's name and objects, the location of the registered office, and the authorized capital (the memorandum of association is the company's charter); and

(iv) Articles of association specifying regulations relating to the company's internal management.

The Department of Company Affairs, Government of India, has issued guidelines to the Registrar of Companies on making a name available for registration. No company may be registered by a name that, in the opinion, of the central government is undesirable. [70]

---

[70] Companies Act, 1956. Sec. 20.

The Registrar of Companies' office verifies that the documents submitted are in order and that all the formalities necessary for company formation have been complied with. The Registrar of Companies certifies under his hand that the company is formed and issues a certificate of incorporation. The company then emerges as a legal entity with limited liability. [71]

---

[71] Companies Act, 1956, Sec. 34.

A certificate of incorporation granted by the Registrar of Companies with respect to any association will be conclusive evidence that all the requirements of the Act have been complied with with respect to registration and the matters precedent and incidental thereto, and that the association is a company authorized to be a registered company and is duly registered under the Companies Act. [72]

---

[72] Companies Act, 1956, Sec. 35.

The registration of a company requires the payment of stamp duty, which is levied by the state in which the company is incorporated, and filing fees for documents lodged for registration with the Registrar of Companies.

The filing fees payable to the Registrar of Companies are uniform throughout India (see the Worksheets). The stamp duty varies from state to state.

D. Memorandum of Association

The charter of an Indian company is called the memorandum of association. The memorandum of association must be signed by two or more persons in the case of a private company and seven or more in the case of a public company, [73] and must state the following:

[73] Companies Act, 1956, Sec. 12.

(i) The name of the company, including the words "Private Limited," or "Limited" in the case of a public company;

(ii) The state in which the registered office is to be situated;

(iii) The objects of the company stated as "main," "incidental and ancillary," and "others" separately, and the state or states (except in the case of trading corporations) to which the objects extend; and

(iv) The total amount of the share capital and the par value of the company's shares. [74]

[74] Companies Act, 1956, Sec. 13.

The memorandum of association of a company limited by shares should be in the form specified in Table B, Schedule I of the Companies Act or as near thereto as circumstances permit [75] (see the Worksheets). The memorandum should be printed, divided into paragraphs numbered consecutively and signed by each subscriber in the presence of a witness. [76] The shareholders may alter the memorandum with respect to a change of place of its registered office from one state to another or with respect to the objects of the Company by special resolution, subject to the provisions of the Companies Act, except where the alteration relates to a change of the place of the registered office from one state to another, which requires confirmation by the central government. [77]

[75] Companies Act, 1956, Sec. 14.

[76] Companies Act, 1956, Sec. 15.

[77] Companies Act, 1956, Sec. 17.

A company may change the place of its registered office from one place falling within the jurisdiction of one Registrar of Companies in one state, to another place falling within the jurisdiction of another Registrar of Companies within the same state, with the confirmation of the Regional Director. [78]

[78] Companies Act, 1956, Sec. 17A.

A company may change its name by special resolution and with the approval of the central government. [79]

[79] Companies Act, 1956, Sec. 21.

"Person" includes a company or someone signing on behalf of a company as well as any other person; an agent duly authorized may sign as a subscriber to the memorandum.

The subscribers need not have any personal beneficial interest in the shares subscribed for by them. All of them may be nominees of a single person and signing their names may be merely a formality.

E. Articles of Association

The bylaws of an Indian company are called the articles of association. The articles of association of a company are its Magna Carta. The articles regulate the internal management of the company. They comprise the regulations for the conduct of the affairs of the company. The Companies Act does not specify what the articles must provide, but does specify that certain powers may not be exercised unless authorized by the articles. [80]

[80] Companies Act, 1956, Secs. 80, 92, 93, 94, 100 and 114.

A company may not provide that any of its articles are to remain unaltered, except to the extent provided in the Companies Act or any other law.

Comment: The articles constitute a covenant between the company and its shareholders. A shareholder may restrain the company from acting contrary to the articles, but third parties derive no contractual rights from them.

It is common for a foreign investor and the local partners to enter into shareholders' agreements recording various agreements they have reached relating to the operations of the company. Such agreements are enforceable on the parties thereto but are not binding on the company, though very often the agreements are noted in board of directors' meetings. A foreign investor will derive greater comfort by incorporating such agreements in the articles of association.

A public company limited by shares need not adopt any articles, but if it does not, the regulations contained in Table A, Schedule I (see the Worksheets) will apply to it. [81]

---

[81] Companies Act, 1956, Sec. 28.

A private company is required to include the following regulations:

(i) A restriction on the transfer of its shares;

(ii) A limitation on the number of its members to 50;

(iii) A prohibition against any invitation to or acceptance of deposits from a person other than its members or its directors or their relatives; and

(iv) A prohibition against any invitation to public subscription for its shares or debentures. [82]

---

[82] Companies Act, 1956, Sec. 27(3).

All other companies, not being companies limited by shares, may adopt the appropriate articles set forth in Schedule I. [83]

---

[83] Companies Act, 1956, Sec. 29.

The articles of association should be printed, divided into paragraphs numbered consecutively, signed by each subscriber to the memorandum of association and duly witnessed. [84]

---

[84] Companies Act, 1956, Sec. 30.

The shareholders may alter the articles by special resolution, subject to the provisions of the Companies Act and the conditions contained in the memorandum. An alteration that has the effect of converting a public company into a private company will be effective only after the approval of the alteration by the central government. On approval of such an alteration by the central government, a printed copy of the articles must be filed by the company with the Registrar of Companies within one month of the date of receipt of the order of approval. [85]

---

[85] Companies Act, 1956, Sec. 31.

F. Holding and Subsidiary Company

The Companies Act specifies the circumstances that must exist to constitute the relationship of holding and subsidiary companies.

Company A is a subsidiary of Company B, only if:

(i) Company B (Holding Company) controls the composition of the board of directors of Company A (Subsidiary);

(ii) Company B (Holding Company) holds more than 50% of the equity capital of Company A (Subsidiary) based on nominal value, regardless of the amount paid up on the shares; or

(iii) Company A (Subsidiary) is a subsidiary of Company C, which is a subsidiary of Company B.

Control over the composition of the board of directors of a company means that the holding company has the power,

at its discretion, to appoint or remove all or a majority of the directors of the subsidiary without the consent of any other person.

In case of a body corporate incorporated outside India, a subsidiary or holding company of such body corporate under the law of the country of incorporation will be deemed to be a subsidiary or holding company of the body corporate for purposes of the Act. [86]

[86] Companies Act, 1956, Sec. 4.

G. Shares

1. Kinds of Shares

A company may issue only equity and preference shares. New issues of equity share capital may be of two types: shares with voting rights; and shares with differential rights as to dividends, voting, or other rights. [87] An Indian company may issue redeemable preference shares, provided its articles so authorize, to be redeemed within a period of 20 years. [88] Preference shares may not carry voting rights except where dividends on such shares are in arrears for a certain period of time or when their rights would be affected by a proposed resolution. [89]

[87] Companies Act, 1956, Secs. 85 and 86.

[88] Companies Act, 1956, Sec. 80.

[89] Companies Act, 1956, Sec. 87(2).

2. Payment of Commission

The payment of commission to any person who subscribes or procures subscriptions for shares of a company in specified circumstances is permitted under the Companies Act. [90]

[90] Companies Act, 1956, Sec. 76.

3. Buy-back of Shares

The Companies Act prohibits a company from purchasing its own shares, unless the consequent reduction of capital is effected and sanctioned in pursuance of the provisions of the Act. [91]

[91] Companies Act, 1956, Sec. 77(1).

Notwithstanding the above, a company may purchase its own shares or other specified securities (referred to as a "buy-back") out of:

(i) Its free reserves;

(ii) The securities premium account; or

(iii) The proceeds of any issue of shares or other specified securities provided no buy-back of any kind of shares or other specified securities may be made out of the proceeds of an earlier issue of the same kind of shares or the same kind of other specified securities.

The buy-back of shares is subject to the following conditions being fulfilled:

(i) The buy-back must be authorized by the articles of association of the company;

(ii) A special resolution must have been passed at a general meeting of the company authorizing the buy-back. A special resolution is not required if the buy-back is of less then 10 % of the paid-up capital and reserves and is authorized by the board of directors;

(iii) The buy-back may not exceed 25% of the total paid-up capital and free reserves of the company and in any case the buy-back of equity shares in any financial year may not exceed 25% of the total paid-up equity capital in that financial year;

(iv) The amount of debt owed by the company may not be more than twice its capital and free reserves (or such higher amount of debt as may be prescribed by the central government for a class or classes of companies) after the buy-back;

(v) All the shares or other specified securities to be bought back must be fully paid-up;

(vi) The buy-back of shares or other specified securities listed on any recognized stock exchange must be in accordance with the regulations made by the SEBI in this respect;

(vii) The buy-back of shares or other specified securities other than those specified above in (vi) must be in accordance with such guidelines as may be prescribed; and

(viii) No buy-back is permitted within a period of 365 days from the date of an earlier buy-back offer.

The notice of the meeting at which the special resolution is proposed to be passed must be accompanied by an explanatory statement containing:

(i) A full and complete disclosure of all the material facts;

(ii) The reason why the buy-back is necessary;

(iii) The class of security intended to be purchased under the buy-back;

(iv) The amount to be invested under the buy-back; and

(v) The time limit for completion of the buy-back.

The buy-back must be completed within 12 months from the date of passing of the special resolution. The buy-back may be:

(i) From the existing security holders on a proportionate basis;

(ii) From the open market;

(iii) From odd lots, that is where the lot of securities in a listed public company is smaller than such market lot as may be specified by the stock exchange; or

(iv) By purchase of the securities issued to the employees of the company pursuant to a stock option or sweat equity scheme.

Before making the buy-back, the company must file with the Registrar of Companies and the SEBI a declaration of solvency, verified by an affidavit to the effect that the board of directors has made a full inquiry into the affairs of the company, as a result of which it has formed an opinion that it is capable of meeting its liabilities and will not be rendered insolvent within a period of one year of the date of declaration adopted by the board of directors and signed by at least two directors of the company, one of whom must be the managing director of the company, if there is one. However, no declaration of solvency is required to be filed with the SEBI by a company, the shares of which are not listed on any recognized stock exchange.

The securities bought back must be extinguished and physically destroyed within seven days of the date of completion of the buy-back.

Where a company completes a buy-back of its shares or other specified securities, the company may not make a further issue of the same kind of shares (including an issue of rights shares) or other specified securities within a period of six months, except by way of bonus shares or in the discharge of subsisting obligations such as the conversion of warrants, stock option schemes, sweat equity or the conversion of preference shares or debentures into equity shares.

The company is required to maintain a register of securities bought back, the consideration paid for the securities bought back, the date of cancellation of the securities, the date of the extinguishing and physical destruction of the securities, and such other particulars as may be prescribed.

Within 30 days of completion of the buy-back, the company must file with the Registrar of Companies and the SEBI, a return containing such particulars relating to the buy-back as may be prescribed. However, no return need be filed with the SEBI by a company the shares of which are not listed on any recognized stock exchange.

Note: **For purposes of the section, the term "specified securities" includes employee stock options and such other securities as may be notified by the central government.** [92]

---

[92] **Companies Act, 1956, Sec. 77A.**

A company is not permitted to purchase its own shares or other specified securities, whether directly or indirectly:

(i) Through any subsidiary company, including any of its own subsidiary companies;

(ii) Through any investment company or group of investment companies; or

(iii) If the company has defaulted in repayment of a deposit or interest payable thereon, while any redemption of debentures or preference shares or payment of a dividend to any shareholder or repayment of any term loan or interest payable thereon to any financial institution or bank is subsisting.

Buy-back is prohibited if the company has not complied with the provisions with respect to the filing of annual returns and financial statements or the payment of dividends. [93]

---

[93] Companies Act, 1956, Sec. 77B.

---

4. Issue of Rights Shares

Further issues of a company's authorized but unissued equity capital must be offered to existing shareholders in proportion to shares paid up and held by them on the date of offer. The shares thus obtained are referred to as "rights shares." The shareholders may forego this preemptive right by a special resolution or a general resolution approved by the central government. However, the preemptive right is not available when an issue or allotment of shares is made within two years of the formation of a company or within one year after the first allotment, whichever event occurs earlier. The foregoing provisions do not apply to the issue of shares by private limited companies. [94]

---

[94] Companies Act, 1956, Sec. 81.

---

5. Rights of Preference Shareholders

Preference shareholders have no preemptive rights, even with respect to further issues of preferred shares.

Comment: **Public limited companies may issue cumulative convertible preference shares for financing projects.**

6. Stock Option Scheme for Companies Listed on a Recognized Stock Exchange

The SEBI has issued guidelines with respect to employee stock option schemes (ESOSs) and employee stock purchase schemes (ESPSs). These guidelines are applicable to companies listed on a recognized stock exchange.

An ESOS means a scheme under which a company grants options to its employees. The company has to constitute the Compensation Committee for the administration and superintendence of the scheme. The Committee comprises the board of directors with a majority of independent directors. Such a scheme must be approved by the shareholders of the company before it may be offered to the employees.

Companies granting options to their employees pursuant to an ESOS will have the freedom to determine the grant price.

The Compensation Committee draws up suitable policies and systems to ensure that employees do not violate The Securities and Exchange Board of India (Insider Trading) Regulations, 1992 and The Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to the Securities Market) Regulations, 1995.

There must be a minimum period of one year between the grant of options and the vesting of options. The company has the freedom to specify the lock-in-period for the shares issued pursuant to the exercise of an option.

Options granted to an employee are not transferable to any other person.

An ESPS means a scheme under which a company offers shares to employees as part of a public issue or otherwise.

No ESOS or ESPS may be offered to employees of a company unless the shareholders of the company approve such an action. An ESPS must be approved by the shareholders of a company before it may be offered to the employees. Companies issuing shares to their employees pursuant to an ESPS will have the freedom to determine the issue price.

The SEBI has specified the accounting policies to be followed by companies implementing ESOSs and ESPSs.

The accounting value of options granted during a period or of stocks issued to employees during a period is to be treated as another form of employee compensation in the financial statements of the company relating to that period.

The accounting value of an option granted is equal to the aggregate, over all employee stock options granted during the accounting period, of the fair value of the option. For this purpose:

(i) "Fair value" means the option discount or, if the company so chooses, the value of the option calculated using the Black Scholes formula or some other similar valuation method.

(ii) "Option discount" means the excess of the market price of the share at the date of grant of the option

under an ESOS over the exercise price of the option.

The accounting value as determined above is amortized on a straight-line basis over the vesting period.

The accounting value of shares issued under an ESPS is equal to the aggregate price discount over all the shares under the scheme.

Shares issued under an ESPS must be locked in for a minimum period of one year from the date of allotment.

7. Issue of Shares at a Premium

Shares may be issued at a premium. [95] They may also be issued at a discount, subject to certain conditions and with the approval of the central government. [96]

---

[95] Companies Act, 1956, Sec. 78.

[96] Companies Act, 1956, Sec. 79.

---

8. Issue of "Sweat Equity" Shares

A company may issue "sweat equity" shares of a class of shares already issued, subject to the following conditions:

(i) The issue of sweat equity must be authorized by a resolution passed by the company in a general meeting;

(ii) The resolution must specify the number of shares, their current market price, the consideration to be paid, if any, and the class or classes of directors or employees to whom the equity shares are to be issued;

(iii) As of the date of issue, not less than one year must have elapsed since the date on which the company was entitled to commence business;

(iv) The issue of sweat equity shares of a company, the equity shares of which are listed on a recognized stock exchange, must be in accordance with the regulations adopted by the SEBI in this respect; and

(v) The issue of sweat equity shares of a company, the equity shares of which are not listed on any recognized stock exchange, must be in accordance with prescribed guidelines.

Note 1: **The expression "company" means a company incorporated, formed and registered under the Companies Act and includes a subsidiary company of such a company incorporated in a country outside India.**

Note 2: **The expression "sweat equity shares" means equity shares issued by a company to its employees or directors, at a discount or for consideration other than cash, for providing know-how or making available rights in the nature of intellectual property rights or value additions, by whatever name called.**

The limitations, restrictions and provisions relating to equity shares are also applicable to sweat equity shares. [97]

---

[97] Companies Act, 1956, Sec. 79A.

---

9. Other General Provisions

A company may issue shares as partly paid-up shares. The usual pattern is payment of 25% with the application and another 25% on allotment, with the remaining 50% payable on a maximum of two calls, as and when the company needs the capital.

In the case of a private company that is not a subsidiary of a public company, there is no restriction on the kind of shares that may be issued nor is there any restriction on voting rights. [98]

---

[98] Companies Act, 1956, Sec. 90(2).

An alteration of capital may be made by an ordinary resolution if the articles so authorize. This will entail altering the conditions of the memorandum. An alteration of capital means that a company may increase, consolidate and divide, convert, sub-divide or cancel its shares but is not considered a reduction of share capital. [99] A reduction of capital may be made by special resolution if the articles so authorize and the National Company Law Tribunal (NCLT) confirms the reduction. By means of a reduction of capital, a company may:

---

[99] Companies Act, 1956, Sec. 94.

(i) Extinguish or reduce the liability on any of its shares with respect to share capital not paid up;

(ii) Either with or without extinguishing or reducing liability on any of its shares, cancel any paid-up share capital that is lost or is not represented by available assets;

(iii) Either with or without extinguishing or reducing liability on any of its shares, pay off any paid-up capital that is in excess of the requirements of the company. [100]

---

[100] Companies Act, 1956, Sec. 100.

H. Debentures

In addition to ordinary and preference shares, a company may issue debentures. Debentures include debenture stock, bonds and other securities of a company, whether or not constituting a charge on the assets of a company. [101]

---

[101] Companies Act, 1956, Sec. 2(12).

The right of preemption does not apply to a public company if the subscribed capital is increased owing to the exercise of an option attached to debentures issued by the company to convert such debentures into shares, provided the conversion is in conformity with rules specified by the central government and approved by a special resolution of the company before the issue of the debentures. [102]

---

[102] Companies Act, 1956, Sec. 81(3)(b)(i).

A debenture issued to the central government or any of its finance agencies may be converted by the central government into shares of the company, even if the debenture is not so convertible under its terms, "if in the opinion of the Central Government it is necessary to do so in the public interest." [103] A conversion order to that effect must be laid before Parliament for 30 days before issue. The company may appeal to the High Court for reversal of the order if its terms and conditions are not acceptable to the company. [104]

---

[103] Companies Act, 1956, Sec. 81(4)(5).

[104] Companies Act, 1956, Sec. 81(6)(7).

Public limited companies may issue secured convertible or nonconvertible debentures in accordance with the guidelines issued by the SEBI. Such companies are, however, not permitted to issue bearer debentures.

Nonconvertible debentures are generally redeemed during the seventh, eighth and ninth years from the date of issue.

A company may not issue debentures carrying voting rights at any meeting of the company, whether generally or with respect to particular classes of business. [105]

---

[105] Companies Act, 1956, Sec. 117.

A trust deed for securing any issue of debentures must be in the prescribed form and must be executed within the prescribed period. [106]

---

[106] Companies Act, 1956, Sec. 117A.

A company may not issue a prospectus or letter of offer to the public for subscription of its debentures unless the company has, before such issue, appointed one or more debenture trustees, subject to certain conditions, for such debentures and the company has, on the face of the prospectus or the letter of offer, stated that the debenture trustee or trustees have given their consent to the company to be so appointed. The functions of the debenture trustees are generally to protect the interests of the debenture holders (including the creation of securities within the stipulated time) and to redress their grievances effectively. [107]

---

[107] Companies Act, 1956, Sec. 117B.

A company issuing debentures must create a debenture redemption reserve for the redemption of the debentures, to

which adequate amounts must be credited from its profits each year, until the debentures are redeemed. The amounts credited to the debenture redemption reserve account may not be utilized by the company except for this purpose. The company must pay interest and redeem the debentures in accordance with the terms and conditions of their issue. [108]

[108] Companies Act, 1956, Sec. 117C.

I. Public Offering/Foreign Borrowing

1. Public Offering in India

The regulation of public issues of shares and debentures in India derives from:

(i) The Companies Act, which prescribes, among other things, the disclosure requirements for a prospectus; and

(ii) The guidelines issued by the SEBI for investor protection.

The raising of capital by subscription must be pursuant to a prospectus complying with the provisions of the Companies Act. In terms of the Contract Act, 1859, a prospectus is an "Invitation to Offer." To minimize the risks of investment and to be able to make informed decisions, investors must have detailed knowledge of the company in which they are investing. Because of the prevalence of unreliable promises of attractive returns on investment and the unscrupulous dissemination of false and misleading information, it is necessary for all relevant and material information to be provided to prospective investors. For this reason, the Companies Act contains elaborate provisions with respect to prospectuses.

"Prospectus" is defined in the Companies Act to mean "any document described or issued as a prospectus including any notice, circular, advertisement or other document inviting deposits from the public or inviting offers from the public for the subscription or purchase of any shares in, or debentures of, a body corporate." [109] Every prospectus must have a publication date. [110] The matters to be specified and reports to be drawn up in the prospectus are specified in Schedule II to the Act. [111] This schedule contains three parts: Part I contains information to be provided; Part II contains reports to be drawn up; and Part III gives explanations about the requirements of the contents of Parts I and II. A prospectus must be registered with the Registrar of Companies before publication, must be signed by every director or proposed director, and must be issued within 90 days after the date on which it is registered with the Registrar of Companies. [112]

[109] Companies Act, 1956, Sec. 2(36).

[110] Companies Act, 1956, Sec. 55.

[111] Companies Act, 1956, Sec. 56.

[112] Companies Act, 1956, Sec. 60.

A public company making an issue of securities is required to circulate an information memorandum to the public before filing a prospectus. This procedure is useful when the issuing company wishes to test the market before finalizing the issue size and/or issue price. The information memorandum should indicate the price band as well as the issue size band. "Information memorandum" means a process undertaken prior to the filing of a prospectus by means of which a demand for the securities proposed to be issued by a company is elicited, and the price and terms of issue of such securities is assessed, by means of a notice, circular, advertisement or document. [113] A company inviting subscription by way of an information memorandum is bound to file a prospectus prior to the opening of the subscriptions lists and the offer as a "red-herring prospectus," at least three days before the opening of the offer. The information memorandum and the red-herring prospectus carry the same obligations as apply in the case of a prospectus.

[113] Companies Act, 1956, Sec. 2(19B).

The issuing company must highlight any variations between the information memorandum and the red-herring prospectus as variations. For these purposes, a "red-herring prospectus" means a prospectus that does not have complete particulars on the price of the securities offered and the quantum of securities offered. On the closing of the offer of securities, a final prospectus stating the total capital raised, whether by way of debt or share capital, and the

closing price of the securities, and any other details that were not complete in the red-herring prospectus must be filed, in the case of a listed company, with the SEBI and, in any other case, with the Registrar of Companies. [114]

[114] Companies Act, 1956, Sec. 60B.

Every listed public company, making an initial public offer of any security for a sum of Rs.100 million (approximately US$ 2 million) or more, must issue the security, only in dematerialized form, in compliance with the requisite provisions of the Depositories Act, 1996 and the regulations adopted thereunder [115] (see Z, below).

[115] Companies Act, 1956, Sec. 68B.

There are severe criminal and civil liabilities for mistakes or false statements made in the prospectus. [116] In addition, if a mistake or false statement is made, a subscriber may rescind the contract for the shares or debentures.

[116] Companies Act, 1956, Secs. 62, 63 and 68.

Share capital offered to the public for subscription must not be allotted unless the minimum subscription, as mentioned in the prospectus, is received by the company within 120 days after the first issue of the prospectus. [117]

[117] Companies Act, 1956, Sec. 69.

The central government requires that the allotment of shares in cases of over-subscription of public issues should be made in such a manner that the interests of small investors are promoted and the widest possible dispersal of the shareholding takes place.

The subscription list should be kept open for at least three days in the case of a public company opting to list its shares on a recognized stock exchange. The maximum period for keeping open the subscription lists of such companies is 21 days, where the issue is underwritten by a public financial institution, and 10 days in all other cases.

Where a company having share capital does not issue a prospectus inviting the public to subscribe for shares or debentures, the company must file with the Registrar of Companies a statement in lieu of a prospectus, as specified in Schedule II to the Companies Act at least three days before the first allotment of the shares or debentures. [118]

[118] Companies Act, 1956, Sec. 70.

When a prospectus is issued, an allotment may not be made until the beginning of the fifth day after the date on which the prospectus was first issued or such later time as may be specified in the prospectus. [119]

[119] Companies Act, 1956, Sec. 72.

Every public company is required, before issuing shares or debentures for public subscription by issue of a prospectus, to make an application to list the securities on one or more recognized stock exchanges. If permission is not granted by any stock exchange before the expiration of 10 weeks from the date of closing of the subscription list, no allotment may be made. If no application is made, or permission is not granted, the company must refund all money received from applicants within eight days, failing which the company and its directors may be liable to penal provisions, as applicable. [120]

[120] Companies Act, 1956, Sec. 73.

It is mandatory for a company offering shares to the public for subscription to make certain of obtaining the necessary capital by having the issue underwritten. The conditions for the payment of commission for underwriting an issue are:

(i) Payment must be authorized by the articles of the company;

(ii) The amount of the payment must not exceed 5% of the issue price in the case of shares or 2.5% of the issue price in the case of debentures;

(iii) The amount or rate per cent of commission must be disclosed in the prospectus, and the number of shares or debentures to which persons have agreed to subscribe, whether absolutely or conditionally, must be stated; and

(iv) A copy of the contract relating to the payment of the commission must be delivered to the Registrar of Companies.

No commission is to be paid to any person for shares or debentures that are not offered to the public for subscription.[121]

---

[121] Companies Act, 1956, Sec. 76.

Pursuant to the powers conferred on it, the SEBI has issued guidelines to ensure proper disclosure and investor protection. These guidelines must be observed by companies making public offerings. Additionally, the SEBI requires all listed companies to comply with the following conditions/meet following requirements:

(i) Enter into a listing agreement with the stock exchanges concerned. An important provision of such an agreement is Clause 49, which deals with the following matters:

- **The independence of the Board of Directors;**
- **The composition and role of the Audit Committee; and**
- **Regulations and guidelines with regard to maintaining financial reporting and transparency in relation thereto, including the certification of the audited financial statements and cash flow statement by the Chief Executive Officer and the Chief Financial Officer, a statement of the application of funds raised, the criteria for payments to nonexecutive directors, etc.**

(ii) Publish quarterly/half yearly financial results accompanied by a limited review report by the statutory auditors.

2. Public Offering Overseas

Under the Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993, Indian companies are allowed to raise capital in convertible foreign exchange by issuing either global depository receipts (GDRs) or foreign currency convertible bonds (FCCBs).

An Indian company may sponsor an issue of GDRs or American Depository Receipts (ADRs) with an overseas depository against shares held by its shareholders at a price to be determined by the lead manager with respect to divestment by shareholders of their holdings in Indian companies listed in India or divestment by shareholders of their holdings in Indian companies listed overseas. Unlisted Indian companies issuing GDRs/FCCBs will be required to list their shares simultaneously on Indian stock exchanges.

An issuing company requires the prior permission of the Department of Economic Affairs, Ministry of Finance, Government of India for raising funds overseas by issue of GDRs/FCCBs.

GDRs may be issued for one or more underlying shares or bonds in negotiable form and may be listed on any international stock exchange or over the counter exchange for trading outside India. GDRs are freely transferable.

On issuing ordinary shares or bonds under this scheme, a company is required to deliver the ordinary shares or bonds to a domestic custodian bank, which will, in terms of an agreement, instruct an overseas depository bank to issue GDRs or certificates to nonresident investors against the shares or bonds held by the domestic custodian bank.

The ordinary shares and FCCBs issued against the GDRs are treated as direct foreign investment in the issuing company. The aggregate of foreign investment made either directly or indirectly (through the GDR mechanism) may not exceed 51% of the issued and subscribed capital of the issuing company. This limit does not apply to investments made through offshore funds or Foreign Institutional Investors (FIIs). FCCBs and GDRs may be denominated in any freely convertible foreign currency. The ordinary shares underlying the GDRs and the shares issued on the conversion of the FCCBs will be denominated only in Indian currency. Neither the conversion of FCCBs into shares nor the transfer of FCCBs made outside India by one person to another gives rise to any capital gains tax liability in India.

Both GDRs and FCCBs are exempt from wealth tax under the Wealth Tax Act, 1957. During the period of fiduciary ownership of shares in the hands of an overseas depository bank, the provisions of the double taxation agreement entered into by the government of India with the country of residence of the overseas depository bank will apply as regards the taxation of income from dividends on underlying shares and dividends and interest on FCCBs.

Dividends on GDRs and dividends and interest on FCCBs attract concessional tax rates of 10% (see VI, E, 1, below). Capital gains arising on the transfer of GDRs/FCCBs in India also attract a concessional tax rate of 10% (again, see VI, E, 6, below).

Indian companies may make overseas public offerings of equity and related instruments in accordance with the guidelines issued by the central government in this regard. These guidelines are reviewed periodically.

3. External Commercial Borrowings

Indian companies may raise External Commercial Borrowings (ECBs) in accordance with the guidelines issued by the RBI in this regard (see the Worksheets). ECBs are commercial loans in the form of bank loans, buyers' credit, suppliers' credit, and securitized instruments obtained from nonresident lenders.

FCCBs and foreign currency exchangeable bonds (FCEBs) are bonds issued by an Indian company expressed in foreign currency with the principal and interest payable in foreign currency. The policy for ECBs is also applicable to FCCBs and FCEBs.

ECBs may be accessed under two routes:

(i) The Automatic Route; and

(ii) The Approval Route.

The guidelines cover a number of areas, the most significant of which are the following:

(i) Eligibility;

(ii) Recognized lenders;

(iii) Amounts that may be raised and maturity;

(iv) All in cost ceilings;

(v) End use and restrictions on end use;

(vi) Prepayment;

(vii) Refinancing; and

(viii) Debt servicing.

J. Transfers of Shares and Debentures

An essential condition for registering a transfer of shares or debentures is that a duly stamped and executed instrument should be delivered to the company within the prescribed period, accompanied by the certificate or letter of allotment relating to the shares or debentures. [122] This provision does not apply in the case of transfers by operation of law. The company, at its discretion, may require proof of transfer and may include in its articles a procedure relating to the recognition of transfers.

---

[122] Companies Act, 1956, Sec. 108.

A transfer executed by the legal representative of a deceased shareholder is valid as if executed by the shareholder him or herself. [123]

---

[123] Companies Act, 1956, Sec. 109.

Every holder of shares in, or debentures of, a company may at any time nominate a person to whom the person's shares or debentures are to vest in the event of his or her death. Where more than one person holds the shares in, or debentures of, a company jointly, the joint holders may together nominate a person to whom all the rights in the shares or debentures of the company are to vest in the event of the death of all the joint holders. [124]

---

[124] Companies Act, 1956, Sec. 109A.

An application for the registration of a transfer of shares in a company may be made either by the transferor or by the transferee. In the case of partly paid-up shares, the transfer may not be registered unless notice by registered mail is given to the transferee and the transferee does not object within two weeks. [125]

---

[125] Companies Act, 1956, Sec. 110.

Private companies are free to enforce any restrictions contained in their articles of association against the right to transfer shares. A company that refuses to register the transfer or transmission of any share or debenture must, within two months of the lodgment of the instrument of transfer or notice of transmission, send notice of the refusal, giving reasons for the refusal. In cases of refusal or failure to register, or undue delay in registering, a transfer or transmission by a company, an appeal lies to the NCLT. The Board, by an order in writing, either directs the registration of the transfer or transmission, or confirms the refusal and, in the former case, may direct the company concerned to pay damages to the aggrieved party. [126]

---

[126] Companies Act, 1956, Sec. 111.

The shares or debentures, or any interest therein, of a public company are freely transferable. The NCLT may, on an application made to it, and after making such enquiries as it thinks fit, direct that the register of members or records be rectified if a transfer of shares or debentures is in contravention of any of the provisions of the Securities and Exchange Board of India Act, 1992 or regulations issued thereunder. The application to the Company Law Board may be made by a depository company or an investor, or the SEBI within two months of the date of the transfer of any shares or debentures held by a depository or from the date on which the instrument of transfer or intimation of transmission was delivered to the company. The NCLT may, at its discretion, make an interim order to suspend the voting rights pending an inquiry. There are no restrictions on the right of a holder of shares or debentures to transfer such shares or debentures and the person acquiring the shares or debentures is entitled to voting rights unless the voting rights have been suspended by the NCLT. [127]

---

[127] Companies Act, 1956, Sec. 111A.

K. Registration of Charges

Corporate borrowing requires loans to be raised from various sources to which assets are charged as security (i.e., assets are mortgaged or hypothecated as security). The concept of a floating charge is recognized, whereby the same assets are charged to several lenders and also to several lenders in a series. The Companies Act prescribes the registration of charges with the Registrar of Companies. This registration operates as a constructive notice, to all persons, of the charges existing on the assets of a company.

The registration prescribed by the Companies Act is achieved by filing the necessary particulars with the Registrar of Companies within 30 days after the date on which the charge is created. The charge becomes void against the liquidator or creditors if it is not registered within the prescribed time. The Registrar of Companies may permit a further 30 days if the company satisfies the Registrar of Companies that it had sufficient cause for not filing the necessary particulars. [128]

---

[128] Companies Act, 1956, Sec. 125.

The following charges are required to be registered:

(i) A charge for securing any issue of debentures;

(ii) A charge on uncalled share capital of a company;

(iii) A charge on any real property, wherever situated, or any interest therein;

(iv) A charge on any book debts of a company;

(v) A charge on any movable property of a company (not being a pledge);

(vi) A floating charge on the undertaking or any property of a company, including stock-in-trade (inventory);

(vii) A charge on calls made but not paid;

(viii) A charge on a ship or any share in a ship; and

(ix) A charge on goodwill, on a patent or a license under a patent, on a trademark, or on a copyright or a license under a copyright.

In the case of a charge created out of India, and comprising solely property outside India, the instrument creating or evidencing the charge, or a copy thereof, must be received in India within 30 days from the date of creation of the instrument in due course of post and if dispatched with due diligence. [129]

[129] Companies Act, 1956, Sec. 125(5).

Where a charge created in India comprises property outside India, the instrument creating or purporting to create the charge, or a copy thereof, may be filed for registration notwithstanding the fact that further proceedings may be necessary to make the charge valid or effectual according to the law of the country in which the property is situated. [130]

[130] Companies Act, 1956, Sec. 125(6).

The Registrar of Companies issues a certificate of registration of any charge registered, specifying the amounts secured, which is conclusive evidence that registration has been completed. [131] Whenever a company satisfies a charge on its assets, the Registrar of Companies issues a memorandum of satisfaction, on an application being made. [132]

[131] Companies Act, 1956, Sec. 132.

[132] Companies Act, 1956, Secs. 138, 139 and 140.

A register of charges must be maintained by a company at its registered office wherein all charges specifically affecting property of the company must be entered, giving in each case a short description of the property charged, the amount of the charge, and the names of the persons entitled to the charge. [133]

[133] Companies Act, 1956, Sec. 143.

The central government, on an application being made to it by the company or any interested person, and in specified circumstances, may rectify omissions or misstatements in the register of charges and also extend the time for filing the particulars of charges beyond the time permitted (which is 30 days plus a 30-day extension for sufficient cause). [134]

[134] Companies Act, 1956, Sec. 141.

L. Registered Office

A company will have a registered office from the day on which it begins to carry on business or within 30 days of its incorporation, whichever is earlier.

A notice of the situation of the registered office or any change therein is to be given to the Registrar of Companies within 30 days of the change. However, a change of the registered office outside the local limits of any city, town or village where the office is situated will require the authority of a special resolution passed by the Company. [135]

[135] Companies Act, 1956, Sec. 146.

The name and address of the registered office must be painted on or affixed to the outside of every office or place in which its business is carried by the company and on official stationery and publications of the company. [136]

[136] Companies Act, 1956, Sec. 147.

M. Commencement of Business

A private company is permitted, under the Companies Act, to commence business and exercise borrowing powers on being granted a certificate of incorporation. However, a public company limited by shares that has issued a prospectus inviting the public to subscribe for its shares may neither commence business nor exercise any borrowing powers unless:

(i) Shares held subject to the payment of the whole amount thereof in cash have been allotted to an amount not less in the whole than the minimum subscription;

(ii) Every director of the company has paid to the company, on each of the shares taken or contracted to be taken by him or her and for which he or she is liable to pay in cash, a proportion equal to the proportion payable on application and allotment on the shares offered for public subscription;

(iii) No money is, or may become, liable to be repaid to applicants for any shares or debentures that have been offered for public subscription by reason of any failure to apply for, or to obtain permission for, the shares or debentures to be dealt in on any recognized stock exchange; and

(iv) A duly verified declaration has been filed with the Registrar of Companies by one of the directors or the secretary or, where the company has not appointed a secretary, a secretary in full-time practice, that clauses (i), (ii), and (iii) have been complied with.

A company that has not issued a prospectus inviting the public to subscribe to its shares may not commence any business or exercise any borrowing powers unless:

(i) A statement in lieu of a prospectus has been filed with the Registrar of Companies;

(ii) Every director of the company has paid to the company, on each of the shares taken or contracted to be taken by him or her and for which he or she is liable to pay in cash, a proportion equal to the proportion payable on application and allotment on the shares payable in cash; and

(iii) A duly verified declaration has been filed with the Registrar of Companies by one of the directors or the secretary or, where the company has not appointed a secretary, a secretary in full-time practice, that clauses (i) and (ii) have been complied with.

On the filing of the duly verified declaration, the Registrar of Companies will certify that the company is entitled to commence business. The certificate to commence business is issued by the Registrar of Companies on receipt of a declaration by one of the directors stating that the conditions specified in the Companies Act have been complied with.

Any contract made by a company before the date of commencement of business will be provisional only and will not be binding on the company until that date. It will become binding on the date on which the company is entitled to commence business. [137]

---

[137] Companies Act, 1956, Sec. 149.

N. Shareholders' Meetings

The Companies Act is specific on the regularity and formality of company meetings so that shareholders have full control of the affairs of the company. [138] Three types of meeting are prescribed under the Act where the voting may be by proxy:

---

[138] Companies Act, 1956, Secs. 165–197.

(i) The statutory meeting;

(ii) Annual general meetings; and

(iii) Extraordinary meetings.

A statutory meeting is to be held, only by a public company limited by shares, within a period not earlier than one month and not later than six months from the date on which the company is entitled to commence business. The board of directors is required to forward a statutory report to all the members of the company at least 21 days before the day of the statutory meeting. The statutory report must set out the particulars specified in the Companies Act. [139]

---

[139] Companies Act, 1956, Sec. 165.

In addition to any other meetings, a company is required to hold a general meeting as its annual general meeting during business hours on a day that is not a public holiday and in the city, town, or village where the registered office of the company is situated. The first annual general meeting is required to be held within 18 months of a company's incorporation. Subsequent meetings must be held within 15 months of the previous meeting and one such meeting must be held each year. [140]

---

[140] Companies Act, 1956, Sec. 166.

Any meeting convened by the board of directors besides the annual general meeting and the statutory meeting is termed an extraordinary general meeting.

In an annual general meeting, all the business transacted is termed special business, with the exception of the following:

(i) The consideration of the accounts, the balance sheet, and the reports of the board of directors and the auditors;

(ii) The declaration of a dividend;

(iii) The appointment of new directors in place of retiring directors; and

(iv) The appointment of auditors and the fixing of remuneration.

In the case of any other meeting, all the business transacted is termed special business. Whenever special business is to be transacted, an explanatory statement setting out the material facts concerning each such item of business, including the nature of any concern or interest of any director in each of the proposed resolutions, is required to be annexed to the notice convening the meeting. In the case of a resolution relating to another company, the shareholding interest of each director in the other company should be disclosed, where such shareholding interest in the other company is 20% or more. [141]

---

[141] Companies Act, 1956, Sec. 173.

Five members of a public company personally present and two members of any other company personally present constitute the quorum for a meeting, unless the articles of the company specify a larger number. [142]

---

[142] Companies Act, 1956, Sec. 174.

Two types of resolution are permitted by the Companies Act. An ordinary resolution requires a simple majority vote of those present in person or voting by proxy. A special resolution requires a majority of three-fourths of the members voting in person or by proxy. [143]

---

[143] Companies Act, 1956, Sec. 189.

A special resolution is required for transacting business only where it is specifically required by the Companies Act or by the company's articles. All other business may be transacted by an ordinary resolution.

Comment: **The purpose of a special resolution is to protect the interests of minority shareholders with regard to important company matters. The special resolution of Indian company law is generally comforting to foreign investors who are in a minority equity position. In this connection, it is advisable for a foreign investor to hold at least 26% of the equity shares.**

A special resolution is required under the Act for such important matters as the following:

(i) Altering the provisions of the memorandum with respect to:

- **The objects of the company;**
- **Changing the place of the registered office from one state to another;**
- **Commencing any new line of business;**
- **Changing the name of the company (which also requires the approval of the central government);**
- **Omitting the word or words "Limited" or 'Private Limited" from the name of the company; or**
- **Changing the name of a charitable or other nonprofit company by omitting the word or words "Limited" or "Private Limited";**

(ii) Altering or adding to the articles;

(iii) Purchasing the company's own shares or specified securities;

(iv) Issuing sweat equity shares;

(v) Issuing further shares without preemptive rights to nonmembers or converting loans or debentures into shares;

(vi) Determining that any portion of the share capital not already called up should not be called up except in the event of, and for purposes of, winding up the company;

(vii) Reducing the share capital (this should be permitted by the articles and confirmed by the court);

(viii) Approving a variation in the rights of special classes of shares;

(ix) Removing the registered office of the company outside the local limits of the state, town or village in which it is situated;

(x) Keeping registers and returns at any place other than within the city, town or village in which the registered office is situated;

(xi) Authorizing the payment of interest on the paid-up amount of share capital raised to defray the expenses of constructing any work or building or the purchase of any machinery that may not be made profitable for a lengthy period;

(xii) Asking the government to investigate the affairs of the company and to appoint inspectors for the purpose;

(xiii) Fixing the remuneration of directors, where the articles require such resolution;

(xiv) Sanctioning the remuneration of directors other than managing or full-time directors on a percentage-of-profit basis, in certain instances, and renewing such sanction;

(xv) Consenting to a director or his relative, a partner, a firm or a private company holding an office or profit-making position, except that of managing director, manager, banker, or trustee for debenture holders of the company;

(xvi) Making the liability of any director or manager unlimited where this is authorized by the articles;

(xvii) Appointing auditors in the case of a company in which the central and/or any state government, and/or public financial institution or institutions, together hold 25% or more of its subscribed capital;

(xviii) Appointing the sole selling or buying or purchasing agent of a company having paid-up share capital of Rs.5 million or more;

(xix) Making intercorporate loans and investments or providing guarantees if the aggregate amount thereof exceeds the limit of 60% of the company's paid-up share capital and free reserves or 100% of its free reserves, whichever is more;

(xx) Applying to a court to wind up the company;

(xxi) Winding up the company voluntarily;

(xxii) Binding the company by an arrangement;

(xxiii) Deciding other matters pertaining to the winding-up of the company; or

(xxiv) Altering the constitution of a company registered under Part IX of the Companies Act.

A listed public company *may* and, in the case of resolutions relating to such business as the central government may, by notification, declare to be conducted only by postal ballot, *must* get any resolution passed by means of a postal ballot, instead of transacting the business in a general meeting of the company. A company that decides to pass any resolution by resorting to a postal ballot must send a notice to all the shareholders along with a draft resolution explaining the reasons therefor, and requesting them to send their assent or dissent in writing on a postal ballot within a period of 30 days from the date of the posting of the letter. A resolution assented to by a requisite majority of the shareholders by means of a postal ballot is deemed to have been duly passed at a general meeting convened for that purpose. In this context "postal ballot" includes voting by electronic means. [144]

---

[144] **Companies Act, 1956, Sec. 192A.**

O. Dividends

Dividends may be declared or paid for any financial year only out of profits of the company for that year, after providing for depreciation and the transfer to reserves of a percentage of the company's profits for that year. The percentage is not to exceed 10%, as prescribed under the Companies (Transfer of Profits to Reserves) Rules, 1975. A transfer to reserves of a higher percentage may be made voluntarily in accordance with rules set by the central government. [145]

---

[145] **Companies Act, 1956, Sec. 205.**

If, in a particular year, there are no profits or profits are inadequate and the company nonetheless proposes to declare a dividend out of the accumulated profits earned by the company in previous years and transferred to reserves, the declaration must be made in accordance with the Companies (Declaration of Dividend out of Reserves) Rules, 1975. [146]

---

[146] **Companies Act, 1956, Sec. 205A.**

Depreciation may be computed at the rates specified in Schedule XIV to the Companies Act (see the Worksheets) or on any other basis approved by the central government.

The board may declare an interim dividend, provided the articles of the company authorize such a declaration.

The amount of the dividend and the interim dividend must be deposited in a separate bank account within five days from the date of declaration of the dividend. The amount so deposited may be utilized only for purposes of paying the dividend.

A dividend, including an interim dividend, must be paid within 30 days from the date of declaration to the shareholders entitled to payment of the dividend. [147] There are stringent penalties for failure to distribute dividends within 30 days. [148]

---

[147] **Companies Act, 1956, Sec. 207.**

[148] **Companies Act, 1956, Sec. 207.**

Where a dividend has been declared by a company but has not been paid to or claimed by any shareholder entitled to payment of the dividend within 30 days from the date of declaration, the company must, within seven days from the expiry of the 30-day period, transfer the total amount to a special account (an "unpaid dividend account") to be opened by the company for that purpose in any scheduled bank. [149]

---

[149] **Companies Act, 1956, Sec. 205-A(1).**

Any amount transferred to the unpaid dividend account of a company that remains unpaid or unclaimed for a period of seven years from the date of transfer must be transferred by a company to the "Investor Education and Protection Fund." [150]

---

[150] **Companies Act, 1956, Secs. 205-A(5) and 205 – C(1).**

The issue of bonus shares (stock dividends) is governed by the guidelines issued by the SEBI.

P. Audit and Accounts

Books of account are required to be kept by a company at its registered office or such other place in India as the board of directors may decide. Books of account relating to transactions effected at a branch office are to be kept at the branch and quarterly returns forwarded to the registered office or such other place in India as the board may decide. [151] Books are to be maintained on the accrual basis and in accordance with the double entry system of accounting and must give a true and fair view of the state of affairs of the company or branch. Books and vouchers must be preserved for a period of eight years. [152]

---

[151] Companies Act, 1956, Sec. 209.

[152] Companies Act, 1956, Sec. 209.

The board of directors is required to present to the shareholders before every annual meeting an audited profit and loss statement and balance sheet. [153]

---

[153] Companies Act, 1956, Sec. 210.

Every balance sheet and profit and loss account must be in the form set out in Part I and Part II of Schedule VI to the Companies Act. Further, every balance sheet and profit and loss account must comply with the accounting standards issued by the Institute of Chartered Accountants of India. Where the balance sheet and profit and loss account of the company do not comply with the accounting standards, the company must disclose in its balance sheet and profit and loss account, the following:

(i) The deviation from the accounting standards;

(ii) The reasons for the deviation; and

(iii) The financial effect, if any, resulting from the deviation.

"Accounting standards" means the standards of accounting recommended by the Institute of Chartered Accountants of India (ICAI) that may be prescribed by the central government in consultation with the National Advisory Committee on Accounting Standards duly constituted for this purpose (see the Worksheets). [154]

---

[154] Companies Act, 1956, Sec. 211.

The auditor is required to make a report to the members (shareholders) of the company on the accounts, the balance sheet and profit and loss account, and on every other document under the Companies Act that is required to be annexed to the balance sheet or profit and loss account, and that is laid before the annual general meeting. The report must state, *inter alia*, whether in the opinion of the auditor the accounts give a true and fair view of the state of affairs of the company, as reflected by the balance sheet, and the profit or loss, as reflected by the profit and loss account. The central government may, by special or general order, direct that in the case of such class or description of companies as may be specified in the order, the auditor's report must include additional statements (see the Worksheets). [155]

---

[155] Companies Act, 1956, Sec. 227.

The balance sheet and profit and loss account must be filed with the Registrar of Companies within 30 days of the annual general meeting before which these were laid. [156]

---

[156] Companies Act, 1956, Sec. 220.

An annual return must be filed with the Registrar of Companies by every company within 60 days of the annual general meeting. [157]

---

[157] Companies Act, 1956, Sec. 159.

Every company that is not required by law to employ a full-time company secretary and having a paid-up capital in excess of Rs.1 million but less than Rs.20 million is required to obtain a Secretarial Compliance Certificate from a secretary in full-time practice certifying compliance with prescribed requirements under the Companies Act. This certificate must be attached to the report of the board of directors tabled before the annual general meeting, and must be filed with the Registrar of Companies within 30 days of the meeting. [158]

[158] Companies Act, 1956, Sec. 383A.

An auditor is appointed at the annual general meeting to hold office from the conclusion of that meeting until the conclusion of the next annual general meeting. Auditors must be independent. They may not be officers of the company.

The first auditors of a company must be appointed by the board of directors within one month of the date of incorporation of the company. [159]

[159] Companies Act, 1956, Sec. 224.

Q. Directors

The Companies Act places great emphasis on the powers and responsibilities of directors. The provisions contained in the Act are intended to empower directors to exercise effective, active and continuous control of the company's affairs. At the same time, the Act imposes restrictions on directors to curb such abuses as interlocking directorates, self-interest and the like.

Only individuals may be directors. [160] The Companies Act imposes no restrictions on the nationality of directors. A director is not required to be a shareholder.

[160] Companies Act, 1956, Sec. 253.

Directors in all listed, unlisted and private corporates must obtain a director identification number (DIN). A director who does not have a DIN will not be recognized and his companies will be unable to file documents online with the Registrar of Companies of the respective States and Union Territory.

Each private company must have at least two directors and each public company at least three directors. A public company with: (i) a paid up capital of Rs.50 million or more; and (ii) 1,000 or more small shareholders, may have directors elected by small shareholders. For this purpose, "small shareholder" means a shareholder holding shares with a nominal value of Rs.20,000 or less in a public company. The articles usually prescribe the minimum and maximum number of directors and the names of the initial directors. At least two-thirds of the directors must be subject to retirement by rotation, but are eligible to be reappointed. One-third of the directors subject to retirement must be elected at each annual meeting of the company. A managing director is not liable to retire by rotation. The one-third not subject to retirement may be appointed on such terms and basis as the articles provide.

Note: **Foreign investors are usually granted the right in the articles to nominate one or more directors depending generally on the extent of their equity participation. Government finance agencies that have lent large sums of money to companies are given the right to designate one or two directors as nonexecutive nominee directors.**

The board of directors has the power to appoint additional directors or to fill in casual vacancies among directors, subject to the articles of the company. Additional directors hold office up to the date of the next annual general meeting of the company. [161] A director appointed to fill a casual vacancy holds office until the date the director in whose place he or she is appointed would have held office. [162]

[161] Companies Act, 1956, Sec. 260.

[162] Companies Act, 1956, Sec. 262.

If its articles so authorize, or by shareholder approval, a company may appoint alternate directors to act in place of an original director who is expected to be out of the state in which the meetings of the directors are ordinarily held for a period exceeding three months. [163]

[163] Companies Act, 1956, Sec. 313.

The Companies Act also authorizes Indian companies to elect directors on the principle of proportional representation. [164] If such a practice is adopted by the articles, it must apply to at least two-thirds of the board and there must be an election every three years of those directors subject to proportional representation election. The other one-third of the board may be appointed as prescribed by the articles.

---

[164] Companies Act, 1956, Sec. 265.

The company may appoint either a managing director or a manager, but not both. The managing director or manager has to work under the overall supervision and control of the board of directors. [165] A managing director is a full-time director with such powers of management of the company's affairs as are delegated to or conferred on him or her by the memorandum or articles, or by an agreement or resolution of the board, or by the company in general meeting. The Act prohibits the appointment of undesirable persons as managing or full-time directors of companies. [166]

---

[165] Companies Act, 1956, Sec. 197A.

[166] Companies Act, 1956, Sec. 267.

Every public company and every private company that is a subsidiary of a public company and has paid-up share capital of Rs.50 million or more must have a managing or full-time director, or a manager. [167] The decision as to whether a managing director, full-time director or manager is appointed is at the discretion of the board of directors.

---

[167] Companies Act, 1956, Sec. 269(1).

The appointment of a managing or a full-time director, or a manager must be made in accordance with the conditions specified in Schedule XIII to the Companies Act [168] (see the Worksheets). If the specified conditions are not met, the appointment must be made with the approval of the central government. This provision does not apply to a private company.

---

[168] Companies Act, 1956, Sec. 269(2).

A managing director may be the managing director of not more than two companies, where at least one of the two companies is a public company or a private company that is a subsidiary of a public company. A full-time director, being a full-time employee, may not be a full-time director of more than one company. [169] A director's term of office may not exceed five years at a time. [170] The resignation of a managing or full-time director becomes effective only when accepted by the company.

---

[169] Companies Act, 1956, Sec. 316.

[170] Companies Act, 1956, Sec. 317.

A manager is an individual appointed to direct all or substantially all of the affairs of the company. [171] A manager need not be, and usually is not, a director.

---

[171] Companies Act, 1956, Sec. 2(24).

The Companies Act specifies the circumstances in which a person may not be appointed the director of a company. [172]

---

[172] Companies Act, 1956, Sec. 274.

Meetings of the directors must be held at least once in each quarter. [173] One-third of the number of directors or two directors (whichever is higher) constitute a quorum. [174] Resolutions require a majority vote of those entitled to vote. [175] Directors with an interest in a resolution do not form part of the quorum for and may not vote on that resolution.

---

[173] Companies Act, 1956, Sec. 285.

[174] Companies Act, 1956, Sec. 287.

[175] Companies Act, 1956, Sec. 289.

Every public company with a paid up capital of Rs.50 million or more must constitute a committee of the board known as the "audit committee." The audit committee must consist of at least three directors and such number of other

directors as the Board may determine, of which two-thirds of the total number must be directors, other than the managing or full-time director. The audit committee must act in accordance with the terms of reference specified by the board. [176]

[176] Companies Act, 1956, Sec. 292A.

The Companies Act empowers the board to exercise "all such powers and to do all such acts and things as the company is authorized to exercise and do," except those required to be exercised by the company in general meeting. [177] The Act specifically lists the following as requiring the consent of the shareholders at the general meeting: [178]

[177] Companies Act, 1956, Sec. 291.

[178] Companies Act, 1956, Sec. 293.

(i) The sale, lease, or other disposition of the whole, or any, of the undertakings of the company;

(ii) The remission of, or the granting of time for the repayment of, any debt due from a director;

(iii) The investment, other than in trust securities, of the sale proceeds on the sale of any of the company's undertakings or properties, or of the compensation for compulsory acquisition of such undertakings or properties;

(iv) The borrowing of money, when the money borrowed exceeds the aggregate of the paid-up capital and free reserves of the company; and

(v) Contributions to charities and other funds not directly related to the business of the company or the welfare of its employees of any amount exceeding in any financial year the greater of Rs.50,000 or 5% of the average net profits during the three previous financial years.

The Companies Act also places the following restrictions on directors and their relatives:

(i) No person may be a director of more than 15 companies. [179]

(ii) No company may give a loan to a director, the relative or partner of a director, or a firm in which the director is a partner, or a private company in which he or she is a director, or any body corporate at a general meeting of which not less than 25% of the total voting power may be exercised or controlled by any such director or by two or more such directors together, or any body corporate of which the board of directors, managing director or manager is accustomed to act in accordance with directions or instructions of the board or of any director or directors of the lending company without the approval of the central government. This restriction does not apply to any loan given by a private company that is not a subsidiary of a public company, or by a banking company, or to any loan made by a holding company to its subsidiary company. [180]

(iii) A director, the relative of a director, or a firm in which such director or relative is a partner, any other partner in such a firm, or a private company of which the director is a member or director, may not enter into contracts with the company for the sale, purchase or supply of any goods, materials or services exceeding Rs.5,000 per year, or underwrite the shares or debentures of the company without the consent of the board of directors. Further, if the company has a paid-up share capital of Rs.10 million or more, such a contract may not be entered into without the prior approval of the central government. [181]

(iv) A director, the relative of a director, or the partner of a director, a firm in which such director or relative of such director is a partner; a private company of which such director is a director or a member, and a director or manager of such a private company, may not be employed by the company to hold an office or position of profit, without the sanction of a special resolution of the shareholders. [182]

[179] Companies Act, 1956, Secs. 275 and 278.

[180] Companies Act, 1956, Sec. 295.

[181] Companies Act, 1956, Sec. 297.

[182] Companies Act, 1956, Sec. 314.

In the case of any company other than a private company that is not a subsidiary of any public company, the remuneration of management, exclusive of directors' fees for attending meetings, may not exceed 11% of the net

profits of the company. [183] Further restrictions are imposed within this overall limitation, as follows:

[183] Companies Act, 1956, Sec. 198(1).

(i) The compensation of a managing/full-time director or a manager may not exceed 5% of the net profits. Where there are two or more managing/full-time directors, their combined compensation may not exceed 10% of the net profits. [184]

(ii) Directors who are neither full-time nor managing directors may be paid a remuneration of:

- 1% of the net profits of the company, if the company has a managing or full-time director or manager; or
- 3% of the net profits of the company otherwise. [185]

[184] Companies Act, 1956, Secs. 309(3) and 387.

[185] Companies Act, 1956, Sec. 309(4).

R. Selling Agents

Sole selling agents for any area may be appointed for a period not exceeding five years, subject to approval by a resolution of the members at a general meeting of the company. [186]

[186] Companies Act, 1956, Sec. 294(1).

The central government is granted broad powers of scrutiny and control over selling agency agreements. [187] The powers of the board of directors to appoint selling agents other than as sole selling agents remain unaffected. The provisions apply to all private and public companies.

[187] Companies Act, 1956, Sec. 294(5).

In the following cases, a company is not liable to pay compensation to a sole selling agent for premature termination: [188]

[188] Companies Act, 1956, Sec. 294A(1).

(i) When the appointment of the agent is not approved in the first general meeting after his or her appointment;

(ii) When the agent resigns due to the reconstruction of the company or its amalgamation with another body corporate and is appointed as sole selling agent of the new body corporate;

(iii) Where the agent resigns from his or her office;

(iv) Where the agent is guilty of fraud, breach of trust or gross negligence of his or her duty as sole selling agent; or

(v) Where the agent instigates his or her own termination, whether directly or indirectly.

In all other cases, compensation is payable for the unexpired term or for a period of three years, whichever is shorter. Compensation is calculated based on the average remuneration actually earned in the previous three years.

Permission from the central government is required where an individual or a firm or a body corporate having a substantial interest in the company is appointed as sole selling agent of the company.

A company having paid up share capital of Rs.5 million or more may not appoint sole selling agents without approval being given in general meeting by a special resolution, as well as the approval of the central government. [189]

[189] Companies Act, 1956, Sec. 294AA.

S. Intercorporate Loans and Investments

A company may not, directly or indirectly:

(i) Make any loan to any other body corporate;

(ii) Give any guarantee or provide security in connection with any loan made by any other person to, or to any person by, any body corporate; or

(iii) Acquire, by way of subscription, purchase or otherwise, the securities of any other body corporate, where the aggregate of such loans, investments, guarantees and securities would exceed 60% of its paid-up share capital and free reserves, or 100% of its reserves, whichever is higher.

Where the aggregate of loans and investments made and the amounts for which guarantees or security are provided together with the investment, loan, guarantee or security proposed to be made or given by the board of directors, exceeds the limit referred to above, prior authorization by means of a special resolution of the shareholders in a general meeting is required.

However, the board of directors may give a guarantee without being previously authorized by a special resolution, if:

• A resolution is passed at a meeting of the board of directors authorizing it to give a guarantee and the resolution is confirmed, within 12 months, at a general meeting of the company or the annual general meeting of the company held immediately after the passing of the board resolution, whichever is earlier; and

• There exist exceptional circumstances that prevent the company from obtaining previous authorization by a special resolution passed in a general meeting for giving a guarantee.

The resolution authorizing a loan or investment to be made or a guarantee or security to be given must be passed with the consent of all the directors present at the meeting and the prior approval of the public financial institutions where any term loans subsist. However, the prior approval of a public financial institution is not required where the aggregate of the loans and investments made, and the amounts for which guarantee or security is provided, along with the investments, loans, guarantee or security proposed to be made or given does not exceed the 60% limit, if there is no default in repayment of loan installments or payment of interest thereon under the terms and conditions of the loan.

A company is not permitted to make a loan to a body corporate at a rate of interest lower than the prevailing bank rate.

The restrictions referred to above under (i) through (iii) also apply to a company that has defaulted in complying with the provisions applicable for accepting deposits from the public, while such default subsists.

However, the restrictions do not apply to:

(i) Any loan made by a holding company to its wholly-owned subsidiary;

(ii) Any guarantee given or any security provided by a holding company with respect to a loan made to its wholly-owned subsidiary;

(iii) The acquisition by a holding company, by way of subscription, purchase or otherwise, of the securities of its wholly-owned subsidiary;

(iv) Investment in the rights issues of the company (see G, 4, above); or

(v) Any loan made, any guarantee given or any security provided or any investment made by:

• A banking or insurance company or housing finance company, or a company established with the object of financing industrial enterprises or of providing infrastructure facilities;

• A company the principal business of which is the acquisition of shares, stock, debentures or other securities; or

- A private company that is not a subsidiary of a public company. [190]

[190] Companies Act, 1956, Sec. 372A.

T. Compromise, Arrangement, Reconstruction and Amalgamation

A company may enter into a compromise or arrangement between itself and its creditors, or between itself and its members. An application may be made by the company, any creditor or any member of the company, or by the liquidator in the case of a company in the process of winding up, to the NCLT, which may order a meeting of the parties to the scheme of compromise or arrangement. If three-fourths of the members or creditors present in person or by proxy agree to a compromise or arrangement, the NCLT must sanction the scheme, which is binding on the company, the liquidator and contributory (see definition in V, below), and all the members or creditors, as the case may be. [191] The word "arrangement" is to be interpreted broadly and includes a reorganization of the share capital of a company.

[191] Companies Act, 1956, Sec. 391.

The NCLT sanctioning the scheme of compromise or arrangement has powers, under the Companies Act, to supervise the carrying out of the compromise or arrangement, and to give directions or make modifications necessary for the proper working of the compromise or arrangement. [192] Where the compromise or arrangement is in connection with a scheme for reconstruction/reorganization of any company or companies, or the amalgamation of any two or more companies and, under the scheme, all or part of the undertaking, property or liabilities of the transferor company is to be transferred to the transferee company, the NCLT may by an order provide for: [193]

[192] Companies Act, 1956, Sec. 392.

[193] Companies Act, 1956, Sec. 394.

(i) The transfer to the transferee company of the whole or any part of the property or liabilities of the transferor company;

(ii) The allotment or appropriation by the transferee company of any shares, debentures, policies or other like interests in the transferor company that, under the compromise or arrangement, are to be allotted or appropriated by the transferor company to or for any person;

(iii) The continuation by or against the transferee company of any legal proceedings pending by or against the transferor company;

(iv) The dissolution, without winding-up, of the transferor company;

(v) Payments to creditors who, within such time and in such manner as the NCLT directs, dissent from the compromise or arrangement; and

(vi) Such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction or amalgamation is fully and effectively carried out.

The Companies Act provides for another form of arrangement or amalgamation that does not require an application to the court for the scheme to be carried out. Under this form, the transferee company makes an offer to the shareholders of the transferor company to purchase their shares in the transferor company at a stated price and specifies a time within which the offer is to be accepted. If shareholders of the transferor company owning nine-tenths in value of the transferor company's shares accept the offer, the transferee company purchases their shares and proceeds to acquire the shares of the dissident shareholders in the manner provided for in the Act. There is provision in the Act for adequately safeguarding the rights of dissident shareholders. [194]

[194] Companies Act, 1956, Sec. 395.

U. Protection of Minority and Public Interests

A number of provisions protect minority shareholders against oppression or mismanagement of a company's affairs by majority shareholders and/or management.

The members of a company have the right to apply to the NCLT for relief if the affairs of the company are conducted in a manner oppressive to any member or in a manner prejudicial to public interest. The petition should indicate that the facts would justify issuing a winding up order but it should also request that such an order not be issued because it would unfairly prejudice the petitioner and other members. [195]

[195] Companies Act, 1956, Sec. 397.

The members of a company also have the right to apply to the NCLT for relief if the affairs of the company are conducted in a manner prejudicial to the public interest or the interest of the company or if, because of a change in the management or control of the company, it is likely that the affairs of the company will be conducted in a manner prejudicial to public interest or in a manner prejudicial to the interests of the company. [196]

[196] Companies Act, 1956, Sec. 398.

The right to apply to the NCLT is given to 100 members, or to 1/10 of the total number of members, whichever is less, or any member or members holding not less than 1/10 of the issued share capital of the company. [197] The right to apply is not confined to an oppressed minority of the shareholders alone. An oppressed majority may also apply.

[197] Companies Act, 1956, Sec. 399.

If oppression or mismanagement is proved, the NCLT may, among other things, pass an order providing for any of the following:

(i) The regulation of the future conduct of the company's affairs;

(ii) The purchase of the shares or interests of any members of the company by other members of the company or by the company itself;

(iii) Where the company purchases its own shares as indicated above in (ii), the consequent reduction of its share capital;

(iv) The termination, setting aside or modification of any agreement between the company and specified persons;

(v) The termination, setting aside or modification of any agreement between the company and any person other than the managing director or any other director or manager after due notice has been given to such party and after consent to modify any such agreement has been obtained;

(vi) The setting aside of any transfer, delivery of goods, payment execution, or other acts relating to property within three months before the date of application; and

(vii) Any other matter that, in the opinion of the NCLT, is just and equitable. [198]

[198] Companies Act, 1956, Sec. 402.

The aggrieved shareholders may also apply for administrative relief. The central government is empowered to appoint to the board of the company the number of directors specified by the NCLT, to safeguard effectively the interests of the company, its shareholders or the public interest. The central government may issue further directions for the removal of an auditor already appointed and the appointment another auditor in his or her place, or for the alteration of the articles of the company. [199]

[199] Companies Act, 1956, Sec. 408.

The central government has the power to intervene in the affairs of a company in the public interest or in the interest of the company. It may bring an action against a person as being unfit to hold the office of director or a position in

the management of the company. [200]

---

[200] **Companies Act, 1956, Sec. 388-B.**

V. Winding Up and Dissolution

A company may be wound up (liquidated) if it is insolvent, if the shareholders desire to wind it up or if it is considered desirable in the public interest. The Companies Act prescribes two methods for winding up a company: by the NCLT or voluntarily. [201]

---

[201] **Companies Act, 1956, Sec. 425.**

A company may be wound up by the NCLT if:

(i) The company has, by special resolution, resolved that the company be wound up by the NCLT;

(ii) The company is unable to pay its debts;

(iii) The company defaults in delivering the statutory report to the Registrar of Companies or in holding the statutory meeting;

(iv) The company does not commence its business within a year of its incorporation or suspends its business for a whole year;

(v) The number of members is reduced below the statutory minimum;

(vi) The NCLT is of the opinion that it is just and equitable to wind up the company;

(vii) The company has defaulted in filing with the Registrar of Companies its balance sheet and profit and loss account or annual return for any five consecutive financial years;

(viii) The company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality; or

(ix) In the case of a sick industrial company, the Tribunal, after considering various factors, is of the opinion that the company should be wound up. [202]

---

[202] **Companies Act, 1956, Sec. 433. "Sick" Industrial Companies are defined in Companies Act, 1956, Sec. 3(46AA).**

A petition to the NCLT for winding up may be brought by:

(i) The company;

(ii) A creditor;

(iii) A "contributory;"

(iv) All or any of the above parties;

(v) The Registrar of Companies; or

(vi) A person authorized by the central government under Section 243 of the Companies Act, on the grounds that it is just and equitable to wind up the company; [203] **or**

(vii) The central government, on the grounds that the company has acted against the interests of the sovereignty and integrity of India, the security of the State, friendly relations with foreign States, public order, decency or morality.

[203] Companies Act, 1956, Sec. 439.

A "contributory" is defined as a person liable to contribute to the assets of the company in the event of its dissolution. In a company limited by shares, a contributory is generally a shareholder that has not fully paid up on the shares that it holds.

One or more liquidators are appointed by the company or court to wind up the company's affairs and distribute its assets.

In the case of winding up by the NCLT, the company stands dissolved from the date the NCLT issues an order that the company be dissolved. The NCLT issues an order of dissolution when the affairs of a company are completely wound up or when, in the opinion of the NCLT, the liquidator may not proceed with the winding up any further and in the circumstances of the case it is just and reasonable that the company should be dissolved. [204]

[204] Companies Act, 1956, Sec. 481.

A company may be wound up voluntarily by a special resolution to that effect. [205] In such a case, the company ceases to do business except for purposes of the winding up. The company's corporate status, however, continues until the company is dissolved. [206] In the case of a voluntary winding up, the company stands dissolved from the date the liquidator submits his report to the NCLT stating that the affairs of the company have not been conducted in a manner prejudicial to the interests of its members or to the public interest. [207]

[205] Companies Act, 1956, Sec. 484.

[206] Companies Act, 1956, Sec. 487.

[207] Companies Act, 1956, Sec. 497.

W. Foreign Corporations

Foreign corporations are permitted to operate in India under their foreign charters pursuant to regulations prescribed by the Companies Act. [208] Within 30 days after establishing a place of business in India, a foreign corporation must submit to the Registrar of Companies the following:

[208] Companies Act, 1956, Secs. 591–608.

(i) A certified copy of the charter, statutes or memorandum, and articles of the company, or other instrument defining the company's constitution, with a certified translation of the documents in English if they are not in English. (Rule 16 of the Companies (Central Government's) Rules specifies the manner in which the translation is to be certified and Rule 17 specifies the persons who are required to certify the documents);

(ii) The full address of the registered or principal office of the company abroad;

(iii) A list of directors giving, with respect to each of the directors who is an individual, his or her current name and surname in full, any former name or names and surname or surnames in full, usual residential address, nationality, nationality of origin if different from current nationality, and business occupation or particulars of any one of his or her other directorships, and in the case of directors that are bodies corporate, with respect to each of them, its corporate name, its registered or principal office, and the full name and address, nationality, and nationality of origin (if different) of each of its directors;

(iv) The current name and surname, former name and surname, and usual residential address of the secretary if the secretary is an individual; its corporate name and its registered or principal office if the secretary is a body corporate; and, in the case of a firm, the partners of which are joint secretaries, the name and principal office of the firm only;

(v) The names and addresses of persons resident in India and authorized to accept service of documents, notices and processes on behalf of the company; and

(vi) The address and the principal place of business in India. [209]

---

[209] Companies Act, 1956, Sec. 592.

Any change or alteration in the above particulars must be reported to the Registrar of Companies within two months of the date of the change or alteration. [210]

---

[210] Companies Act, 1956, Sec. 593.

The documents and other information must be filed in two places, that is, with the Registrar of Companies of the state in which the foreign company has its principal place of business and with the Registrar of Companies in New Delhi. [211] The latter requirement is for purposes of having a central record of foreign companies registered in India. The obligation to file documents and particulars terminates if a foreign company ceases to have a place of business in India and gives notice to the Registrar of Companies to that effect. [212]

---

[211] Companies Act, 1956, Sec. 597(1) and (2).

[212] Companies Act, 1956, Sec. 597(3).

A foreign company is required, each calendar year, to make up a profit and loss account and balance sheet under the provisions of the Companies Act, which are laid before the general meeting of the shareholders, and to file a copy of these documents with the Registrar of Companies. If any such document is not in English, a certified translation thereof must be annexed to it. [213] Every foreign company must have its name (indicating whether it is a limited company) and its country of incorporation displayed conspicuously, in English and the local language, on the outside of its place of business, in every prospectus inviting subscriptions in India for its shares and debentures and on the official stationery/publications of the company. [214]

---

[213] Companies Act, 1956, Sec. 594.

[214] Companies Act, 1956, Sec. 595.

The provisions of the Companies Act relating to the registration of charges (see K, above) and books of account apply to a foreign company. [215]

---

[215] Companies Act, 1956, Sec. 600.

X. Administration

The general administration of the Companies Act is the responsibility of the NCLT, which is constituted by the central government. The NCLT is a quasi–judicial authority. It exercises the powers and functions conferred on it under the Companies Act and discharges such powers and functions of the central government as may be conferred on it.

The NCLT consists of a President and a number of judicial and technical members, not exceeding 62, appointed by the central government. [216] The Tribunal has the power to constitute regional branches and to draw up rules and procedures for the conduct of its business and the business of its regional branches. There is a Registrar of Companies in each state to receive and deal with statutory documents and other matters (including annual financial statements).

---

[216] Companies Act, 1956, Sec. 10FC.

The NCLT and its regional branches have quasi–judicial powers pursuant to the code of civil procedure with respect to matters specified in the Companies Act. Under the Companies Act, the Tribunal is required to be guided by the principles of natural justice and to act on its own discretion. An appeal lies to the National Company Law Appellate Tribunal (NCLAT) on any question of law arising from any decision or order of the NCLT. [217]

---

[217] Companies Act, 1956, Sec. 10FQ.

Y. Securities and Exchange Board of India

The SEBI regulates and promotes the orderly development of the capital market in India.

The SEBI has three primary functions:

(i) To deal with all matters relating to the development and regulation of the securities market and investor protection, and to advise the government on these matters;

(ii) To prepare comprehensive legislation for the regulation and development of the securities market; and

(iii) To carry out such functions as may be delegated to it by the central government for the development and regulation of the securities market.

Mutual funds, merchant bankers, FIIs, portfolio managers, stockbrokers, sub-brokers, share transfer agents, bankers and registrars to public issue, underwriters, investment advisors, and any other intermediaries who may be associated with the securities market in any manner have been brought under the purview of the regulatory powers of the SEBI. Rules, regulations and guidelines have been issued by the SEBI in this regard and are available on the website http://www.sebi.gov.in.

Some of the important rules, regulations and guidelines issued by SEBI are:

(i) The SEBI (Insider Trading) Regulations 1992;

(ii) The SEBI (Merchant Bankers) Rules/Regulations 1992;

(iii) The SEBI (Mutual Funds) Regulations 1996;

(iv) The SEBI (Portfolio Managers) Rules/Regulations 1993;

(v) The SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Markets) Regulations 2003;

(vi) The SEBI (Depositories and Participants) Regulations 1996;

(vii) The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 1997;

(viii) The SEBI (Buy Back of Securities) Regulations 1998;

(ix) The SEBI (Stock Brokers and Sub-brokers) Rules/Regulations 1992;

(x) The SEBI (Underwriters) Rules/Regulations 1993;

(xi) The SEBI (Debentures Trustees) Rules/Regulations 1993;

(xii) The SEBI (Bankers to an Issue) Rules/Regulation 1994;

(xiii) The SEBI (Registrars to an Issue and Share Transfer Agents) Rules/Regulations 1993;

(xiv) The SEBI (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines 1999;

(xv) The SEBI (Credit Rating Agencies) Regulations 1999;

(xvi) The SEBI (Collective Investment Schemes) Regulations 1999;

(xvii) The Private Limited Company and Unlisted Public Limited Company (Buy-Back of Securities) Rules 1999;

(xviii) The SEBI (Custodian of Securities) Regulations 1996;

(xix) The SEBI (Venture Capital Funds) Regulations 1996;

(xx) The SEBI (Foreign Institutional Investors) Regulations 2006;

(xxi) The SEBI (Procedure for Board Meetings) 2001;

(xxii) The SEBI (Foreign Venture Capital Investors) Regulations 2000;

(xxiii) The SEBI (Issue of Sweat Equity) Regulations 2000;

(xxiv) The SEBI (Procedure for Holding Enquiry by Enquiry officer and Imposing penalty) Regulations 2002;

(xxv) The SEBI (Ombudsman) Regulations 2003;

(xxvi) The SEBI (Central Database of Market Participants) Regulations 2003;

(xxvii) The SEBI (Self Regulatory Organizations) Regulations 2004;

(xxviii) The SEBI (Criteria for Fit and Proper Person) Regulations 2004;

(xxix) The SEBI (Interest Liability Regularisation) Scheme 2004;

(xxx) The Guidelines for Opening of Trading Terminals Abroad;

(xxxi) The SEBI (Delisting of Securities) Guidelines 2003;

(xxxii) The SEBI (Informal Guidance) Scheme 2003;

(xxxiii) The Guidelines for Anti-money laundering measures;

(xxxiv) The SEBI (Disclosure and Investor Protection) Guidelines 2000; and

(xxxv) The SEBI (Regulatory Fee on Stock Exchanges) Regulations 2006.

Z. Depositories Act, 1996

The Depositories Act, 1996 introduced the system of depositories to Indian capital markets. The depository system that has come into being is founded on absolute trust combined with a strict rule-based approach. The rule under the Act seeks to ensure that investors opting for the depository mode will at all times be protected from any abuse of the system.

1. Creation of Depositories

The Depositories Act, 1996 provides for the creation of one or more depository institutions registered under the Companies Act that has/have been granted a certificate of registration by the SEBI. A depository acts as a depository only after obtaining a certificate of commencement of business from the SEBI. A depository must have adequate

systems and safeguards to prevent the manipulation of records and transactions in order to be eligible to obtain a certificate of commencement of business. [218]

[218] Depositories Act, 1996, Sec. 3.

2. Depository and Participant

The Depositories Act, 1996 envisages that a depository participant will be deemed an agent of the depository. [219] The Act envisages that a depository will interface with users through a set of depository participants, who are persons dealing directly with the depository on their own account or for their clients. [220]

[219] Depositories Act, 1996, Sec. 4.

[220] Depositories Act, 1996, Sec. 5.

3. Options for Receiving Security Certificates or Holding Securities with a Depository

An investor is given the option of holding physical securities currently or of choosing a depository-based ownership record. This option may be exercised by the investor either at the time the company initially offers the securities indicating his/her choice in the application form or at any subsequent time. The investor is also able to switch from the depository mode to the nondepository (i.e., paper-based) mode and vice versa. [221]

[221] Depositories Act, 1996, Sec. 8.

4. Securities to Be Fungible

The securities held by a depository are fungible. [222] In accordance with the Depositories Act, 1956, share certificates need not carry distinctive numbers and all shares form part of a "fungible mass." All share certificates are interchangeable; this is akin to withdrawing money from a bank account without being concerned about the number and denomination of the currency notes issued by the bank cashier at the time of withdrawal.

[222] Depositories Act, 1996, Sec. 9.

5. Ownership Records and Hypothecation

Ownership records in a depository are accepted as *prima facie* evidence in legal proceedings. The depository records receive the same treatment as is available to banks under the Banker's Book Evidence Act. [223] A depository must also allow for pledging or hypothecation with respect to securities left in the depository mode. [224]

[223] Depositories Act, 1996, Sec. 15.

[224] Depositories Act, 1996, Sec. 12.

Taxes conventionally are broadly classified as direct taxes or indirect taxes. Direct taxes are taxes that a taxpayer pays directly from his income, wealth or estate. India's direct taxes comprise income tax and wealth tax. Indirect taxes are taxes that a taxpayer pays indirectly — while purchasing goods or paying for services. India's indirect taxes include service tax, excise duty, customs duty, sales tax and stamp duty. Direct taxes could be described as taxes that are paid after income reaches the hands of the taxpayer; indirect taxes are taxes paid before goods reach the taxpayer.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
IV. Principal Taxes

A. Income Tax

The first Income Tax Act in India was introduced in 1860 and was enacted to be in force for five years. The Act of 1886 was the first regular Act in the country. The scheme of taxation was modeled on English income tax law

although, over the years, it has come to differ from such law in many of its essential features. The Income Tax Act of 1922 formed the basic legislation until 1961, when a new Act was enacted to rationalize and simplify the system, which had grown complex over the years.

The income tax law of India is currently embodied in the Income Tax Act of 1961 (ITA), which is derived from two legislative Acts. The tax structure and administration is contained in the ITA. The annual Finance Act fixes the tax rates each year. The Finance Acts often also enact amendments to the basic ITA. In addition, Income Tax Amendment Acts are enacted when basic changes are made in the tax laws.

The Central Board of Direct Taxes (CBDT) is empowered to make rules for the administration of the income tax, which, when published, have the force of law. The rules prescribe the procedures and various forms for implementing the substantive provisions of the law.

Decisions of the tribunals and courts are published periodically. The decisions of the Appellate Tribunals and courts are published in various journals and magazines.

Tax cases decided before Independence are still valid law. Also, English decisions are looked to for precedent, even though they do not deal directly with the Indian income tax law.

Income tax is levied on the income and capital gains of any person, whether an individual or a legal entity. Residents are taxed on worldwide income; nonresidents are taxed on income that is received or deemed to be received in India or that accrues or arises, or is deemed to accrue or arise, in India. See further at V, A, below.

***Note*: The government of India is committed to bringing about reforms to the tax laws in the country to make them commensurate with the needs of the modern business and economic world, keeping in mind the growth of India in recent years and its continuing dominant position in the context of economic growth and development, in the region and globally. The intention is to provide a competitive environment to overseas investors seeking to invest in India and to provide such investors with a platform that is significantly more beneficial than other options that might be considered for investment. To this effect, a draft Direct Tax Code has been placed before Parliament and is currently being discussed and refined in a number of forums, including professional bodies and chambers of commerce. The Direct Tax Code is proposed to be enacted as law, effective April 1, 2011.**

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
IV. Principal Taxes

B. Wealth Tax

Wealth tax in India is levied under the Wealth Tax Act, 1957. The tax is payable each year on taxable wealth. Liability to wealth tax depends on residential status and citizenship.

Resident Indian citizens and companies pay tax on global wealth. Individuals who are "resident but not ordinarily resident" and nonresident individuals and companies are taxed on their wealth in India, their foreign wealth being entirely exempt. Foreign citizens, whether resident in India or abroad, pay wealth tax only on net wealth in India. Foreign wealth is exempt. See further at V, B, below.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
IV. Principal Taxes

C. Inheritance or Gift Tax

There is no gift or inheritance tax in India. However, any receipt in excess of Rs. 50,000 by an individual or a Hindu Undivided Family (HUF), by way of cash or real property, for inadequate or no consideration, is taxable under the head "Income from Other Sources." (See V, A, 4, e, below.)

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
IV. Principal Taxes

D. Excise Duty

Excise duty is a duty or tax levied on the manufacture or production of goods in India. Excise duty is charged as a specific duty, an *ad valorem* duty, as a percentage of "tariff" value, or as a duty based on a maximum retail price. See further at VII, B, below.

Foreign Income Portfolios

E. Customs Duty

The Customs Act, 1962 provides for the levy and collection of duty on imports as well as exports of goods. See further at VII, C, below.

F. Stamp Duty

Stamp duties are levied on instruments recording transactions. See further at VII, E, below.

G. Sales Tax/Value Added Tax

Sales taxes are levied by the central government and value added tax (VAT) by the states. Central sales tax is imposed by the government on the interstate movement of goods. VAT is levied by the Indian states on sales of goods by dealers. Only moveable goods are taxed. A state may levy VAT only on transactions where both the purchaser and the seller are within the state. A state has no power to tax interstate sales. See further at VII, F, below.

H. Service Tax

Certain services are chargeable to service tax in India under Chapter V of the Finance Act, 1994, as amended by subsequent Finance Acts. The tax is levied on taxable services and the person rendering the services is responsible for collecting the service tax and paying it to the central government. See further at VII, G, below.

A. Income Tax

The income tax law of India is embodied in the Income Tax Act of 1961 (ITA), which is derived from two legislative Acts. The tax structure and administration is contained in the ITA. The annual Finance Act fixes the tax rates each year. The Finance Acts often also enact amendments to the basic ITA. In addition, Income Tax Amendment Acts are enacted when basic changes are made in the tax laws.

The Central Board of Direct Taxes (CBDT) is empowered to make rules for the administration of the income tax, which, when published, have the force of law. The rules prescribe the procedures and various forms for implementing the substantive provisions of the law.

Decisions of the tribunals and courts are published periodically. The decisions of the Appellate Tribunals and courts are published in various journals, websites and magazines.

Tax cases decided before Independence are still valid law. Also, English decisions are looked to for precedents even though they do not deal directly with the Indian income tax law.

In India, the avoidance of tax liability by arranging commercial affairs so as to minimize the tax burden is, generally, not prohibited. A taxpayer may resort to a device to divert income before it accrues or arises to him. The effectiveness of the device depends not on considerations of morality, but on the operation of the ITA. However, it was held by the Supreme Court that it is up to the court to determine the nature of new and sophisticated legal devices to avoid taxes, to expose the devices for what they are, and to refuse to give judicial benediction to them. [225] It was further stated

by the Court that it is neither fair nor desirable to expect legislation to intervene and take care of every device and scheme to avoid taxation. This judgment had far-reaching implications until another pronouncement of the Supreme Court held that, where the true effect of the construction of any instrument or deed is clear and admits of no ambiguity, it is not relevant for the Court to consider the plea of tax avoidance by the Revenue. [226] In a landmark judgment, the Supreme Court has held that if the Court finds that, notwithstanding a series of legal steps taken by an assessee (i.e., the taxpayer), the intended legal result has not been achieved, the Court might be justified in overlooking the intermediate steps, but it would not be permissible for the Court to treat the intervening legal steps as *non est* based on some hypothetical assessment of the "real motive" of the assessee. The Court must deal with what is tangible in an objective manner and cannot afford to chase a will-o'-the-wisp. The submission cannot be accepted that an act that is otherwise valid in law may be treated as *non est* merely on the basis of some underlying motive supposedly resulting in some economic detriment or prejudice to the national interests. [227]

[225] *McDowell & Co. Ltd. v. C.T.O.* (S.C.) 154 I.T.R. 148 [1985].

[226] *C.W.T. v. Arvind Narottam* (S.C.) 173 I.T.R. 479 [1988].

[227] *Union of India v. Azadi Bachao Andolan* (S.C.) 263 I.T.R. 706 [2003].

1. Tax Year

a. Assessment Year

The taxpayer's income of the financial year (tax year) immediately preceding the assessment year (i.e., the "previous year") is taxed during the assessment year at the rates prescribed for such assessment year by the relevant Finance Act. The assessment year means the period of 12 months beginning on April 1 of each year and ending on March 31 of the following year. [228]

[228] Income Tax Act, 1961 (ITA), Sec. 2(9).

b. Previous Year

The "previous year" is the financial year (tax year) immediately preceding the assessment year and begins on April 1 and ends on March 31 for all taxpayers. [229] This uniform financial year should be followed for all sources of income.

[229] ITA, Sec. 3.

Example: If the assessment year is 2010-11, the previous year is the year April 1, 2009 to March 31, 2010.

In the case of a newly set up business or profession or a source of income arising for the first time, the first previous year is the period beginning on the date of the setting up of the business/profession or the date on which the source of income arose for the first time and ending on the following March 31.

The ITA, as it stands amended on the first day of April of any year, applies to the assessment of that year. Any amendments to the Act that come into force after the first day of April of an assessment year do not apply to that year, even if the assessment is actually made after the amendments come into force. This principle was laid down by the Supreme Court. [230] If, after an assessment order is passed but pending an appeal or a reference, legislation with retrospective effect comes into operation, the deciding authority must give effect to such legislation.

[230] *Karimtharuvi Tea Estate Ltd. v. State of Kerala* (S.C.) 60 I.T.R. 262 [1966].

2. Residence

Liability to tax under the ITA depends on a taxpayer's residential status and is not affected by the taxpayer's nationality or domicile. [231]

[231] ITA, Sec. 6.

a. Individuals

An individual is regarded as resident in India in any tax year if he or she:

(i) Is in India for a period or periods amounting to 182 days or more in a tax year; or

(ii) Is in India for an aggregate period of 60 days or more (182 days in certain cases [232]) in a tax year and has been in India for an aggregate period of 365 days or more in the four tax years preceding that tax year.

[232] These cases are that of: (1) an individual who is a citizen of India who leaves India in any previous year as a member of the crew of an Indian ship or for the purpose of employment outside India; or (2) an individual who is a citizen of India, or a person of Indian origin, who, being outside India, comes on a visit in any previous year.

An individual is regarded as "resident but not ordinarily resident" (NOR) in India in any tax year, even if it qualifies as a resident on one or both of the bases referred to above in (i) and (ii), if he or she:

(i) Has been a nonresident of India in nine out of the 10 tax years preceding that tax year; or

(ii) Has, during the seven tax years preceding that year, been in India for a period or periods amounting to 729 days or less.

A nonresident is an individual who is not resident in India.

Residential status under other direct tax laws is the same as under the ITA.

b. Hindu Undivided Family/Firm/Association of Persons

A Hindu Undivided Family (HUF)/Firm/Association of Persons (AOP) is regarded as resident in India in any tax year in every case, except where, during the year, the control and management of its affairs is situated wholly outside India.

A HUF is regarded as NOR in any tax year, even if it qualifies as a resident on the bases referred to above if the manager of the HUF:

(i) Has been a nonresident of India in nine out of the 10 previous years preceding that year; or

(ii) Has, during the seven years preceding that year, been in India for a period of, or periods amounting in all to, 729 days or less.

c. Companies

A company is said to be resident in India in any previous year if:

(i) It is an Indian company; or

(ii) During that year, the control and management of its affairs is situated wholly in India.

A foreign company would have a part of its management and control outside India and hence would be nonresident. There is no intermediary NOR status for a company as there is for individuals.

A domestic company is an Indian company or any other company that, with respect to its income liable to income tax under the ITA, has made the prescribed arrangements for the declaration and payment within India of dividends (including dividends on preference shares) payable out of such income. [233]

[233] ITA, Sec. 2(22A).

A widely held domestic company is defined to mean a company that is not a private company and that either is owned or controlled by the government or the Reserve Bank of India (RBI) or has its equity shares listed on a recognized stock exchange in India or held by cooperative societies. Such a company is regarded as a company in which the public has a substantial interest. [234]

[234] ITA, Sec. 2(18).

All other companies are regarded as companies in which the public does not have a substantial interest.

A foreign company under the ITA is a company that is not a domestic company. [235]

[235] ITA, Sec. 2(23A).

d. Other Persons

Other persons are said to be resident in India in any tax year in every case, except where during that year the control and management of their affairs is situated wholly outside India.

e. Scope of Income Chargeable to Tax

A resident (whether an individual or a legal entity) is taxed on all income in a taxable year, from whatever source derived, that:

(i) Is received or deemed to be received in India;

(ii) Accrues or arises, or is deemed to accrue or arise, in India; or

(iii) Accrues or arises outside India.

Income that accrues or arises to a NOR individual outside India is not charged to tax unless it is derived from a business controlled, or a profession set up, in India.

A nonresident (whether an individual or a legal entity) is taxed on all income in a tax year, from whatever source derived, that:

(i) Is received or deemed to be received in India; or

(ii) Accrues or arises, or is deemed to accrue or arise, in India. [236]

---

[236] **ITA, Sec. 5.**

Note: **Income accruing or arising outside India is not deemed to be received in India by reason only of the fact that it is taken into account in a balance sheet prepared in India.**

Income taxed on the basis that it accrues or arises, or is deemed to accrue or arise, in India is not again taxed on the basis that it is received or is sourced in India.

See e, below, for a discussion of income sourced in India.

3. Charge of Income Tax

a. Principles

The following are the basic principles of income taxation in India: [237]

---

[237] **ITA, Sec. 4.**

(i) Income tax is an annual charge on income.

(ii) Income of the previous year is charged to tax in the following assessment year at the rates applicable to that assessment year.

(iii) Tax rates are fixed annually by the Finance Act; for example, in arriving at the total income tax liability for the previous (tax) year April 1, 2009, to March 31, 2010, relevant to the assessment year 2010-11, the provisions of the law in effect on April 1, 2010, apply.

(iv) The tax is levied on the total income of every taxpayer computed in accordance with the provisions of the ITA.

(v) With respect to income chargeable to tax, the tax is deducted at source or paid in advance as required under the provisions of the ITA.

In relation to the concept of "real income" and the accrual of income, the Supreme Court has laid down the following principles: [238]

---

[238] ***State Bank of Travancore v. CIT*** **(S.C.) 158 I.T.R. 102 [1986].**

(i) It is the real income that accrues or arises to the taxpayer that is taxable. Whether the income has really accrued or arisen to the taxpayer must be judged in light of the reality of the situation.

(ii) If there is any diversion of income at source under any statute or by overriding title, there is really no income that has accrued to the taxpayer.

(iii) The conduct of the parties in treating the income in a particular manner is material evidence of whether the income has accrued or not.

(iv) An acceptable formula for correlating the notion of real income with the method of accounting for

purposes of the computation of income for tax purposes is difficult to evolve.

(v) Any "strait-jacket formula" is bound to create problems in its application to every situation. Resort must, therefore, be had to the facts and circumstances of each case.

The Supreme Court has held that, if a particular type of income is not taxable under the ITA, it may not be taxed on the basis of estoppel or any other equitable doctrine. [239]

---

[239] *CIT v. V. MR. P. Firm, Muar* (S.C.) 56 I.T.R. 67 [1965].

Comment: **The definition of "income" in the ITA is an inclusive one. [240] Even if a receipt is not specifically included in the definition of "income," it may none the less constitute "income." To argue otherwise would require that an exhaustive definition be given to the word "income," when the statute expressly provides an inclusive definition. The idea behind providing an inclusive definition is not to restrict the meaning of "income," but to widen it. [241]**

---

[240] ITA, Sec. 2(24).

[241] *CIT v. G.R. Karthikeyan* (S.C.) 201 I.T.R. 866 [1993].

The word "income" is to be interpreted in its natural and proper sense and thus tax is due on income earned in reality. Where a taxpayer is bound by or undertakes an obligation of an overriding nature to third parties that might compel him to make payments to others to earn profits, only the income actually earned by the taxpayer is taxable in his hands. In such a case, the payments made to the third parties may not be deemed to be payments made out of profits; they are payments made to earn profits. This distinction holds without exception. The true test for determining whether there is a diversion of income by an overriding obligation is whether the amount sought to be disregarded as the taxpayer's income, in fact, never reached him as his income. [242] For example, where a partner in a professional firm is bound by a provision in the partnership agreement that provides that all fees earned by him in his individual capacity as a liquidator of companies belong to the firm, then such fees may not be taxed as the individual income of the partner.

---

[242] *CIT v. Sitaldas Tirathdas* (S.C.) 41 I.T.R. 367 [1993].

---

b. Revenue and Capital Receipts

Income connotes revenue receipts only and not capital receipts. The Supreme Court has held that, for purposes of deciding whether a receipt is a capital or a revenue receipt, the nature of the receipt is determined by its nature in the hands of the recipient and not those of the payer. [243] It is the true nature of the receipt, and not the category under which it is shown in the books, that is decisive. For example, the following have been held to be capital receipts: compensation for the loss of a job; compensation for refraining from competing; compensation received for loss or damage to a capital asset; and the receipt of bonus shares. The following, on the other hand, have been held to be revenue receipts: consideration received for the transfer of a benefit under a contract; amounts received as the capitalized value of a royalty; the reimbursement of expenditure; interest awarded under a statute or contract; profits on foreign exchange fluctuations; and subsidies and grants received.

---

[243] *CIT v. Kamal Behari Lal Singha* (S.C.) 82 I.T.R. 460 [1971].

---

c. Taxable Income

The income of each taxpayer is determined under five heads of income: salaries; income from house property; profits and gains of a business or profession; capital gains; and income from other sources. Specific rules determine what constitutes income from each source.

The total income computed from all sources is adjusted for the setoff of losses from other sources, losses carried forward and unabsorbed depreciation of earlier years. The income so adjusted is the gross total income. The gross total income, less certain specified deductions and tax incentives provided under the ITA, is the total taxable income of a taxpayer.

Certain types of income and receipts are fully exempt from tax and do not form part of gross total income.

d. Agricultural Income

Agriculture is governed by state law and there is no central income tax on income from agriculture or wealth tax on agricultural wealth. However, agricultural income is aggregated with other income to determine the appropriate rate of tax. Certain states with sugar, tea, coffee, cashew, rubber and cardamom plantations levy income tax on agricultural income.

e. Income Deemed to Accrue or Arise in India

Income accruing or arising, directly or indirectly, through or from any business connection, any property, any asset or any source of income in India or through the transfer of a capital asset situated in India is deemed to accrue or arise in India irrespective of whether, in reality, such income accrues or arises in India.

Comment: **Where the dominant purpose of entering into agreements between two foreign companies was for one foreign company to acquire a controlling interest or business economic interests, tangible and intangible, in an Indian company controlled by the other foreign company and not merely shares that the other foreign company held in the Indian company, the agreements would be treated as the transfer of a business asset situated in India and, therefore, the transactions would be subjected to the municipal laws of India, including the ITA and income from such transactions would be deemed to accrue or arise in India.** [244]

---

[244] ***Vodafone International Holdings B.V. v. Union of India*** **(Bom.) 311 I.T.R. 46 [2008].**

The ITA provides for the following exceptions to this general rule: [245]

---

[245] **ITA, Sec. 9.**

(i) If all the operations of a business are not carried on in India, only such part of the income as is reasonably attributable to the operations in India is deemed to accrue or arise in India.

(ii) If a nonresident carries on operations confined to the purchase of goods for purposes of export, no income is deemed to accrue or arise in India.

(iii) If a nonresident is engaged in the business of running a news agency, or publishing newspapers, magazines or journals, no income is deemed to accrue or arise in India from activities confined to the collection and transmission of news and views in India for transmission out of India.

(iv) If a nonresident is an individual who is not a citizen of India, or a firm that does not have any partner who is a citizen of India or who is resident in India, or a company that does not have any shareholder who is a citizen of India or who is resident in India, no income is deemed to accrue or arise to such individual, firm or company in India merely from the shooting of any cinematographic film in India.

The term "business connection" assumes great significance for a nonresident doing business in India. Adequate care should be exercised to ensure mitigation of the tax liability that may arise as a result of the application of this principle. For example, a nonresident selling goods in India should do so on a principal-to-principal basis, lest the profits on such sales be charged to tax in India.

The Supreme Court has held that the expression "business connection" undoubtedly means something more than business. [246] **A business connection involves a relationship between a business carried on by a nonresident that yields profits or gains and some activity in India that contributes directly or indirectly to the earning of those profits or gains. It predicates an element of continuity between the business of the nonresident and the activity in India; a stray or isolated transaction is normally not regarded as a business connection. A business connection may take several forms; it may include the carrying on of a part of the main business or activity incidental to the main business of the nonresident through an agent, or it may merely be a relationship between the business of the nonresident and the activity in India that facilitates or assists the carrying on of that business. Whether there is a business connection from or through which income, profits or gains arise or accrue to a nonresident must be determined based on the facts and circumstances of each case. The expression "business connection" postulates a real and intimate relationship between the activity carried on outside the taxable territories and the activity within the territories, the relationship between the two contributing to the earning of the income by the nonresident in his activity.**

---

[246] ***CIT v. R.D. Aggarwal & Co. and another*** **(S.C.) 56 I.T.R. 20 [1965].**

The term "business connection" has been defined to include any business activity carried out through a person who, acting on behalf of the nonresident:

(i) Has and habitually exercises in India an authority to conclude contracts on behalf of the nonresident, unless his activities are limited to the purchase of goods or merchandise for the nonresident;

(ii) Has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the nonresident; or

(iii) Habitually secures orders in India, mainly or wholly from the nonresident or for that nonresident and other nonresidents controlling, controlled by, or subject to the same common control as, that nonresident.

However, a business connection does not encompass activity carried on through a broker, a general commission agent or any other agent having an independent status and acting in the ordinary course of his business.

Where a broker, general commission agent or other agent works mainly or wholly on behalf of a nonresident (hereafter referred to as the principal nonresident) or on behalf of such nonresident and other nonresidents that are controlled by the principal nonresident or have a controlling interest in the principal nonresident or are subject to the same common control as the principal nonresident, he is not regarded as a broker, a general commission agent or an agent of independent status.

Comment: **A question always arises as regards the computation of profits under the ITA of a permanent establishment (PE) of a foreign enterprise in India. Since there is no specific provision under the Act for computing profits accruing in India in the hands of foreign entities, the profits attributable to the Indian PE of a foreign enterprise are required to be computed in accordance with normal accounting principles and in terms of the general provisions of the ITA. Therefore, the ascertainment of a foreign enterprise's taxable business profits in India involves an artificial division between profits earned in India and profits earned outside India. The ITA is concerned only with the profits earned in India. A method has to be found to ascertain the profits arising in India and the only way to do so is to treat an Indian PE as a separate profit center *vis-à-vis* the foreign enterprise of which it is a PE. This demarcation is necessary in order to earmark the tax jurisdiction over the operation of a company. Unless the PE is treated as a separate profit center, it is not possible to ascertain the profits of the PE, which, in turn, constitute profits arising to the foreign enterprise in India. The computation of profits of each PE (taxable jurisdiction) determines the quantum of income on which the source country may levy the tax. It is, therefore, necessary for the profits of a PE to be computed as independent units.** [247]

---

[247] ***CIT v. Hyundai Heavy Industries Co. Ltd.*** **(S.C.) 291 I.T.R. 482 [2007].**

The following income is also deemed to accrue or arise in India:

(i) Salaries earned in India. For this purpose, any salary payable for:

- **Services rendered in India; and**
- **A rest period or leave period that is preceded and succeeded by services rendered in India and forms part of the service contract of employment, is regarded as income earned in India.**

The Supreme Court has addressed the question of whether a home salary payment made to expatriated employees by a foreign company in a foreign currency abroad may be held to be "deemed to accrue or arise in India" and has held that this would depend on an in-depth examination of the facts in each case. Where a home salary/special allowance payment made by a foreign company abroad is for the rendering of services in India and no work is found to have been performed abroad for the foreign company, such payment would certainly come within the purview of Section 192 of the ITA (relating to tax withholding on salaries), read in conjunction with section 9(1)(ii). [248]

---

[248] ***CIT v. Eli Lilly & Co. (India) Pvt. Ltd.*** **(S.C.) 312 I.T.R. 225 [2009].**

(ii) Income chargeable under the head "Salaries" payable by the government to a citizen of India for service outside India.

(iii) Dividends paid by an Indian company outside India.

(iv) Interest payable by:

- **The Government of India;**
- **A resident, unless the interest is payable with respect to a debt incurred or moneys borrowed and used for purposes of a business or profession carried on by such person outside India or for making or earning any income from any source outside India; or**
- **A nonresident where the interest is payable with respect to any debt incurred or moneys borrowed and used for purposes of a business or profession carried on by such person in India.**

(v) A royalty payable by:

- **The Government of India;**
- **A resident, except where the royalty is payable with respect to a right, property, information used or service utilized for purposes of a business or profession carried on by such person outside India or for purposes of making or earning any income from a source outside India; or**
- **A nonresident, where the royalty is payable with respect to any right, property, information, or service used for purposes of a business carried on by such person in India or for purposes of making or earning any income from any source in India.**

Note: **"Royalty" means consideration (including any lump sum consideration but excluding any consideration that would be income of the recipient chargeable under the head "Capital gains") for:**

- **The transfer of all or any rights (including the granting of a license) with respect to a patent, invention, model, design, secret formula or process or trademark or similar property;**
- **The imparting of any information concerning the working of, or the use of, a patent, invention, model, design, secret formula or process or trade mark or similar property;**
- **The use of any patent, invention, model, design, secret formula or process or trade mark or similar property;**
- **The imparting of any information concerning technical, industrial, commercial or scientific knowledge, experience or skill;**
- **The use of or the right to use any industrial, commercial or scientific equipment;**
- **The transfer of all or any rights (including the granting of a license) with respect to any copyright, literary, artistic or scientific work including a film or video tape for use in connection with television or a tape for use in connection with radio broadcasting, but not including consideration for the sale, distribution or exhibition of a cinematographic film; or**
- **The rendering of any service in connection with the activities referred to above.**

(vi) Income by way of fees for technical services payable by:

- **The Government of India;**
- **A resident, except where the fees are payable with respect to services used in a business or profession carried on by the resident outside India or for making or earning any income from any source outside India; and**
- **A nonresident where the fees are payable with respect to services used in a business or profession carried on by the nonresident in India or for making or earning income from any source in India.**

Note 1: **"Fees for technical services" means any consideration (including any lump sum consideration) for the rendering of any managerial, technical or consultancy services (including the provision of services of technical or other personnel), but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration that would be income of the recipient chargeable under the head "Salaries".**

Note 2: **Income by way of interest, royalties or fees for technical services is deemed to accrue and arise in India and is included in the total income of the nonresident, irrespective of whether the nonresident has:**

(i) A residence or place of business or business connection in India; or

(ii) Rendered services in India.

Under the ITA, the source rule is to be applied for the taxation of interest, royalties and fees for technical services, the intention being to tax interest, royalties and fees for technical services, even in cases where services are provided outside India, as long as they are utilized in India. The source rule, therefore, means that the situs of the rendering of services is not relevant. It is the situs of the payer and the situs of the utilization of the services that will determine the taxability of the services in India. This was the settled position of law until 2007. However, the Honorable Supreme Court held that for any such income to be taxable in India there must be sufficient territorial nexus between the income and the territory of India. It further held that, to establish such a territorial nexus, the services must be rendered in India as well as utilized in India. [249] This interpretation was not in accordance with the source rule. Therefore, to remove doubts regarding the source rule, an Explanation was inserted below Sub-section (2) of Section 9 with retrospective effect from June 1, 1976. (See Note 2, above.)

---

[249] ***Ishikawajima-Harima Heavy Industries Ltd. v. Director of Income-Tax*** **(S.C.) 288 I.T.R. 408 [2007].**

The Supreme Court has held [250] that the term "deemed" income, within the language of Section 9 of the ITA, brings within the net of chargeability income that has not actually accrued but that is supposed notionally to have accrued. The concept of deemed income is a statutory fiction that may include accrued income that would otherwise not have been so included.

---

[250] ***CIT v. Messrs. Bhogilal Leherchand*** **(S.C.) 25 I.T.R. 50 [1954].**

The scope of these deeming provisions is best explained in a decision of the Calcutta High Court. [251] The court held that Section 9(1)(i) of the ITA deals with income deemed to accrue or arise within India, although in fact it does not so accrue or arise. It is income that arises outside India but that, by virtue of the statute, is deemed to accrue or arise within India. This deeming provision describes the nexus between such income and India, which may be:

---

[251] *CIT v. National and Grindlays Bank Ltd*. (Calcutta) 72 I.T.R. 121 [1969].

(i) A business connection in India;

(ii) Property in India;

(iii) An asset in India;

(iv) "Money lent at interest but brought into [India] in cash or in kind"; or

(v) A capital asset in India.

It is the taxpayer who is the objective or the target for the Revenue and, where the taxpayer is a nonresident, the taxpayer's agent is necessarily the target or objective and, as such, is deemed to be the taxpayer for purposes of the ITA.

The ITA specifies the persons who may be treated as agents in relation to a nonresident. These include any person in India: [252]

---

[252] ITA, Sec. 163.

(i) Who is employed by or on behalf of the nonresident;

(ii) Who has any business connection with the nonresident;

(iii) From or through whom the nonresident is in receipt of any income, whether directly or indirectly; or

(iv) Who is the trustee of the nonresident, including also any other person who, whether a resident or nonresident, has acquired by means of a transfer, a capital asset in India.

An agent is a representative taxpayer for purposes of the ITA. [253] An agent is liable to assessment in his own name with respect to the income of the nonresident as if the income is received by or accrued to the agent. The tax is levied on the agent in like manner and to the same extent as it would be leviable on and recoverable from the person represented by the agent. [254]

---

[253] ITA, Sec. 160(1).

[254] ITA, Sec. 161.

The Supreme Court has further held that, in the context in which the expression "business connection" is used in Section 9 of the ITA, there is no warrant for giving a restricted meaning to it. [255] The expression would also encompass professional connections.

---

[255] *Barendra Prasad Ray and others v. I.T.O. and others* (S.C.) 129 I.T.R. 295 [1981].

The courts have as far as possible avoided assigning a definite meaning to the expression "business connection," as it has been considered wholly unwise, if not impossible, to do so. While each court ruling would depend upon facts relevant to the situation concerned, the decisions of the various courts would be illustrative of considerations that have been applied to enable comprehension of the meaning of the expression.

If no operations of business are carried on in India, income accruing or arising abroad through or from any business connection in India may not be deemed to accrue or arise in India. [256]

---

[256] *Commissioner of Income Tax A.P. v. Toshoku Ltd.* (S.C.) 125 I.T.R. 525 [1980].

The following illustrate some of the circumstances in which a business connection in India may (or may not) exist:

(i) Such a connection exists when regular purchases are made in India through a regular agency. However, the mere procurement of orders on behalf of foreign principals does not establish a business connection.

(ii) Where a company in India and a company outside India are both controlled by the same person and there is a flow of business between the two, there is a business connection even if the transaction between them is finalized outside India.

(iii) A solitary loan transaction between a resident and a nonresident does not constitute a business connection between them, even if that loan and interest were to be paid over a period of, for example, five years.

(iv) Where goods are sold by a nonresident through an agency for only one year, a business connection exists if a large number of orders are placed.

(v) A managing agent of a foreign company in India constitutes a business connection.

(vi) In circumstances in which there was regular correspondence between a firm of solicitors in India and a firm of solicitors in London regarding evidence to be adduced in certain suits and fixing hearings when a counsel from London would attend, a business connection was held to exist.

(vii) In circumstances where technical information was provided by a German firm to an Indian firm in Germany, no business connection was held to exist.

(viii) A business connection exists where a nonresident maintains a branch office in India for the purchase and sale of goods, or for transacting other business.

(ix) Normally, when a nonresident deals with an Indian resident on a principal-to-principal basis, such an arrangement *prima facie* negates the existence of any business connection.

(x) When an Indian broker is free to place the orders secured by him with any person he likes and he places his orders with a nonresident taxpayer, the relationship between them is not a business connection.

f. Transfer Pricing

See VIII, below.

g. Avoidance of Tax by Transactions Resulting in Transfer of Income to Nonresidents

Where a transfer of assets is effected in such a manner that any income becomes payable to a nonresident or a person who is resident but NOR, and the transferor acquires any rights by virtue of which he has the power to enjoy such income, either immediately or in the future, the income is deemed to be the income of the transferor.

Where before or after such transfer, the transferor receives or is entitled to receive a capital sum, the payment of which is connected with the transfer, then any income consequent to such transfer constitutes income in the hands of the transferor.

These provisions do not apply in cases where the taxpayer is able to prove that the transfer of assets was not effected for purposes of reducing or avoiding a tax liability of the resident transferor, or where the transaction was a *bona fide* commercial transaction not designed for such purposes. [257]

---

[257] ITA, Sec. 93.

---

h. Avoidance of Tax by Way of Certain Transactions in Securities

When the owner of any securities sells or transfers the securities and buys them (or similar securities) back and, as a result, interest income accrues to a person other than the owner of the securities, the interest income may be assessed to tax as income of the owner. [258]

---

[258] ITA, Sec. 94.

Similarly, when a person who has any beneficial interest in securities, as a result of any transaction in those securities, either receives no income or receives income less than the income that he might have been entitled to but for such transactions, the income is deemed to be income of the person beneficially interested in the securities.

The above provisions do not apply if the taxpayer proves to the satisfaction of the Assessing Officer that there has been no avoidance of income tax, or that the avoidance is exceptional and not systematic, and the taxpayer has not undertaken such transactions for avoidance of tax in any of the three preceding years.

Where any person carrying on a business that consists wholly or partly in dealing in securities buys or acquires any securities and sells back or retransfers the securities or similar securities, and the resultant interest is chargeable to the other person, as set out above, then no account will be taken, in the hands of the first person, of any profit or loss arising from such transaction.

When a person buys or acquires securities or units of mutual funds within a period of three months prior to the record

date fixed for the declaration of dividends or distribution of income with respect to those securities or units, and sells or transfers the securities within a period of three months or sells or transfers units within a period of nine months after the record date, if the dividend or income received or receivable is exempt from tax, the loss, if any, arising from the sale or transfer is ignored to the extent the loss does not exceed the amount of the dividend or interest.

Where:

(i) Any person buys or acquires any units within a period of three months prior to the record date;

(ii) The person is allotted additional units without any payment on the basis of holding the units on that date;

(iii) The person sells or transfers all or any of the units referred to in (i), within a period of nine months after that date while continuing to hold all or any of the additional units referred to in (ii),

the loss, if any, arising to him on account of such purchase and sale of all or any of such units is ignored for purposes of computing his income chargeable to tax, notwithstanding anything contained in any other provisions of the ITA, and the amount of loss so ignored is deemed to be the cost of purchase or acquisition of the additional units referred to in (ii) that are held by him on the date of such sale or transfer.

i. Expenditure Incurred in Relation to Income Not Includible in Total Income

Expenditure incurred by a taxpayer in relation to income that does not form part of total income is not eligible for deduction for purposes of computing taxable income. [259]

---

[259] ITA, Sec. 14A.

The Assessing Officer determines the amount of expenditure incurred in relation to income that does not form part of the total income under the ITA in accordance with such method as may be prescribed, if the Assessing Officer, with regard to the accounts of the taxpayer, is not satisfied with the correctness of the claim of the taxpayer with respect to expenditure in relation to income that does not form part of the taxpayer's total income. These provisions also apply where the taxpayer claims that no expenditure has been incurred by him in relation to income that does not form part of the taxpayer's total income.

4. Categories of Income

a. Salaries

Salary is charged to tax either when it becomes due or when it is received by the taxpayer, whichever is earlier. [260] Salary is defined to include: [261]

---

[260] ITA, Sec. 15.

[261] ITA, Sec. 17(1).

(i) Wages;

(ii) Any annuity or pension;

(iii) Gratuities;

(iv) Fees, commissions, perquisites, or profits in lieu of or in addition to any salary or wages;

(v) Advance salary;

(vi) Payment received with respect to any period of leave not used by an employee;

(vii) The annual accretion to the balance in a recognized provident fund, if the employer's contribution exceeds 12% of the employee's salary or if the interest credited is in excess of 12%;

(viii) The transferred balance in a recognized provident fund to the extent that it is taxable; and

(ix) A contribution made by the central government or any other employer to the account of the employee under a prescribed pension scheme.

Pursuant to an advance ruling, a stock option given by a parent company to the employees of an Indian company that is a wholly owned subsidiary of a foreign company, constitutes salary in the hands of the employees. [262]

[262] **Authority for Advance Rulings (AAR), Advance Rulings Petition No. 15 of 1998.**

As noted above in (iv), the term salary also includes "perquisites" and "profits in lieu of salary." The term "perquisites" includes, among other things:

(i) The value of rent-free accommodation provided by an employer to an employee.

(ii) The value of any concession in rent with respect to accommodation provided by an employer to an employee.

(iii) The value of any benefit or amenity granted or provided free of cost or at a concessional rate in any of the following cases:

(a) By a company to an employee-director;

(b) By a company to an employee who has a substantial interest in the company; or

(c) By an employer (including a company) to an employee to whom the provisions of (a) and (b) do not apply and whose income under the heading "Salaries," exclusive of the value of all benefits or amenities not provided for by way of monetary payment, exceeds Rs.50,000.

Note: **The use of a vehicle provided by an employer for the journey from/to the residence to/from the place of work of an employee is not regarded as a benefit or an amenity as stated above.**

(iv) Any amount paid by an employer with respect to any obligation that, but for such payment, would have been payable by an employee.

(v) Any sum payable by an employer, whether directly or through a fund, other than a recognized provident fund or an approved superannuation fund or a deposit linked insurance fund, to effect an assurance on the life of an employee or to contract for an annuity.

(vi) The value of any specified security or sweat equity shares allotted or transferred, directly or indirectly, by an employer, free of cost or at concessional rate to the taxpayer.

(vii) The amount of any contribution to an approved superannuation fund by an employer with respect to the taxpayer, to the extent it exceeds Rs.100,000.

(viii) The value of any other fringe benefit or amenity that may be prescribed.

Specific rules have been prescribed for determining the value of perquisites (see the Worksheets).

Specified payments/reimbursements made by an employer towards the medical expenses/medical insurance premium of an employee are not considered perquisites, subject to certain conditions.

The following are exempt from tax:

(i) A leave travel concession received by an individual from an employer for himself and his family for proceeding on leave to any place in India (including at the time of retirement), subject to prescribed conditions. This exemption is available with respect to the actual expenditure incurred on such journeys and is available only for two journeys in a block of four calendar years; [263]

(ii) A gratuity, where received under the Payment of Gratuity Act, 1972, to the extent prescribed and, in other cases, to the extent that the gratuity does not exceed half a month's salary for each year of completed service or a sum of Rs.350,000, whichever is less; [264]

(iii) Leave salary up to a maximum of 10 months' salary, with respect to earned leave credited to the employee, if cashed in at the time of retirement or a sum of Rs.300,000, whichever is less; [265]

(iv) Any amount received or receivable by an employee on his or her voluntary retirement, if the scheme of voluntary retirement is drawn up in accordance with prescribed guidelines, to the extent the amount does not exceed Rs.500,000; [266]

(v) Tax paid by an employer on behalf of an employee with respect to income in the nature of a "perquisite" not provided by way of monetary payment; [267]

(vi) Any sum received by an individual under a life insurance policy, including bonus allocations, subject to certain exceptions; [268]

(vii) Any payment from a provident fund to which the Provident Fund Act applies, or the accumulated balance due and payable to an employee from a recognized provident fund, or any payment from an approved superannuation fund; [269]

(viii) Any allowance granted by an employer to an employee to meet the expenditure actually incurred on the payment of rent for residential accommodation occupied by the employee, to the extent prescribed; [270] and

(ix) Any special allowance or benefit, not being in the nature of "perquisite," specifically granted to meet expenses incurred wholly, necessarily and exclusively in the performance of duties of an office or employment of profit, to such extent and in such manner as may be prescribed. [271]

---

[263] ITA, Sec. 10(5).

[264] ITA, Sec. 10(10).

[265] ITA, Sec. 10(10AA).

[266] ITA, Sec. 10(10C).

[267] ITA, Sec. 10(10CC).

[268] ITA, Sec. 10(10D).

[269] ITA, Sec. 10(11)–10(13).

[270] ITA, Sec. 10(13A).

[271] ITA, Sec. 10(14).

Salary earned in India is deemed to accrue or arise in India, even if it is paid outside India or is paid or payable after the contract of employment comes to an end.

Salary payable for services rendered in India, and for a rest period or leave period that is preceded and succeeded by services rendered in India that forms part of the service contract of employment, is regarded as income earned in India. A pension paid abroad is deemed to accrue in India if it is paid with respect to services rendered in India. [272]

---

[272] ITA, Sec. 9(1)(ii).

Salary (excluding allowances and perquisites) paid by the Indian government to an Indian national is deemed to accrue or arise in India, even if the service is rendered outside India. [273]

---

[273] ITA, Sec. 9(1)(iii).

The term "profits in lieu of salary" includes:

(i) The amount of any compensation due to or received by an employee from his employer or former employer at or in connection with the termination of his employment or the modification of the terms and conditions relating thereto;

(ii) Any payment (other than specified exclusions) due to or received by an employee from an employer or a former employer or from a provident or other fund, to the extent it does not consist of contributions made by the employee or interest on such contributions or any sum received under a Keyman insurance policy including the sum allocated by way of bonus on such policy; or

(iii) Any amount due to or received by an employee from an employer either before the commencement of employment or after the cessation of employment. [274]

---

[274] ITA, Sec. 17(3).

Any salary received by a partner of a firm is not taxed as "salary" but as income from a business or profession. [275]

---

[275] ITA, Sec. 28(v).

---

b. Income from House Property

The annual value of property consisting of any buildings or land appurtenant thereto of which the taxpayer is the owner (excluding portions of such property occupied by the taxpayer for purposes of a business or profession the profits of which are subject to tax) is chargeable to tax under the head "income from house property." [276]

[276] ITA, Sec. 22.

The annual value for these purposes is:

(i) The sum for which the property might reasonably be expected to let from year to year;

(ii) Where the property or any part of the property is let and the actual rent received or receivable by the owner is in excess of the sum referred to above in (i), the amount so received or receivable; or

(iii) Where the property or any part of the property is let and was vacant during the whole or any part of the tax year and, owing to such vacancy, the actual rent received or receivable by the owner is less than the sum referred to above in (i), the amount so received or receivable.

Where the house property is occupied by the owner as his or her own residence or may not actually be occupied by the owner owing to his or her employment, business or profession being carried on at any other place and the owner having to reside at that other place in a building not belonging to him or her, the annual value of the house will be taken to be nil if the following conditions are satisfied:

(i) The property or a part thereof is not actually let during the whole or any part of the year; and

(ii) No other benefit is derived therefrom.

However, where the property consists of more than one house:

(i) The annual value of only one of the houses will be taken as nil, at the option of the taxpayer; and

(ii) The annual value of the other house(s) will be determined as set out above.

Taxes levied by any local authority with respect to the property will be deducted from the annual value only when such taxes are actually paid by the owner. [277]

[277] ITA, Sec. 23.

The following deductions are allowed from income under the head "income from house property:" [278]

[278] ITA, Sec. 24.

(i) A sum equal to 30% of the annual value; and

(ii) Where the property was acquired, constructed, repaired, renewed or reconstructed with borrowed capital after April 1, 1999, and the acquisition, etc. is completed within three years from the end of the tax year in which the capital was borrowed, the amount of interest paid on that capital not exceeding Rs.150,000.

Unrealized rent [279] or arrears of rent [280] with respect to property that are received in a subsequent tax year will be taxable in that tax year as "Income from House Property" in the hands of the taxpayer, even if the taxpayer is no longer the owner of the property in that tax year.

[279] ITA, Sec. 25AA.

[280] ITA, Sec. 25B.

Co-owners of property having definite and ascertainable shares in the property will be subject to tax on the income from the property, as set out above, in proportion to their respective shares. [281]

[281] ITA, Sec. 26.

c. Income from Business or Profession

(1) General

The profits and gains of a business or profession include:

(i) The profits and gains of any business or profession carried on by the taxpayer during the taxable year.

(ii) Any compensation or other payment due to or received by:

(a) Any person, by whatever name called, managing the whole or substantially the whole of the affairs of an Indian company, at or in connection with the termination of his management or the modification of the terms and conditions relating thereto;

(b) Any person, by whatever name called, managing the whole or substantially the whole of the affairs in India of any other company, at or in connection with the termination of his office or the modification of the terms and conditions relating thereto;

(c) Any person, by whatever name called, holding an agency in India for any part of the activities relating to the business of any other person, at or in connection with the termination of the agency or the modification of the terms and conditions relating thereto; or

(d) Any person, for or in connection with the vesting in the Government, or in any corporation owned or controlled by the Government, under any law for the time being in force, of the management of any property or business.

(iii) Income derived by a trade, professional or similar association from specific services performed for its members.

(iv) Profits on the sale of a license under the Import Control Order.

(v) Cash assistance received or receivable by any person against exports under any scheme of the government.

(vi) Customs or excise duty repaid or repayable as duty drawback.

(vii) Any sum, whether received or receivable, in cash or kind, on account of any capital asset (other than land, goodwill or a financial instrument) being demolished, destroyed, discarded or transferred, if the whole of the expenditure on the capital asset was allowed as a deduction under Section 35AD of the ITA (see 5, f, below).

(viii) Any profit on the transfer of a Duty Entitlement Pass Book (DEPB) scheme under a duty remission scheme.

(ix) Any profit on the transfer of a Duty Free Replenishment Certificate (DFRC) scheme under a Duty remission scheme.

(x) The value of any benefit or perquisite, whether or not convertible into money, arising from a business or the exercise of a profession.

(xi) Any interest, salary, bonus, commission or other payment due to or received by a partner from a firm, subject to certain limits.

(xii) Any sum, whether received or receivable in cash or kind, under an agreement for:

(a) Not carrying out any activity in relation to any business; or

(b) Not sharing any know-how, patent, copyright, trademark, license, franchise or any other business or commercial right of a similar nature or information or any technique likely to assist in the manufacture or processing of goods or the provision of services. [282]

Clause (a) does not apply to:

- **Any sum, whether received or receivable, in cash or kind, on account of the transfer of the right to manufacture, produce or process any article or thing or the right to carry on any business that is chargeable under the head "capital gains;" or**

- **Any sum received as compensation from the multilateral fund of the Montreal Protocol on Substances that Deplete the Ozone layer under the United Nations Environment Programme, in accordance with the terms of the agreement entered into with the Government of India.**

For purposes of the above:

• The term "agreement" is defined to include any arrangement or understanding or action in concert;

• Whether or not such arrangement, understanding or action is formal or in writing;

• Whether or not such arrangement, understanding or action is intended to be enforceable by legal proceedings; and

• The term "service'' is defined to mean a service of any description that is made available to potential users and includes the provision of services in connection with business of any industrial or commercial nature such as accounting, banking, communication, the conveying of news or information, advertising, entertainment, amusement, education, financing, insurance, chit funds, real property, construction, transport, storage, processing, the supply of electrical or other energy, boarding and lodging.

(xiii) Any sum received under a key man insurance policy, including the sum allocated by way of bonus on such a policy.

---

[282] ITA, Sec. 28.

Note 1: **When speculative transactions carried on by the taxpayer are such as to constitute a business, then such "speculative business" is treated as distinct and separate from the taxpayer's other business.**

Note 2: **The Supreme Court has held that, where a transaction is not in the taxpayer's regular line of business, but is an isolated transaction, the onus is on the Revenue Authorities to prove that the solitary transaction is an adventure in the nature of trade. [283]**

---

[283] *Saroj Kumar Mazumdar v. CIT* (S.C.) 37 I.T.R. 242 [1959].

The following are the important deductions and allowances specified in the ITA that are available to a taxpayer in computing profits and gains from a business or profession:

(i) Rent, rates, taxes, repairs and insurance with respect to buildings;

(ii) Repairs to and the insurance of machinery, plant and furniture;

(iii) Depreciation allowance;

(iv) Contributions to the Site Restoration Fund;

(v) Expenditure on scientific research;

(vi) Amortization of capital expenditure for acquiring a license to operate telecommunication services;

(vii) Expenditure on eligible projects or schemes;

(viii) Expenditure with respect to a specified business;

(ix) Expenditure on payments to associations, etc., for carrying out rural development programs;

(x) Amortization of preliminary expenses;

(xi) Amortization of expenditure in the case of amalgamation or demerger;

(xii) Amortization of expenditure incurred under the Voluntary Retirement Scheme;

(xiii) Amortization of expenditure on prospecting for the development of certain minerals; and

(xiv) Expenditure of a revenue nature incurred wholly and exclusively for purposes of the business. [284]

---

[284] ITA, Secs. 30 to 35E, 36 and 37.

The above list is not exhaustive. Only items of loss or expenditure incurred or expended wholly and exclusively for purposes of the business are allowable as deductions in computing taxable business income.

Note: **Where any building, machinery, plant or furniture is not exclusively used for purposes of the business or profession of the taxpayer, the Assessing Officer may determine the proportion attributable to use for purposes of the business or profession and the deductions will be restricted accordingly. [285]**

[285] ITA, Sec. 38.

It should be noted that it is not necessary that the primary motive for the expenditure be directly related to the earning of income. Expenditure incurred not with a view to obtaining direct and immediate benefit but for the purposes of commercial expediency and in order to facilitate the carrying on of the business is expenditure laid out wholly and exclusively for the purposes of the business. [286]

[286] *See Meenakshi Mills Ltd. v. CIT* (S.C.) 63 I.T.R. 207 [1967].

To be allowable as a deduction an expense should be incurred for the "purpose of business," this expression having a wider import than the term "purpose of earning profits." Its range is wide and encompasses not only the day-to-day running of the business but also the rationalization of its administration and the modernization of its machinery. It may also include measures for the protection of the business, and for the protection of its assets and property from expropriation, coercive process or assertion of hostile title. The expression may also include the payment of statutory dues and taxes imposed as a precondition for commencing or carrying on the business, and many other acts incidental to the carrying on of the business. The purpose must be the purpose of the business, that is to say, the expenditure must be for the carrying on of the business and the taxpayer must incur it in his capacity as a person carrying on the business. It may not include sums spent by the taxpayer as an agent of a third party, whether the origin of the agency is voluntary or statutory. [287]

[287] *CIT v. Malayalam Plantations Ltd.* (S.C.) 53 I.T.R. 140 [1964].

In determining whether an item may or may not be deducted from profits, it is necessary first to enquire whether the deduction is expressly or by necessary implication prohibited by the ITA, and then, if it is not so prohibited, to consider whether it is of such a nature that it should be charged against income in the computation of profits and gains. [288]

[288] *Badridas Daga v. CIT* (S.C.) 53 I.T.R. 140 [1964].

In the case of a partnership firm carrying on a business or profession, the following deductions are not admissible:

(i) Payments of salary, bonus, commission or remuneration ("remuneration") to a partner who is not a working partner;

(ii) Payments of remuneration or interest to a working partner that are not authorized by a written partnership agreement;

(iii) Payments of interest to a partner at a rate exceeding 12% per annum; and

(iv) Payments of remuneration to working partners authorized by a written partnership agreement if the total amount exceeds:

- On the first Rs.300,000 of the book-profit or in the case of a loss: Rs.150,000 or 90% of the book-profit, whichever is more; and
- On the balance of the book-profit: the rate of 60%.

For this purpose, "working partner" means a person who is fully engaged in conducting the affairs of the business or profession of which that person is a partner. [289]

[289] ITA, Sec. 40(b).

(2) Statutory Liabilities

A deduction with respect to the following is available only if the amount in question is actually paid during the year (although if the amount is paid before the due date for furnishing the return of income even if this is after the year-end, a deduction may be claimed for the year if proof of payment is attached to the return of income): [290]

[290] ITA, Sec. 43B.

(i) Any sum payable as tax, duty, cess or fee by whatever name called under any law in force at the time;

(ii) Any sum payable by the taxpayer as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of his employees;

(iii) Any sum payable as bonus or commission to employees for services rendered;

(iv) Any sum payable as interest on any loan or borrowing from a public financial institution, state financial corporation or state industrial investment corporation in accordance with the terms and conditions governing such loan or borrowing;

(v) Any sum payable as interest on any loan or advance from a scheduled bank in accordance with the terms and conditions governing such loan or advance; and

(vi) Any sum payable by an employer to an employee in lieu of any leave to the employee's credit.

(3) Maintenance of Accounts

Taxpayers carrying on legal, medical, engineering, accounting, technical consulting, interior decorating or other specified professions are required to maintain prescribed books of account and related documents.

Taxpayers carrying on businesses or professions other than the professions specified above are required to maintain books of account:

(i) If the income from the business or profession exceeds Rs.120,000 or the total sales, turnover, or gross receipts of the business or profession exceed Rs.1 million in any one of the three years immediately preceding the tax year;

(ii) Where the business or profession is newly set up in the previous year and the income is likely to exceed Rs.120,000, or the sales, turnover or gross receipts are likely to exceed Rs.1 million during such tax year; and

(iii) Where the profits and gains from a business are deemed profits and gains of the taxpayer under the special provisions applicable (see VI, C, below) and the taxpayer has claimed his income to be lower than the deemed profits and gains as so provided, or the income exceeds the maximum amount not chargeable to tax, where specified, during the tax year concerned. [291]

---

[291] **ITA, Sec. 44AA.**

Books of account are not required to be maintained in the case of nonresidents that earn profits and gains from a business of operating ships or aircraft.

(4) Auditing of Accounts

Under the ITA, it is obligatory for any person to get his accounts audited if that person: [292]

(i) Carries on business and his total sales turnover or gross receipts, as the case may be, exceed Rs. 6 million in any previous year;

(ii) Carries on a profession and his gross receipts exceed Rs. 1.5 million in any previous year; or

(iii) Carries on business under the special provisions applicable (see VI, C, below) and claims his income to be lower than the deemed profits and gains as provided, and his income exceeds the maximum amount not chargeable to tax in any previous year.

---

[292] **ITA, Sec. 44AB.**

Taxpayers are required to furnish a tax audit report from an accountant in the prescribed form before September 30 of the relevant assessment year.

The audit under the ITA is in addition to any audit that may be required under any other statute.

Accounts are not required to be audited in the case of nonresidents that earn profits and gains from a business of operating ships or aircraft.

(5) Method of Accounting

Income of a taxpayer chargeable under the head "Income from Business or Profession" or under the head "Income from Other Sources" must be computed in accordance with either the cash (receipt) basis or the mercantile system (accrual basis) of accounting regularly followed by the taxpayer. For this purpose, the central government may give notice of accounting standards to be followed by any particular class of taxpayer or with respect to any particular class of income.

Where the Assessing Officer is not satisfied with the correctness or completeness of the accounts of the taxpayer, or

where the method of accounting or the notified accounting standards have not been regularly followed, the Assessing Officer may make a best judgment assessment. [293]

[293] **ITA, Sec. 145.**

Notwithstanding the above:

(i) The valuation of purchases and sales of goods and inventory for purposes of determining income chargeable under the head "Profits and gains of business or profession" must be:

- **In accordance with the method of accounting regularly employed by the taxpayer; and**
- **Adjusted to include the amount of any tax, duty, cess or fee actually paid or incurred by the taxpayer to bring the goods to the place of their location and to their condition as of the date of valuation.**

(ii) Interest received by a taxpayer on compensation or on enhanced compensation, will be deemed to be the income of the year in which it is received. [294]

[294] **ITA, Sec. 145A.**

It should be noted that the taxability of a receipt depends upon the method of accounting regularly followed by the taxpayer. A clear distinction is drawn between the method of accounting adopted and the actual entries in the accounts. The method of accounting, and not the actual entries in the accounts, is the relevant factor. [295]

[295] ***CIT v. Chunilal V. Mehta & Sons P. Ltd.*** **(S.C.) 82 I.T.R. 54 [1971].**

It should further be noted that the mercantile (accrual) system of bookkeeping differs greatly from the cash system of bookkeeping. Under the mercantile system, postponement of the date of payment is immaterial and does not affect the accrual of income. The fact that the amount is not subsequently received does not detract from or affect the accrual of income, though nonreceipt thereof, in appropriate circumstances, may be valid grounds for claiming a deduction. [296]

[296] ***Morvi Industries Ltd. v. CIT*** **(S.C.) 82 I.T.R. 835 [1971].**

d. Capital Gains

Profits and gains arising from the transfer of capital assets are charged to tax as capital gains in the year in which the transfer is effected. [297]

[297] **ITA, Sec. 45(1).**

Profits and gains arising from the receipt of any money or other asset from an insurer under a contract of insurance on account of damage to, or destruction of, any capital asset, as a result of:

(i) An act of nature;

(ii) Riot or civil disturbance;

(iii) Accidental fire or explosion; or

(iv) Action by an enemy or action taken in combating an enemy,

are charged to tax as capital gains in the year in which the money or the asset was received. For this purpose, the value of the money or the fair market value of the asset on the date of receipt will be considered to be the full value of the consideration. [298]

[298] **ITA, Sec. 45(1A).**

Profits or gains arising from the transfer by way of conversion by the owner of a capital asset into, or its treatment by him as, stock-in-trade of a business carried on by him will be chargeable to income tax as his income of the previous year in which such stock-in-trade is sold or otherwise transferred by him. The fair market value of the asset on the date of such conversion or treatment will be deemed to be the full value of the consideration received or accruing as a result of the transfer of the capital asset. [299]

[299] ITA, Sec. 45(2).

Where any person has had, at any time during the previous year, any beneficial interest in any securities, any profits or gains arising from a transfer made by the depository of or a participant in such beneficial interest in securities will be chargeable to income tax as the income of the beneficial owner of the previous year in which the transfer took place and will not be regarded as income of the depository who is deemed to be the registered owner of the securities. The cost of acquisition and the period of holding of any securities will be determined based on the first-in-first-out (FIFO) method. [300]

[300] ITA, Sec. 45(2A).

Profits and gains arising from the buy-back of shares or other specified securities by a company are chargeable to capital gains tax in the year in which the shares or other specified securities are purchased by the company. Capital gains tax is chargeable on the difference between the value of the consideration received by the shareholder or the holder of the specified securities and the cost of acquisition. [301]

[301] ITA, Sec. 46A.

A capital asset is defined as "property of any kind" but specifically excludes stock-in-trade (inventory) held for purposes of a business, personal effects (excluding jewelry, archaeological collections, drawings, paintings, sculptures and any work of art), agricultural land situated in specified areas and certain securities issued by the central government. [302]

[302] ITA, Sec. 2(14).

"Transfer" in relation to a capital asset includes:

(i) The sale, exchange or relinquishing of the asset;

(ii) The extinguishing of any rights therein;

(iii) The compulsory acquisition of the asset under any law;

(iv) The conversion of the asset into, or the treatment of the asset as, stock- in-trade (inventory) by the owner of the asset;

(v) The maturity or redemption of a zero-coupon bond;

(vi) Where the asset is real property, any transaction involving allowing the possession of the real property to be taken or retained in part performance of a contract of the kind referred to in Section 53A of the Transfer of Property Act, 1882; or

(vii) Where the asset is real property, any transaction that has the effect of transferring or enabling the enjoyment of the real property. [303]

[303] ITA, Sec. 2(47).

Some examples of transactions that he ITA does not recognize as transfers of capital assets are:

(i) The distribution of the assets of a company to its shareholders on liquidation. However, any money or other assets received by a shareholder on the liquidation of a company will be chargeable to tax as capital gain with respect to the money so received or the market value of the other assets on the date of distribution (as reduced by the amount of the dividend referred to below) and the sum so arrived at will be deemed to be the full value of the consideration for purposes of computing the capital gains. [304] A distribution made on the liquidation of an Indian company results in a dividend (not a capital gain) to the extent the distribution is attributable to the accumulated profits of the company, even if the accumulated profits were capitalized and bonus shares issued before the liquidation; [305]

(ii) Any transfer under a gift, will or irrevocable trust. [306] However, transfers under a gift or an irrevocable trust of capital assets, being shares, debentures or warrants allotted by a company directly or indirectly to its employees under a Employees' Stock Option Plan or Scheme in accordance with specified guidelines, are recognized as transfers of capital assets; and

(iii) The transfer of capital assets by a company to its wholly-owned Indian subsidiary company or by a

wholly-owned subsidiary company to its Indian holding company. [307]

---

[304] ITA, Sec. 46(1).

[305] ITA, Sec. 2(22)(c).

[306] ITA, Sec. 47(iii).

[307] ITA, Sec. 47(iv) and (v).

In the case of the intercompany transfers referred to above, the transferee company is entitled to depreciation only on the written-down value of the asset in the hands of the transferor company, irrespective of the actual consideration paid by it. [308]

---

[308] ITA, Explanation 6 to Sec. 43(1).

Also, if within eight years of such transfer:

- The transferee company converts the capital asset into, or treats it as, stock-in-trade (inventory) of its business; or
- The holding company ceases to own the entire share capital of the subsidiary,

the exemption is withdrawn and the capital gain becomes taxable in the tax year in which the transfer takes place. In this event, the cost of the acquisition of the asset to the transferee company is the cost for which the asset was acquired by it. A completed assessment may be rectified to withdraw the exemption from capital gains; [309]

---

[309] ITA, Sec. 47A(1).

(iv) The transfer of a capital asset, in a scheme of amalgamation, by an amalgamating company to an amalgamated Indian company; [310]

(v) The transfer of a capital asset, in a scheme of amalgamation, consisting of shares held in an Indian company, by an amalgamating foreign company to an amalgamated foreign company, if at least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company and the transfer does not attract tax on capital gains in the country in which the amalgamating company is incorporated; [311]

(vi) Any transfer, in a scheme of amalgamation of a banking company with a banking institution sanctioned and brought into force by the central government, of a capital asset by the banking company to the banking institution; [312]

(vii) Any transfer, in a demerger, of a capital asset by a demerged company to the resulting Indian Company; [313]

(viii) Any transfer, in a demerger, of shares in an Indian company by a demerged foreign company to the resulting foreign company, if shareholders holding at least 75% in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company and the transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated; [314]

(ix) Any transfer or issue of shares by the resulting company, in a scheme of demerger, to the shareholders of a demerged company, if the transfer or issue is made in consideration of the demerger of the undertaking; [315]

(x) The transfer by a shareholder, in a scheme of amalgamation, of shares held by him in an amalgamating company in consideration of the allotment to him of shares in an amalgamated Indian company; [316]

(xi) The transfer of capital assets in the form of bonds or Global Depository Receipts (GDRs) made outside India by a nonresident to another nonresident; [317]

(xii) The transfer of an archaeological, scientific or art collection, a book manuscript, drawings, paintings, etc., to the government, a university, a national museum, a national art gallery or any other specified

institution; [318]

(xiii) Any transfer by way of the conversion of bonds or debentures, debenture-stock or deposit certificates in any form, of a company into shares or debentures of the company; [319]

(xiv) Any transfer by way of the conversion of bonds, held by a nonresident, issued in accordance with a scheme notified by the central government or bonds of a Public Sector company acquired in foreign currency by a nonresident from the central government, into shares or debentures of the company; [320]

(xv) Any transfer of a capital asset, being land of a sick industrial company; [321]

(xvi) Any transfer of a capital asset or intangible asset by a firm to a company as a result of the succession of the firm by a company in the business carried on by the firm, or any transfer of a capital asset to a company in the course of the demutualization or corporatization of a recognized stock exchange in India as a result of which an association of persons or body of individuals is succeeded by such company, if certain conditions are fulfilled; [322]

(xvii) Any transfer of a capital asset, being a membership right held by a member of a recognized stock exchange in India for the acquisition of shares and trading or clearing rights acquired by the member in that recognized stock exchange in accordance with a scheme for demutualization or corporatization approved by the Securities Exchange Board of India (SEBI); [323]

(xviii) Any transfer of a capital asset or intangible asset by a private company or unlisted public company to a limited liability partnership or any transfer of a share or shares held in such a company by a shareholder as a result of the conversion of the company into a limited liability partnership, in accordance with the provisions of the Limited Liability Partnership Act, 2008, if certain conditions are fulfilled; [324]

(xix) Where a sole proprietary concern is succeeded by a company in the business carried on by it and, as a result, the sole proprietary concern sells or otherwise transfers any capital asset or intangible asset to the company, if certain conditions are fulfilled; [325]

(xx) Any transfer in a scheme for the lending of any securities under an agreement or arrangement that the taxpayer has entered into with the borrower of the securities and that is subject to the guidelines issued by the SEBI; [326] **and**

(xxi) Any transfer of a capital asset in a reverse mortgage transaction under a scheme made and notified by the central government. [327]

---

[310] **ITA, Sec. 47(vi).**

[311] **ITA, Sec. 47(via).**

[312] **ITA, Sec. 47 (viaa).**

[313] **ITA, Sec. 47(vib).**

[314] **ITA, Sec. 47(vic).**

[315] **ITA, Sec. 47(vid).**

[316] **ITA, Sec. 47(vii).**

[317] **ITA, Sec. 47(viia).**

[318] **ITA, Sec. 47(ix).**

[319] **ITA, Sec. 47(x).**

[320] **ITA, Sec. 47(xa).**

[321] **ITA, Sec. 47(xii).**

[322] **ITA, Sec. 47(xiii).**

[323] **ITA, Sec. 47(xiiia).**

[324] **ITA, Sec 47(xiiib).**

[325] **ITA, Sec. 47(xiv).**

[326] **ITA, Sec. 47(xv).**

[327] ITA, Sec. 47(xvi).

However, in the case of the conversion of a partnership firm or a private limited company into a limited liability partnership (LLP), the ITA does not provide for any specific exemptions arising out of such conversions. Conversions from a general partnership firm into an LLP will have no tax implications if the rights and obligations of the partners remain the same after conversion and if there is no transfer of any asset or liability after conversion. However, if there is a violation of these conditions, Section 45, dealing with capital gains, will apply (see above).

Capital gains are classified as long-term capital gains if they arise from the transfer of capital assets held:

(i) In the case of shares in a company and other securities listed on a recognized stock exchange in India, units of specified mutual funds, or zero coupon bonds, for a period of 12 months or more; and

(ii) In the case of other assets, for a period of 36 months or more.

Capital gains arising on the transfer of assets held for a shorter period are classified as short-term capital gains. [328]

[328] ITA, Sec. 2(29A) and Sec. 2(42A).

Capital gains are computed after deducting from the full value of the consideration, the transfer expenses and the costs of acquiring or improving the asset transferred. Capital gains arising from the transfer of a long-term capital asset (other than capital gains arising to a nonresident from the transfer of shares in or debentures of an Indian company, as referred to below) are computed after deducting from the full value of the consideration, the transfer expenses and the indexed cost of acquiring or improving the asset transferred.

The cost-of-inflation indices for the revision of costs are announced by the government (see the Worksheets). The benefit of cost indexation is not available in the case of bonds and debentures other than capital indexed bonds issued by the government. Where the capital asset became the property of the taxpayer before April 1, 1981, the taxpayer has the option of substituting for the cost of acquisition, the fair market value of the asset on that date. The cost-of-inflation index is applied to the substituted value.

In the case of a taxpayer who is a nonresident, capital gains arising from transfer of capital assets in the form of shares or debentures of an Indian company are required to be computed by converting the cost of acquisition, expenses incurred for the transfer and the sale consideration into the same foreign currency as was utilized for the purchase of the shares or debentures. The capital gains so computed in such foreign currency are to be reconverted into Indian currency on the date of transfer. [329]

[329] ITA, Sec. 48.

Where consideration declared to be received or accruing as a result of the transfer of land or buildings, or both, is less than the value adopted or assessed or assessable by any state government authority for purposes of the payment of stamp duty with respect to such transfer, the value so adopted or assessed or assessable is deemed to be the full value of the consideration and capital gains must be computed accordingly.

However, where the taxpayer claims that the value adopted or assessed or assessable for stamp duty purposes exceeds the fair market value of the property as of the date of transfer and the taxpayer has not disputed the value so adopted or assessed or assessable before any authority or any court or the High Court, the Assessing Officer may refer the valuation of the relevant asset to a Valuation Officer. If the fair market value determined by the Valuation Officer is more than the value adopted or assessed for stamp duty purposes, the Assessing Officer will not adopt such fair market value but will take the consideration to be the value adopted or assessed for stamp duty purposes.

If the value adopted or assessed or assessable for stamp duty purposes is revised in any appeal, revision or reference, under stamp duty law, the assessment will be amended to recompute the capital gains by taking the revised value as the full value of the consideration. [330]

[330] ITA, Sec. 50C.

Long-term capital gains arising from the transfer of equity shares in a company and units of equity-oriented mutual funds are exempt from tax if the transaction is chargeable to securities transaction tax. [331]

[331] ITA, Sec. 10(38).

Short-term capital gains arising from the transfer of equity shares in a company and units of equity-oriented mutual funds are chargeable to tax at the rate of 15% if the transaction is chargeable to securities transaction tax. [332]

[332] ITA, Sec. 111A.

The following long-term capital gains are either fully or partially exempt:

(i) To the extent specified (see Note 1, below), gains on the transfer of residential premises owned by an individual, if the individual, within one year before or two years after the date on which the transfer took place, purchases or, within a period of three years after that date, constructs, a residential house (the "new asset") and pending such purchase or construction, the amount is deposited in a notified scheme with a bank by the due date for filing the return of income; [333]

(ii) To the extent specified (see Note 1 below), gains on the transfer of land used in the two years preceding the transfer for agricultural purposes and owned by an individual, if the individual purchases any other land for agricultural purposes within two years from the transfer and pending such investment, the amount is deposited in a notified scheme with a bank by the due date for filing the return of income; [334]

(iii) To the extent specified (see Note 3 below), gains on the transfer of a long-term capital asset (the "original asset"), if the whole or part of the capital gain not exceeding Rs.5 million is invested within six months after the date of the transfer in a long-term specified asset (the "new asset"). Where the new asset is transferred or otherwise converted into money at any time within a period of three years from the date of acquisition, the capital gains arising on the transfer of the original asset and exempted from tax will be taxed as long-term capital gains in the tax year in which the transfer or conversion took place; [335]

(iv) To the extent specified (see Note 1 below), gains on the transfer, by way of compulsory acquisition under any law, of a capital asset, being land or building or any rights therein forming part of an industrial undertaking used by the taxpayer for a business and owned by the taxpayer (the "original asset"), if the taxpayer has within three years from such transfer purchased any other land or building or any right therein or constructed a building for shifting, reestablishing or setting up another industrial undertaking, and pending such purchase or construction, the amount is deposited in a notified scheme with a bank by the due date for filing the return of income; [336]

(v) To the extent specified (see Note 2, below), gains on the transfer by an individual of any long-term capital asset other than house property (the "original asset") if the individual, within one year before or two years after the date on which the transfer took place, purchases, or within a period of three years after that date constructs, a residential house (the "new asset") and pending such purchase or construction, the amount is deposited in a notified scheme with a bank by the due date of filing the return of income. This exemption is not available where a taxpayer:

- **Owns more than one residential house, other than the new asset, on the date of transfer of the original asset; or**
- **Purchases any residential house, other than the new asset, within a period of one year after the date of transfer of the original asset; or**
- **Constructs any residential house, other than the new asset, within a period of three years after the date of transfer of the original asset; and**
- **The income from such residential house, other than the one residential house owned on the date of transfer of the original asset, is chargeable under the head "Income from house property;" [337] and**

(vi) To the extent specified (see Note 1, below), gains on the transfer of a capital asset, being machinery or plant, or a building or land (or any rights therein) used for purposes of the business of an industrial undertaking in an urban area (the "original asset") effected in the course of, or in consequence of the shifting of the industrial undertaking to any Special Economic Zone (SEZ), if the taxpayer has within a period of one year before or three years after the date of such transfer:

- **Purchased machinery or plant for purposes of the business of the industrial undertaking in the SEZ to which the undertaking is shifted;**
- **Acquired a building or land or constructed a building for purposes of his business in the SEZ;**
- **Shifted the original asset and transferred the establishment of such undertaking to the SEZ; and**
- **Incurred expenses on such other purposes as may be specified in a scheme drawn up by the central government for this purpose (such costs and expenses being referred to as the "new asset") and pending such purchase, acquisition, shifting and incurring of expenses, the amount is deposited in a notified scheme with a bank by the due date for filing the return of income. [338]**

[333] ITA, Sec. 54.

[334] ITA, Sec. 54B.

[335] ITA, Sec. 54EC.

[336] ITA, Sec. 54D.

[337] ITA, Sec. 54F.

[338] ITA, Sec. 54GA.

***Note 1*: If the amount of the capital gains is greater than the cost of the new asset, the difference between the amount of capital gain and the cost of the new specified asset will be chargeable to tax as capital gains. If the amount of the capital gains is less than or equal to the cost of the new asset, the entire capital gains will be exempt from tax. In the event the new asset is transferred or sold within a period of three years from the date of purchase or construction, for purposes of computing the capital gains on the transfer or sale of the new asset, the cost of acquisition will be taken as zero or reduced by the amount of capital gain not charged to tax, as the case may be.**

***Note 2*: If the cost of the new asset is not less than the net consideration with respect to the original asset, the entire capital gains are exempt from tax. If the cost of the new asset is less than the net consideration with respect to the original asset, the amount of capital gains exempt from tax will be the amount that bears to the entire capital gains the same proportion as the cost of the new asset bears to the net consideration.**

***Note 3*: If the cost of the new asset is not less than the capital gains arising from the transfer of the original asset, the entire capital gains are exempt from tax. If the cost of the new asset is less than the capital gains arising from the transfer of the original asset, the amount of capital gains exempt from tax will be the amount that bears to the entire capital gains the same proportion as the cost of the new asset bears to the whole of the capital gains.**

Depreciation is available on assets used for business purposes. The ITA contains separate provisions for the computation of capital gains in the case of depreciable assets, as follows:

(i) The excess is deemed to be a short-term capital gain where the full value of the consideration received or accruing as a result of the transfer of a block of depreciable assets by a taxpayer during a year exceeds the aggregate of the following:

- **Expenditure incurred wholly or exclusively in connection with such transfer or transfers;**
- **The written-down value of the block of assets at the beginning of the previous year; and**
- **The actual cost of any asset falling within the block of assets acquired during the previous year.**

(ii) Where any block of assets ceases to exist as such, for the reason that all the assets in the block are transferred during the tax year, the cost of acquisition of the block of assets will be the written down value of the block of assets at the beginning of the tax year, as increased by the actual cost of any asset falling within the block of assets acquired by the taxpayer during the previous year, and the income received or accruing as a result of such transfer or transfers will be deemed to be capital gains arising from the transfer of short-term capital assets.

(iii) Profits and gains arising from a slump sale are charged to long-term capital gain tax in the year in which the transfer takes place. However, profits or gains arising from the transfer under a slump sale of any capital asset being one or more undertakings owned or held by a taxpayer for not more than 36 months preceding the date of transfer are deemed to be capital gains arising from the sale of a short-term capital asset.

For these purposes, the net value of a capital asset that is an undertaking or division is the cost of acquisition plus any cost of improvement. The net value may not be adjusted for cost inflation. For purposes of computing the net value, the value of total assets will be:

- **In the case of depreciable assets, the written down value of the block of assets determined in accordance with the provisions of the ITA;**
- **In the case of other assets, the book value of such assets; and**
- **In the case of capital assets with respect to which a 100% deduction has been claimed under section 35AD of the ITA (see 5, f, below), zero.**

Every taxpayer, in the case of a slump sale, will furnish a report from an accountant in the prescribed form along with the return of income. [339]

[339] ITA, Sec. 50B.

Surplus arising on the sale of self-generated assets is not chargeable to tax, except that surplus arising on the disposal of: the goodwill of a business, or a trademark or brand name associated with a business; tenancy rights; stage carriage permits; loom hours; the right to manufacture, produce or process any article or thing; or any entitlement to subscribe to any additional financial assets by virtue of the holding of any share or other security, is taxable. The cost of acquisition of such assets, in the case of acquisition by the taxpayer by purchase from a previous owner, is their purchase cost, and, in other cases, is deemed to be zero. The cost of any financial asset allotted to the taxpayer without any payment and based on his holding of any other financial asset (a stock dividend) is taken as zero for purposes of computing the capital gain on the sale of the financial asset in the case of such a taxpayer. The period of holding of such a financial asset is reckoned from the date of allotment. [340]

[340] ITA, Sec. 55.

e. Income from Other Sources

(1) General

Income that does not specifically fall under any one of the four categories of income (i.e., salary, income from house property, profits and gains of a business or profession, and capital gains) is to be computed and taxed under the category "income from other sources." [341] Where an item falls specifically under one head, it has to be charged under that head and no other. If for any reason, the computation machinery fails, it is not open to the income tax authorities to assess the income under the head "income from other sources." [342]

[341] ITA, Sec. 56(1).

[342] *United Commercial Bank Ltd. v. CIT* (S.C.), 32 I.T.R. 688.

The following types of income are taxed under the category "income from other sources:" [343]

[343] ITA, Sec. 56(2).

(i) Dividends.

Comment: Dividends on securities held as stock-in-trade (inventory) will fall under the head "profits and gains of business or profession." [344]

(ii) Winnings from lotteries, races, card games, and any other games of any sort or form, and gambling of any nature.

(iii) The following types of income, if not taxed under the category "profits and gains of business or profession:"

- Any sum received by the taxpayer from employees as a contribution to a fund for the welfare of employees;
- Interest income;
- Income from leasing machinery, plant or furniture;
- Income from leasing machinery, plant or furniture along with buildings, where the leasing of the buildings is inseparable from the leasing of the plant or machinery; and
- Income received under a "key man" insurance policy, including the sum allocated by way of bonus on such policy;

(iv) In the case of an individual or a HUF:

— Any amount received for no consideration that exceeds Rs.50,000;

— The stamp duty value of any real property received without consideration, the stamp duty value of which exceeds Rs.50,000;

— Any property, other than real property:

(I) For no consideration, the aggregate fair market value of which exceeds Rs.50,000 (the taxable income is the whole of the aggregate fair market value of the property);

(II) For consideration that is less than the aggregate fair market value of the property by an amount exceeding Rs.50,000 (the taxable income is the aggregate fair market value of the property that exceeds the consideration).

---

[344] ***Bengal & Assam Investors Ltd. v. CIT*** **(S.C.) 59 I.T.R. 547 [1966].**

The amount received from specified relatives, or on the occasion of the marriage of the individual, by way of inheritance or on contemplation of the death of the payer, or from any local authority or specified fund, foundation, university, educational institution, hospital, medical institution or trust, is not to be included as income.

(v) Where a firm or a company in which the public is not substantially interested receives any shares of a company in which the public is not substantially interested:

- **Without consideration, the aggregate fair market value of which exceeds Rs. 50,000, the whole of the aggregate fair market value of the property; and**
- **For a consideration that is less than the aggregate fair market value of the property by an amount exceeding Rs. 50,000, the aggregate fair market value of the property to the extent it exceeds such consideration.**

However, the above transactions will not be taxable for these purposes, if they fall within the definition of a transfer under Section 47(via), 47(vic), 47(vicb), 47(vid) or 47(vii). (See V, A, 4, d, above.)

(vi) Income by way of interest received on compensation or on enhanced compensation, which is taxed in the year of receipt.

In computing income from other sources (other than (vi)), a deduction is allowed to the extent of the amount expended to earn that income. A deduction of 50% is allowed against the interest received as described at (vi).

(2) Dividends

Dividends declared at an annual general meeting are deemed to be income of the taxable year in which they are declared. Interim dividends are deemed to be income of the taxable year in which the amount of such dividends is unconditionally made available by the company to a shareholder. [345]

---

[345] **ITA, Sec. 8.**

Dividends from an Indian company, irrespective of where paid, constitute income arising in India. However, dividends of a foreign company, declared and paid outside India, even if derived from earnings within India, are not income arising in India. [346]

---

[346] **ITA, Sec. 9(1)(iv).**

Bonus shares or stock dividends are not dividends. Bonus shares on preference shares are, however, subject to tax.

The following payments or distributions made by a company to its shareholders are deemed to be dividends to the extent of accumulated profits and treated as income of the taxable year in which they are so distributed or paid: [347]

---

[347] **ITA, Sec. 2(22).**

(i) Any distribution entailing the release of the company's assets;

(ii) Distributions of debentures, debenture stock, deposit certificates, and bonuses to preference shareholders;

(iii) Distributions on the liquidation of the company;

(iv) Distributions on a reduction of capital; and

(v) Payments by way of loan or advance made by a closely held company to a shareholder holding a substantial interest in the company, provided the loan was not made in the ordinary course of business and money-lending is not a substantial part of the company's business.

(3) Other

In the following instances, where the taxpayer offers no explanation about the nature and source thereof, or the explanation offered by him is not, in the opinion of the Assessing Officer, satisfactory, the sum credited (or the value of the money, etc.) may be income in the hands of the taxpayer subject to income tax in the tax year in which the sum is credited (or in which the taxpayer is found to be the owner of the money, etc.):

(i) Where any sum is found credited in the books of a taxpayer maintained for any tax year; [348]

(ii) Where, in the tax year, the taxpayer has made investments that are not recorded in the books of account, if any, maintained by him for any source of income; [349]

(iii) Where in any tax year the taxpayer is found to be the owner of any money, bullion, jewelry or other valuable article and such money, bullion, jewelry or valuable article is not recorded in the books of account, if any, maintained by him for any source of income; [350]

(iv) Where in any tax year the taxpayer has made investments or is found to be the owner of any bullion, jewelry or other valuable article, and the Assessing Officer finds that the amount expended on making such investments or in acquiring such bullion, jewelry or other valuable article exceeds the amount recorded in this respect in the books of account maintained by the taxpayer for any source of income; [351]

(v) Where, in any tax year, a taxpayer has incurred any expenditure and offers no satisfactory explanation in respect thereof. The amount of such expenditure will be deemed to be income of the taxpayer. Notwithstanding any other provision of the ITA, unexplained expenditure that is deemed to be income of the taxpayer will not be allowed as a deduction under any head of income. [352]

---

[348] ITA, Sec. 68.

[349] ITA, Sec. 69.

[350] ITA, Sec. 69A.

[351] ITA, Sec. 69B.

[352] ITA, Sec. 69C.

---

5. Deductions in Computing Income from Business or Profession

a. Depreciation Allowance

Depreciation is available on assets owned wholly or partly by a taxpayer and used for the purposes of a business or profession. [353] Depreciable assets are classified as:

---

[353] ITA, Sec. 32.

(i) Assets of an undertaking engaged in the generation or the generation and distribution of power; and

(ii) In the case of other taxpayers, blocks of assets, which are classified as: tangible assets, being buildings, machinery, plant or furniture; and intangible assets, being know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of a similar nature, being intangible assets acquired on or after April 1, 1998.

Note: **The expression "know-how" means any industrial information or technique likely to assist in the manufacture or processing of goods or in the working of a mine, oil-well or other source of mineral deposits (including searching for, discovery of or testing of deposits for purposes of gaining of access to such deposits).**

The depreciation allowable on assets or blocks of assets is the percentage of the written-down value or actual cost prescribed in Appendix 1 or Appendix 1A, respectively under Rule 5 of the Income Tax Rules, 1962 (see the Worksheets). These rates are generally based on the useful life of the assets concerned.

However, an undertaking engaged in the generation or the generation and distribution of power has the option of claiming depreciation on its assets at the rates specified in Appendix 1 applicable to assets falling within a block of assets, provided the option is exercised before the due date for furnishing the return of income. Such an option, once exercised, is final and applies to all subsequent tax years.

Where any asset is newly acquired during the year and is put to use for purposes of the business or profession for a period of less than 180 days in that year, the depreciation with respect to that asset is restricted to 50% of the amount calculated at the percentage prescribed for the block of assets comprising that asset. If an asset is used partly for purposes of the business and partly for other purposes, the deduction on account of depreciation is allowed proportionately.

In the case of a business succession, an amalgamation (merger) or a demerger, the aggregate deduction with respect to depreciation on the block of assets comprising tangible and intangible assets, as specified above, allowable to the predecessor and successor, the amalgamating and amalgamated company, or the demerged and resulting company, may not exceed the deduction calculated at the prescribed rates that would have been available if the succession, amalgamation or demerger had not taken place. The deduction is apportioned between the predecessor and successor, the amalgamating and amalgamated company, or the demerged and resulting company, as the case may be, in proportion to the number of days for which the assets were used by each of them.

Where the business or profession of the taxpayer is carried on in a building not owned by the taxpayer but with respect to which the taxpayer holds a lease or other right of occupancy and any capital expenditure is incurred by the taxpayer for purposes of the business or profession on the construction of any structure or doing of any work in or in relation to, and by way of renovation or extension of, or improvement to, the building, the allowance for depreciation will apply as if the structure or work is a building owned by the taxpayer.

Depreciation is not available on the cost of land or intangible assets other than those specified above.

In the case of any new machinery or plant (other than ships and aircraft) that has been acquired and installed after March 31, 2005, by a taxpayer engaged in the business of manufacturing or producing any article or thing, a further depreciation allowance of 20% of the actual cost is allowed.

Such an additional depreciation deduction is not permitted with respect to:

(i) Any machinery or plant that, before its installation by the taxpayer, was used either within or outside India by any other person;

(ii) Any machinery or plant installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house;

(iii) Any office appliances or road transport vehicles; or

(iv) Any machinery or plant, the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head "profits and gains of business or profession" of any one previous year.

Note: **The depreciation allowance provisions apply whether or not the taxpayer has claimed a deduction with respect to depreciation in computing his total income.**

In the case of any building, machinery, plant or furniture with respect to which depreciation is claimed and allowed and that is sold, discarded, demolished or destroyed in the tax year (other than the tax year in which it is first brought to use), the amount by which the moneys payable with respect to the building, machinery, plant or furniture, together with the amount of scrap value, if any, fall short of the written down value thereof is allowed as depreciation, provided the deficiency is written off in the accounts of the taxpayer.

Rule 5 of the Income Tax Rules contains a list of items under the heading "plant and machinery," but the omission of an asset from that list should not preclude the taxpayer from claiming a depreciation allowance for such an asset.

The term "plant" has been defined to include ships, vehicles, books, scientific apparatus and surgical equipment used for purposes of the business or profession but does not include tea bushes or livestock. [354] A wide range of articles may be covered by the term "plant," as indicated by various judicial pronouncements. [355]

---

[354] ITA, Sec. 43(3).

[355] For example: (i) the sanitary and pipeline fittings of a hotel; (ii) safe deposit locker cabinets; (iii) roller bearing spindles installed in a textile mill; (iv) new steel converters added to existing plant for the manufacture of pharmaceutical products; (v) poles, cables, conductors and switchboards for the distribution of electricity, and the expenses incurred thereon by the taxpayer in changing over from the DC to the AC system; (vi) mains, service lines and switch-gear installed by an electrical supply company; (vii) light fittings, ceiling and pedestal fans, and water- pipe fittings in a hotel, but not lamps or similar fittings generally; (viii) a well, provided the well is dug for purposes of carrying on the business of the taxpayer, as, for instance, for the manufacture of pharmaceuticals; (ix) the pipes of a water tower (but not the actual structure of the water tower), the object of which is to raise water up to a particular height from which, by gravity or otherwise, it will be able to flow over the district. A water storage tank for the supply of water for irrigation purposes was, however, held not to be "plant;" (x) knives and lasts of a shoe manufacturer, though each knife is a separate tool or implement designed to be used in conjunction with the pressing machine; (xi) carts or wagons to transport goods from one place to another; (xii) the ship of a coal merchant; (xiii) a hulk used as a floating warehouse for coal; (xiv) coal tubs, cast iron pipes, winding and guiding ropes; (xv) scaffolding and ladders; (xvi) a movable machine put in one place while not in use and in another place when in use; (xvii) rotating cylinders with their supporting rollers in a cement factory; (xviii) a brewer's pipes and vats; (xix) tramway rails; (xx) railway engines and tools; (xxi) railway sidings installed by a company for the transfer of its raw materials; (xxii) electrical transformers; (xxiii) motor lorries and buses used for road transport; (xxiv) movable partitions; (xxv) bottles and shells used by a manufacturer of soft drinks; (xxvi) drawings and paintings constituting know-how; (xxvii) data processing machines; (xxviii) a cold storage building; (xxix)

thermocole (styrofoam) insulation in a cold storage facility; (xxx) expenditure on construction work on items such as a cold storage room, a platform for machines, and observation and cooling towers that were an essential part of the machinery and plant in an ice cream factory and without which such machinery could not work effectively; (xxxi) an aircraft engine being dismantled; (xxxii) animal-driven vehicles; (xxxiii) cylinders for storing gas; (xxxiv) silos for storing and dispensing grain; (xxxv) a swimming pool and wading pool with filtration, chlorination and heating system at a caravan site; (xxxvi) a building specifically designed and equipped to function as a nursing home; (xxxvii) a building in which power generation plant is housed; (xxxviii) a detailed project report; (xxxix) concrete tanks and reservoirs forming an integral part of a filtration plant; (xl) false ceiling and chairs in a theatre; (xli) bottles and shells used by a manufacturer of soft drinks; and (xlii) a reinforced concrete foundation for supporting machinery.

The written-down value of an asset is the actual cost of the asset less depreciation allowed to the taxpayer under the ITA. Thus, written-down value in the case of a block of assets means the aggregate of the written-down values of all the assets falling within the block at the beginning of the immediately preceding year, adjusted for: [356]

[356] ITA, Sec. 43(6).

(i) The increase in the actual cost of any asset falling within the block that is acquired during the tax year;

(ii) The decrease in the net sale price/scrap value of any asset falling within the block that is sold, demolished, or destroyed during the tax year. The decrease, however, may not exceed the written-down value;

(iii) In the case of a slump sale, the decrease in the actual cost of an asset falling within the block as reduced by:

- **The amount of depreciation actually allowed in any tax year up to March 31, 1987; and**
- **The amount of depreciation that would have been allowable to the taxpayer for any tax year commencing on or after April 1, 1987, if the asset were to have been the only asset in the relevant block of assets.**

The amount of the decrease, however, may not exceed the written down value.

Where a taxpayer was not required to compute his total income for purposes of the ITA for any tax year or tax years preceding the previous year relevant to the assessment year under consideration:

(i) The actual cost of an asset must be adjusted by the amount attributable to the revaluation of the asset, if any, in the books of accounts;

(ii) The total amount of depreciation on such an asset provided in the books of account of the taxpayer with respect to such a tax year or tax years preceding the previous year relevant to the assessment year under consideration is deemed to be the depreciation actually allowed under the ITA for this purpose; and

(iii) The depreciation actually allowed must be adjusted by the amount of depreciation attributable to the revaluation of the asset.

If any asset forming part of a block of assets is transferred during a tax year, by a demerged company:

(i) The written down value of the block of assets of the demerged company for the immediately preceding tax year is reduced by the written down value of the assets transferred to the resulting company pursuant to the demerger; and

(ii) The written down value of the block of assets of the resulting company is the written down value of the transferred assets in the books of the demerged company immediately before the demerger.

If any block of assets is transferred by a private company or unlisted public company to a limited liability partnership and the conditions specified in Section 47(xiiib) of the ITA (see 9, k, below) are satisfied, then, the actual cost of the block of assets in the case of the limited liability partnership is the written down value of the block of assets as in the case of the company on the date of conversion of the company into the limited liability partnership.

"Block of assets" is defined to mean a group of assets falling within a class of assets, comprising:

(i) Tangible assets, being buildings, machinery, plant or furniture; or

(ii) Intangible assets, being know-how, patents, copyrights, trademarks, licenses, franchises, or any other business or commercial rights of a similar nature with respect to which the same percentage of depreciation is provided. [357]

---

[357] ITA, Sec. 2(11).

"Actual cost" is defined to mean the actual cost of an asset to the taxpayer reduced by that portion of the cost, if any, that has been met directly or indirectly by any other person or authority. It is further defined as follows:

(i) Where the asset is used in the business after it ceases to be used for scientific research related to that business, the actual cost of the asset to the taxpayer will be the actual cost to the taxpayer as reduced by the amount of any deduction allowed under Section 35 of the ITA (see c, below).

(ii) Where the assets is acquired by the taxpayer by way of gift or inheritance, the actual cost of the asset to the taxpayer is the actual cost to the previous owner, as reduced by the amount of depreciation that would have been allowable to the taxpayer for any assessment year commencing on or after April 1, 1988.

(iii) Where, before the date of its acquisition by the taxpayer, the asset was at any time used by any other person for purposes of his business or profession and the Assessing Officer is satisfied that the main purpose of the transfer of the asset, whether directly or indirectly, to the taxpayer was the reduction of a liability to income tax (by the claiming of depreciation by reference to an enhanced cost), the actual cost to the taxpayer will be such an amount as the Assessing Officer may, with the prior approval of the Joint Commissioner, determine having regard to all the circumstances of the case.

(iv) Where the asset once belonged to the taxpayer and was used by him for purposes of his business or profession and thereafter ceased to be his property by reason of transfer or otherwise, and is reacquired by him, the actual cost to the taxpayer will be the lesser of the following:

- **The actual cost to the taxpayer when he first acquired the asset as reduced by the amount of depreciation that would have been allowable to him for any assessment year commencing on or after April 1, 1988; or**
- **The actual price paid for the asset re-acquired.**

(v) Where, before the date of acquisition of the asset by the taxpayer, the asset was at any time used by any other person (the "second person"), who has been claiming depreciation on the asset for purposes of his business or profession, and the asset is transferred back to the second person on lease, hire or otherwise, then the actual cost to the taxpayer will be the same as the written down value of the asset at the time of the transfer thereof by the second person.

(vi) Where a building that was previously the property of the taxpayer is brought into use for purposes of his business or profession, the actual cost to the taxpayer will be the actual cost of the building to the taxpayer, as reduced by an amount equal to the depreciation calculated at the rate in force on that date that would have been allowable had the building been used for business/professional purposes since the date of its acquisition by the taxpayer.

(vii) When the asset is transferred by a holding company to its subsidiary company or by a subsidiary company to its holding company, if the conditions of clause (iv) or of clause (v) of Section 47 of the ITA (see 4, d, above) are satisfied, the actual cost of the transferred capital asset to the transferee-company will be taken to be the same as it would have been if the transferor-company had continued to hold the capital asset for the purposes of its business.

(viii) Where, in a scheme of amalgamation/demerger, the asset is transferred by the amalgamating/demerged company to the amalgamated/resulting Indian company, the actual cost of the transferred asset to the amalgamated/resulting company is taken to be the same as it would have been if the amalgamating/demerged company had continued to hold the asset for purposes of its own business.

(ix) If the asset was acquired on or after March 1, 1994, the actual cost is to be reduced by the amount of excise duty or additional duty leviable under Section 3 of the Customs Tariff Act, 1975 with respect to which a claim for credit has been made and allowed under the Central Excise Rules, 1944.

(x) If a portion of the cost of the asset is met directly or indirectly by the central government, a state government or any authority established under any law or by any other person, in the form of a subsidy, grant or reimbursement, the actual cost to the taxpayer is reduced by such portion of the subsidy, etc. as may be related to the asset. Where the subsidy, grant or reimbursement is not related to a specific asset, the actual cost is reduced by an amount that bears to the subsidy the same proportion as the asset bears to

all the assets.

(xi) Where the asset is an asset brought into India by a nonresident taxpayer that the taxpayer acquired outside India and uses for purposes of his business or profession in India, the actual cost of the asset to the taxpayer is the actual cost as reduced by an amount equal to the depreciation calculated at the rates in force that would have been allowed had the asset been used in India for the same purpose since the date of acquisition.

(xii) If the asset is an asset with respect to which a deduction under section 35AD (see 5, f, below) is allowed or allowable, the cost of the asset will be treated as zero in specified cases. [358]

(xiii) Where the asset is an asset that the taxpayer has acquired from a country other than India for purposes of his business or profession and in consequence of a change in the rate of exchange at any time after the acquisition of the asset, there is an increase or reduction in the liability of the taxpayer as expressed in Indian currency for making payment towards the whole or a part of the cost of the asset or for repayment of the whole or a part of the moneys borrowed by him from any person, directly or indirectly, in any foreign currency specifically for purposes of acquiring the asset (being in either case the liability existing immediately before the date on which the change in the rate of exchange takes effect), the amount by which the liability is so increased or reduced during the previous year must be added to, or deducted from, the actual cost of the asset or the amount of expenditure of a capital nature referred to in Sections 35, 35A, 36(1)(ix) of the ITA, or for purposes of computing capital gains. [359]

---

[358] ITA, Sec. 43(1).

[359] ITA, Sec. 43A.

Comment: **The Supreme Court has held that the expression "actual cost" should be construed in a commercial sense and in accordance with the normal rules of accountancy; it includes all expenditure necessary to bring an asset into existence and put it in a working condition. [360]**

---

[360] *Challapalli Sugars Ltd. v. CIT* and *CIT v. Hindustan Petroleum Corp. Ltd.* (S.C.) 98 I.T.R. 167 [1975].

In the case of any building, machinery, plant or furniture of an undertaking engaged in the generation or the generation and distribution of power with respect to which depreciation has been claimed and allowed and that is sold, discarded, demolished or destroyed in the tax year (other than the tax year in which it is first brought into use), a deduction on account of depreciation is allowed of the amount by which the moneys payable with respect to the building, machinery, plant or furniture, together with the amount of scrap value, if any, fall short of the written down value, provided that amount is written off in the books of the taxpayer.

The depreciation allowance may not exceed the original cost of an asset. The depreciation allowance is mandatory and the taxpayer does not have the option of deciding whether to claim depreciation allowance in any year. The unabsorbed depreciation in any year resulting from an absence or insufficiency of profits/taxable income may be carried over to successive years until fully absorbed (see 6, b, below).

b. Deduction of Deposits in Site Restoration Fund

A taxpayer carrying on the business of prospecting for, or extracting or producing, petroleum or natural gas or both in India under an agreement with the central government is entitled to a deduction if the taxpayer has before the end of the tax year:

(i) Deposited with the State Bank of India any amount or amounts in an account (the "special account") maintained with the Bank in accordance with, and for the purposes specified in, a scheme (the "scheme") approved for this purpose by the Government of India in the Ministry of Petroleum and Natural Gas; or

(ii) Deposited any amount in an account (the "Site Restoration Account") opened by the taxpayer in accordance with, and for the purposes specified in, a scheme drawn up by the Ministry referred to above in (i) (the "deposit scheme").

The deduction (which is allowed before any loss brought forward from earlier years is set off) is the lower of:

(i) A sum equal to the amount or the aggregate of the amounts so deposited; or

(ii) A sum equal to 20% of the profits of the business (computed under the head "profits and gains of business or profession" before making any deduction under this section).

Where the taxpayer is a firm or an association of persons or a body of individuals, the deduction is not allowed in the computation of the income of any partner or member of the firm, association of persons or body of individuals.

Where any deduction, with respect to any amount deposited in the special account, or in the Site Restoration Account, has been allowed in any tax year, no deduction is allowed with respect to that amount in any other tax year.

Any amount credited in the special account or the Site Restoration Account by way of interest is deemed to be a deposit. The deduction is not allowed unless the income tax return of the taxpayer is accompanied by an audit report made by an accountant stating that the deduction has been correctly claimed. No amount standing to the credit of the taxpayer in the special account or the Site Restoration Account may be withdrawn except for the purposes specified in the scheme or in the deposit scheme.

No deduction is allowed with respect to any amount utilized for the purchase of:

(i) Any machinery or plant to be installed in any office premises or residential accommodation, including any accommodation in the nature of a guest-house;

(ii) Any office appliance (not being a computer);

(iii) Any machinery or plant, the whole of the actual cost of which is allowed as a deduction (whether by way of depreciation or otherwise) in computing income chargeable under the head "profits and gains of business or profession" of any one tax year; or

(iv) Any new machinery or plant to be installed in an industrial undertaking for purposes of a business of constructing, manufacturing or producing any article or thing specified in the list in the Eleventh Schedule (see the Worksheets).

Where any amount standing to the credit of the taxpayer in the special account or the Site Restoration Account is withdrawn on the closure of the account during any tax year by the taxpayer, the amount so withdrawn from the account, as reduced by the amount, if any, payable to the central government by way of profit or production share as provided in the agreement, is deemed to be profits and gains of the business or profession for that tax year and is accordingly chargeable to income tax as income of that tax year.

Any amount standing to the credit of the taxpayer in the special account or the Site Restoration Account utilized by the taxpayer for purposes of any expenditure in connection with the business in accordance with the scheme or the deposit scheme is not allowed in computing income chargeable under the head "profits and gains of business or profession."

If any amount standing to the credit of the taxpayer in the special account or the Site Restoration Account is released during any tax year by the State Bank of India or is withdrawn by the taxpayer from the Site Restoration Account to be used by the taxpayer for purposes of the business in accordance with the scheme or the deposit scheme but is not so used, either wholly or in part, within that tax year, the whole of the amount or the part thereof that is not so used is deemed to be profits and gains of the business and accordingly chargeable to income tax as income of that tax year.

If within eight years from the end of the tax year, an asset that was acquired in accordance with the scheme or the deposit scheme is sold or otherwise transferred by the taxpayer or any person, such part of the cost of the asset as may be related to the deduction allowed is deemed to be profits and gains of the business or profession for the tax year in which the asset is sold or otherwise transferred and is accordingly chargeable to income tax as income of that tax year.

However, the above will not apply where the asset is sold or otherwise transferred by the taxpayer to the government, a local authority, a corporation established by or under a central, state or provincial act or a government company and where the sale or transfer of the asset is made in connection with the succession of a firm by a company in the business or profession carried on by the firm as a result of which the firm sells or otherwise transfers to the company any asset, and the scheme or the deposit scheme continues to apply to the company in the manner applicable to the firm. [361]

---

[361] **ITA, Sec. 33ABA.**

---

c. Expenditure on Scientific Research

A deduction is allowed for expenditure on scientific research as follows:

(i) A deduction is allowed for revenue expenditure on scientific research incurred by a taxpayer, provided the research is related to the business of the taxpayer.

(ii) Expenditure incurred by a taxpayer on the payment of salary to research personnel or on the purchase of material used in scientific research during a period of three years immediately before the commencement of business is regarded as having been expended in the tax year in which the business is commenced, to the extent certified by the prescribed authority.

(iii) Contributions to an approved research association that has as its object the undertaking of scientific research, or to a university, college or other institution to be used for scientific research, are deductible in

the year they are made. The amount of the deduction is 1.75 times the sum contributed.

(iv) Contributions to a company fulfilling specified conditions and to be used by it for scientific research are eligible for deduction of a sum equal to 1.25 times the sums contributed.

(v) Contributions to a research association that has as its object research in social sciences or statistics, or to a university, college or other institution to be used for research in social sciences or statistical research, are eligible for deduction of a sum equal to 1.75 times the sum contributed.

(vi) Expenditure of a capital nature (excluding expenditure on the acquisition of land but including capital expenditure incurred during a period of three years immediately before the commencement of business) incurred on scientific research related to the taxpayer's business is tax deductible in the year in which it is incurred. However, depreciation allowance is not available with respect to the capital assets concerned. If, in a particular year, the capital expenditure is not fully allowed because there are no profits or insufficient profits, the deficiency, if any, may be carried over to successive years until fully absorbed against profits.

(vii) A contribution to a national laboratory, a university, the Indian Institute of Technology or any other specified person, with a specific direction that the sum be used only for an approved program of scientific research, is eligible for deduction of a sum equal to 1.75 times the sum contributed.

(viii) Expenditure incurred by a company engaged in any business of manufacturing or producing any article or thing, other than that specified in the list of the Eleventh Schedule, on scientific research (not being expenditure on the cost of land or buildings) on in-house research and development (R&D) facilities, as approved by the prescribed authority, is eligible for a deduction equal to 2 times the amount of the expenditure. No further deductions under the ITA are available with respect to sums so expended. [362]

---

[362] **ITA, Sec. 35.**

---

d. Amortization of Expenditure on a License Acquired to Operate Telecommunication Services

The ITA provides for the amortization, over the period for which the license is in force, of capital expenditure incurred to acquire any right to operate telecommunication services (either before the commencement of the business of operating telecommunication services or thereafter at any time during any tax year) for which payment is actually made to obtain a license.

Where the license is transferred and the transfer proceeds (so far as they consist of capital sums) are less than the unamortized expenditure, the taxpayer will be allowed as a deduction in the tax year in which the license is transferred, an amount equal to the unamortized expenditure as reduced by the transfer proceeds.

Where the whole or any part of the license is transferred and the transfer proceeds (so far as they consist of capital sums) exceed the amount of unamortized expenditure, such excess as does not exceed the difference between the expenditure incurred to obtain the license and the unamortized expenditure will be chargeable to tax in the year in which the license is transferred. No further deduction will be allowed in the year in which the license is transferred or in a subsequent year. Where the license is transferred in a tax year in which the business is no longer in existence, the provisions above will apply as if the business continued to be in existence.

The deduction to be allowed for expenditure incurred remaining unallowed is arrived at by subtracting the proceeds of transfer (insofar as they consist of capital sums) from the expenditure remaining unallowed and then dividing the remainder by the number of relevant previous years that have not expired at the beginning of the previous year during which the license is transferred.

Where in a scheme of amalgamation or demerger, the amalgamating/demerged company sells or otherwise transfers the license to the amalgamated/resulting company, the provisions described above will apply only to the amalgamated/resulting company in the same way as they would have applied to the amalgamating/demerged company had the amalgamation/demerger not taken place. [363]

---

[363] **ITA, Sec. 35ABB.**

---

e. Expenditure on an Eligible Project or Scheme

Where a taxpayer incurs any expenditure by way of payment of any sum to a public sector company or local authority, or to an association or institution approved by the National Committee for carrying out any eligible project or scheme, or directly on any project or scheme, the taxpayer will be allowed a deduction of the amount of such expenditure incurred during the previous year.

The deduction is not allowed unless the income tax return of the taxpayer is accompanied by a certificate from the public sector company, local authority or association or institution to which the payment is made, and where the payment is made directly to the project or scheme, a certificate from an accountant stating that the deduction has been correctly claimed.

A taxpayer will not be denied a deduction with respect to any sum paid as above merely on the ground that subsequent to the payment of the sum, the approval granted to the association or institution has been withdrawn or the notification of the eligible project or scheme carried out by the public sector company, local authority or association or institution has been withdrawn.

Where a deduction is claimed and allowed for any assessment year with respect to any expenditure described above, a deduction will not be allowed with respect to such expenditure under any other provisions of the IT Act for the same or any other assessment year.

Where an association or institution is approved by the National Committee and subsequently the Committee is satisfied that the project or scheme is not being carried on in accordance with all or any of the conditions subject to which approval was granted, or the association or institution to which approval was granted has not furnished to the National Committee, after the end of each tax year, a report as required, the National Committee may withdraw the approval at any time after giving a reasonable opportunity of showing cause against the proposed withdrawal, to the association or institution concerned. Similar rules apply with respect to any project or scheme that has been notified as an eligible project, i.e., subsequently the National Committee may withdraw the notification in the same manner as that in which it was issued, after giving a reasonable opportunity of showing cause against the proposed withdrawal, to the association or institution concerned.

An "eligible project" or "scheme" means a project or scheme for promoting the social and economic welfare of, or the uplift of, the public that is notified by the central government on the recommendations of the National Committee. [364]

---

[364] ITA, Sec. 35AC.

---

f. Expenditure on Specified Business

Taxpayers incurring any expenditure of a capital nature (other than expenditure incurred on the acquisition of land, goodwill or a financial instrument) wholly and exclusively for purposes of a specified business will be allowed a 100% deduction with respect to such expenditure. Such expenditure will be allowed as a deduction in the tax year in which the operations of the specified business commence if the expenditure is incurred prior to the commencement of the business and the amount is capitalized in the accounts of the taxpayer on the date of commencement of the operations.

"Specified" business means a business of:

(i) Setting up and operating cold chain facilities for the storage or transportation of agricultural produce, dairy products and other related items;

(ii) Warehousing for storing agricultural produce;

(iii) Laying and operating a cross-country natural gas, crude, or petroleum oil pipeline network for distribution, including where storage facilities are an integral part of such network;

(iv) Building and operating, anywhere in India, a new hotel of two-star category or above, as classified by the central government;

(v) Building and operating, anywhere in India, a new hospital with at least 100 beds for patients; and

(vi) Developing and building a housing project under a scheme for slum redevelopment or rehabilitation framed by the central government or a state government, as the case may be.

The specified business must fulfill the following conditions to claim the deduction:

(i) It is not set up by splitting up, or the reconstruction, of a business already in existence;

(ii) It is not set up by transferring to the specified business machinery or plant previously used for any purpose, in excess of 20% of the total value of the machinery or plant used in such business.

However, any machinery or plant that was used outside India by any person other than the taxpayer will not be regarded as machinery or plant previously used for any purpose, if:

- **Such machinery or plant was not, at any time prior to the date of the installation by the taxpayer, used in India;**
- **Such machinery or plant is imported into India from any country outside India; and**
- **No deduction on account of depreciation with respect to such machinery or plant has been allowed or is allowable under the provisions of the ITA in computing the total income of any person for any period prior to the date of the installation of the machinery or plant by the taxpayer;**

(iii) Where the specified business is in the nature of a business listed above in (ii) (i.e., laying and operating a cross-country natural gas, etc. network), the following additional conditions are required to be fulfilled:

- **The business is owned by a company formed and registered in India under the Companies Act, 1956 or by a consortium of such companies, or by an authority or a board or corporation established or constituted under a central or state act;**
- **The business has been approved by the Petroleum and Natural Gas Regulatory Board and notified by the central government in the Official Gazette, in this respect;**
- **The business has made not less than such proportion of its total pipeline capacity as specified by regulations made by the Petroleum and Natural Gas Regulatory Board established under Sub-section (1) of Section 3 of the Petroleum and Natural Gas Regulatory Board Act, 2006 (19 of 2006) available for use on a common carrier basis by any person other than the assessee or an associated person; and**
- **Any other conditions that may be prescribed.**

No further deductions under the provisions of Chapter VIA under the heading "C. — Deductions in respect of certain incomes" (see 9, below) will be allowed for the specified business for any tax year.

No further deductions will be allowed with regard to the capital expenditure referred to above, under any other section of the ITA in any tax year.

Deduction will be available only if the business commences its operations:

(i) On or after April 1, 2007, where the specified business is in the nature of a business listed above in (iii) (i.e., laying and operating a cross-country natural gas, etc. network);

(ii) On or after April 1, 2010, where the specified business is in the nature of a business listed at (iv), (v) or (vi), above; and

(iii) On or after April 1, 2009, in all other cases. [365]

---

[365] **ITA, Sec. 35AD.**

---

g. Expenditure by Way of Payment to Associations and Institutions for Carrying Out Rural Development Programs

Where a taxpayer incurs any expenditure by way of payment of any sum: to an association or institution that has as its object the undertaking of any program of rural development to be used for carrying out any program of rural development approved by the prescribed authority; or to an institution or association that has as its object the training of persons for implementing programs of rural development; or to a rural development fund set up and notified by the central government for this purpose; or to the National Urban Poverty Eradication Fund set up and notified by the central government for this purpose, the taxpayer will be allowed a deduction of the amount of such expenditure incurred during the previous year. The deduction is not allowed unless the taxpayer furnishes a certificate from the association or institution to the effect that the program of rural development was approved by the prescribed authority before March 1, 1983. Where such payment is made after February 28, 1983, the rural development program must involve work by way of construction of any building or other structure, whether for use as a dispensary, school, training or welfare centre, workshop or for any other purpose or the laying of any road or the construction or boring of a well or tube-well or the installation of any plant or machinery, and such work must have commenced before March 1, 1983

The deduction to the taxpayer with respect to any sum paid as above will not be denied merely on the ground that, subsequent to the payment of the sum, the approval granted to the program, association or institution is withdrawn. [366]

---

[366] **ITA, Sec. 35CCA.**

---

h. Amortization of Preliminary Expenses

The ITA provides for the amortization of preliminary expenses incurred by an Indian company or resident noncorporate taxpayer, in an amount equal to one-fifth of the expenditure per year over a period of five years. The preliminary expenses must be incurred before the commencement of business, or in connection with the extension of an undertaking or the setting up of a new unit. [367]

---

[367] **ITA, Sec. 35D.**

One-fifth of the qualifying expenditure is allowable as a deduction in each of the five successive years beginning with the taxable year in which:

(i) The business commences;

(ii) The extension of the undertaking is completed; or

(iii) The new unit commences production or operation.

Preliminary expenses include expenditure incurred in connection with the preparation of a feasibility report, a project report or a market survey, engineering services, legal charges for drafting any agreement or memorandum and articles of association and related agreements, company registration fees, and public issue expenses, or other such prescribed expenditure.

The aggregate amount of qualifying expenditure incurred after March 31, 1998, may not exceed 5% of the cost of the project. An Indian company has the option of claiming an alternative limit of 5% of the capital employed in the business of the company.

The "cost of the project" means the actual cost of fixed assets that is shown in the books of the taxpayer as of the last day of the tax year in which:

(i) The business of the taxpayer commences;

(ii) The extension of the undertaking is completed; or

(iii) The new unit commences production or operation.

In the last two cases, the cost of the project would mean the cost of the fixed assets acquired or developed in connection with the extension of the undertaking or the setting up of the new unit.

"Capital employed in the business of the company" means the aggregate of the issued share capital, debentures, and long-term borrowings as of the last day of the tax year in which:

(i) The business of the taxpayer commences;

(ii) The extension of the undertaking is completed; or

(iii) The new unit commences production or operation.

In the last two cases, it is the capital, debentures and long-term borrowings issued or obtained in connection with the extension of the undertaking or the setting up of the new unit.

Comment: **The provision for amortization is not intended to supersede any other provision in the ITA under which expenditure is allowed as a deduction against profits.**

Where a deduction for any expenditure stated above is claimed and allowed to a taxpayer for any assessment year, a deduction will not be allowed with respect to such expenditure under any other provision of the ITA for the same or any other assessment year.

Where there is a transfer of an undertaking of an Indian company in a scheme of amalgamation or demerger, before the expiry of the period specified above, to another company, the provisions described above will apply only to the amalgamated/resulting company in the same way as they would have applied to the amalgamating/demerged company had the amalgamation/demerger not taken place.

i. Amortization of Expenditure in the Case of Amalgamation or Demerger

The ITA provides for the amortization of expenditure incurred by an Indian company, wholly and exclusively for purposes of the amalgamation or demerger of an undertaking, of an amount equal to one fifth of the expenditure per year over a period of five years. No deduction thereafter will be allowed with respect to such expenditure under any other provision of the ITA. [368]

---

[368] **ITA, Sec. 35DD.**

---

j. Amortization of Expenditure Incurred Under Voluntary Retirement Scheme

Expenditure incurred by a taxpayer by way of payment to employees in connection with voluntary retirement in accordance with the prescribed guidelines is amortized over a period of five years in equal installments.

In the case of a business succession, an amalgamation (merger) or a demerger, the provisions above would apply

only to the successor, the amalgamated company, or the demerged company, in the same way as they would have applied to the predecessor, the amalgamating company or the demerged company had the succession, amalgamation or demerger not taken place.

No further deductions are allowable with respect to the expenditure referred to above under any of the other provisions of the ITA. [369]

[369] ITA, Sec. 35DDA.

k. Amortization of Expenditure on Prospecting, etc. for the Development of Certain Minerals

The ITA provides for the amortization over a 10-year period of expenditure incurred on prospecting for, or for the extraction, production or development of, a broad range of minerals specified in the ITA. The benefit of amortization is available to Indian companies and resident taxpayers other than companies.

Expenditure on operations relating to prospecting, etc., for minerals qualifies for amortization if it is incurred during the year commercial production begins, or in any one or more of the four years immediately preceding that year. However, expenditure on the following is not eligible for amortization:

(i) The acquisition of the site of the source of any specified minerals, or of any rights in or over the site;

(ii) The acquisition of deposits of any specified minerals or group of associated minerals, or of any rights in or over the deposits; and

(iii) Fixed assets on which depreciation allowance is available.

Amortization is allowable only against profits arising from the commercial exploitation of any mine or deposit, and any unabsorbed amount may be carried over to subsequent years. The aggregate unabsorbed allowance lapses at the end of the tenth year reckoned from the year of commencement of commercial production.

Where a deduction of any of the expenditure referred to above is claimed and allowed to a taxpayer for any assessment year, a deduction will not be allowed with respect to such expenditure under any other provision of the ITA for the same or any other assessment year.

Where there is a transfer of an undertaking of an Indian company in a scheme of amalgamation or demerger, before the expiry of the period specified above, to another company, the provisions described above will apply only to the amalgamated/resulting company in the same way as they would have applied to the amalgamating/demerged company had the amalgamation/demerger not taken place. [370]

[370] ITA, Sec. 35E.

l. Special Provisions Relating to the Income of Shipping Companies

A company having income from the business of operating qualifying ships has the option of being taxed under the Tonnage Tax Scheme (TTS), instead of the other provisions of the ITA. [371] Such income will be taxed as "Profits and gains from business or profession."

[371] ITA, Chapter XII-G, Secs. 115V to 115VZC.

A company will be regarded as operating a ship if it operates any ship, whether owned or chartered by it, and includes a case where even a part of the ship has been chartered by it in an arrangement such as a slot charter or joint charter. However, a company will not be regarded as the operator of a ship where the ship has been chartered out by it on bareboat charter-cum-demise terms or on bareboat charter terms for more than three years.

To qualify under the TTS:

(i) A company must be an Indian company;

(ii) The place of the effective management of the company must be in India;

(iii) The company must own at least one qualifying ship; and

(iv) The main object of the company must be to carry on the business of operating "qualifying ships."

A "qualifying ship" means:

(i) A seagoing ship or vessel of 15 net tonnage or more;

(ii) A ship registered under the Merchant Shipping Act, 1958 or a ship registered outside India with respect to which a license has been issued by the Director General of Shipping; and

(iii) A ship that has a valid certificate indicating its net tonnage.

A "qualifying ship" does not include:

(i) A seagoing ship or vessel if the main purpose for which the ship or vessel is used is the provision of goods or services of a kind normally provided on land;

(ii) A fishing vessel;

(iii) A factory ship;

(iv) A pleasure craft;

(v) A harbor or river ferry;

(vi) An offshore installation; or

(vii) A qualifying ship that is used as a fishing vessel for a period of more than 30 days during the tax year.

A company engaged in the business of operating qualifying ships and opting for the TTS must compute the profits from the business under the TTS. The income from the operation of qualifying ships is considered a separate business, distinct from all other activities or business carried on by the company. The TTS will apply only if the option has been exercised as prescribed. Where a company operating qualifying ships is not covered by the TTS or opts not to be covered by the TTS, the profits and gains from its business will be computed in accordance with the other provisions of the ITA. Tax is levied on the notional income arising from the operation of the qualifying ships at normal tax rates. The notional income is the aggregate of the tonnage income of each qualifying ship and is computed in the following manner:

Qualifying ship having net tonnage	Amount of daily tonnage income
Up to 1,000	Rs.46 for each 100 tons
1,001 – 10,000	Rs.460 plus Rs.35 for each 100 tons exceeding 1,000 tons
10,001 – 25,000	Rs.3,610 plus Rs.28 for each 100 tons exceeding 10,000 tons
Exceeding 25,000	Rs. 7,810 plus Rs.19 for each 100 tons exceeding 25,000 tons

The tonnage income for each qualifying ship is the daily tonnage income of each ship multiplied by:

(i) The number of days in the tax year;

(ii) Where the ship is operated as a qualifying ship for only part of the tax year, the number of days in that part of the tax year.

If a qualifying ship is operated by two or more companies by way of joint interest or by way of an agreement for the use of the ship and their respective shares are definite and ascertainable, the tonnage income of each company will be the amount equal to a share of the income proportionate to its share of that interest. The tonnage income of each company will be computed as if each had been the only operator.

No deduction or set-off is allowed in computing the tonnage income as set out above. In case of a company opting for TTS, only the "tonnage income" will be chargeable to tax, not the "shipping income."

The shipping income for a company opting for the TTS, will be:

(i) Its profit from core activities; and

(ii) Its profit from incidental activities.

However, where the aggregate of income from incidental activities exceeds 25% of the turnover from core activities, the excess will not form part of the relevant shipping income to be taxed under the TTS and will be taxable under the other provisions of the ITA.

The core activities of the tonnage tax company must be:

(i) Activities from operating qualifying ship; and

(ii) Other ship-related activities as under a shipping contract with respect to earning from pooling arrangements and freight contracts; and specific shipping trades, being onboard or onshore activities of

passenger ships, composing fares and food and beverage consumed on board; and slot charter, space charter, joint charter, feeder services, or container box leasing of container shipping.

The central government may, by notification, exclude any of the "other activities" referred to above or prescribe the limit up to which such activities may be included in the core activities. Incidental activities are the activities that are incidental to the core activities and prescribed for the purpose.

Where a tonnage tax company operates any ship that is not a qualifying ship, the income of such ship will be computed under the other provisions of the ITA.

Where any goods or services held for purposes of tonnage tax business are transferred to any other business carried on by a tonnage tax company, or where any goods or services held for purposes of any other business carried on by such tonnage tax company are transferred to the tonnage tax business and, in either case, the consideration, if any, for such transfer as recorded in the accounts of the tonnage tax business does not correspond to the market value of such goods or services as on the date of the transfer, then, the relevant shipping income will be computed as if the transfer, in either case, had been made at the market value of such goods or services as on that date. However, where in the opinion of the Assessing Officer, the computation of the relevant shipping income as specified above, presents exceptional difficulties, the Assessing Officer may compute such income on such reasonable basis as he may deem fit.

Where it appears to the Assessing Officer that, owing to the close connection between the tonnage tax company and any other person, or for any other reason, the course of business between them is so arranged that the business transacted between them produces for the tonnage tax company more than the ordinary profits that might be expected to arise in the tonnage tax business, the Assessing Officer will, in computing the relevant shipping income of the tonnage tax company, take the amount of income to be such as may reasonably be deemed to have been derived therefrom.

If the relevant shipping income of a tonnage tax company is a loss, then, such loss will be ignored for the purposes of computing tonnage income.

Where a tonnage tax company also carries on any business or activity other than tonnage tax business, common costs attributable to the tonnage tax business must be determined on a reasonable basis.

Where any assets, other than qualifying ships, are not used exclusively for tonnage tax business, depreciation on such assets will be allocated between the tonnage tax business and the other business on a fair proportion to be determined by the Assessing Officer.

Depreciation for the first tax year of the TTS is computed on the written down value (WDV), as defined, of the qualifying ships. The WDV of the block of assets constituted by ships on the first day of the tax year will be divided in the ratio of the book WDV of the qualifying ships and the book WDV of the non-qualifying ships. The block of qualifying assets will constitute a separate block of assets.

Where an asset forming part of the block of qualifying assets is used for purposes other than tonnage tax business, an appropriate portion of the WDV allocable to such assets must be subtracted from the WDV of that block and added to the block of other assets.

Where an asset forming part of a block of other assets is used for the tonnage tax business, an appropriate portion of the written down value allocable to such assets must be subtracted from the written down value of the block of other assets and added to the block of qualifying assets.

Where assets are transferred from a block of qualifying assets to a block of other assets or vice versa, depreciation computed for the tax year must be allocated in accordance with the ratio of the number of the days for which the assets were used for purposes the tonnage tax business to the number of the days for which the assets were used for purposes of the other business.

In computing the tonnage income of a tonnage tax (shipping) company, no effect will be given to other deductions, expenses, allowances, concessions or provisions for the carryforward of losses under the other provisions of the ITA. The provisions relating to the carryforward and set-off of business losses available to a shipping company before its opting for the TTS that are attributable to its tonnage tax business will apply as if such losses had been set-off against the relevant shipping income in any of the tax years when the company is under the TTS. Such losses will not be available for set-off against any income other than the relevant shipping income in any tax year beginning on or after the company exercises its option for the TTS.

Any profit or gain arising from the transfer of a capital asset being an asset forming part of the block of qualifying assets is chargeable to income tax in accordance with the other provisions of ITA.

The book profit/loss derived from the activities of a tonnage tax company is excluded for purpose of computing the minimum alternate tax (see 7, c, below).

A qualifying company may opt for the TTS by making an application to the Joint Commissioner having jurisdiction over the company, in such form and manner as may be prescribed. The TTS will remain in force for a period of 10 years from the date on which the option is exercised and will be taken into account from the tax year in which the option is exercised.

An option for the TTS ceases to have effect from the tax year in which:

(i) The qualifying company ceases to be a qualifying company;

(ii) There is a default in complying with the relevant provisions;

(iii) The tonnage tax company is excluded from the TTS; or

(iv) The qualifying company furnishes a declaration in writing to the Assessing Officer requesting that the provision of the TTS not be made applicable to it and the profits and gains of the company from the business of operating qualifying ships are computed in accordance with the other provisions of the ITA.

A company will not be eligible to opt for the TTS for a period of 10 years from the date of opting out, default or order.

The option for the TTS may be renewed within one year from the end of the tax year in which the option ceases to have effect.

A tonnage tax company is required to credit to a reserve account (or tonnage tax reserve account) an amount of not less than 20% of the book profit from core and other activities, to be utilized in the specified manner.

Where the company has a book profit from the business of operating qualifying ships and a book loss from any other sources and, consequently, the company is not in a position to create the reserve, in full or in part, the company must create the reserve to the extent possible in that tax year, the shortfall must be added to the amount of the reserve required to be created for the next following tax year and the shortfall will be deemed to be part of the reserve requirement of the following tax year. Despite the existence of a shortfall in the creation of a reserve during a particular tax year, the company will be considered to have created a sufficient reserve for that tax year. The allowance for making up the shortfall is granted for no more than two consecutive tax years.

The amount credited to the tonnage tax reserve account must be utilized by the company before the expiry of eight years from the year next following the tax year in which the amount was credited for:

(i) Acquiring a new ship for purposes of the business of the company; and

(ii) For purposes of the business of operating qualifying ships but not for purposes of the distribution by way of dividend or profits or remittance outside India for the creation of any assets outside India.

Where any amount credited to the tonnage tax reserve account:

(i) Has been utilised for any purpose other than that referred above;

(ii) Has not been utilised for the purpose referred in (i) in the previous paragraph; or

(iii) Has been utilised for the purposes of acquiring a new ship that is sold or otherwise transferred other than in any scheme of demerger by the company to any person at any time before expiry of three years from the end of the tax year in which it was acquired,

an amount that bears the same proportion to the total relevant shipping income of the year in which the reserve was created, as the amount out of such reserve so utilized (or not utilized) bears to the total reserve created during the year will be taxable under the other provisions of the ITA, in the tax year specified in this regard.

Where the amount credited to the tonnage tax reserve account is less than the minimum amount required to be credited as set out above, an amount that bears the same proportion to the total relevant shipping income, as the shortfall in credit to the reserves bears to the minimum reserve required to be credited will not be taxable under the TTS and will be taxable under the other provisions of the ITA.

If the reserve required to be created is not created for any two consecutive tax years, the option of the company for the TTS will cease to have effect from the beginning of the tax year following the second consecutive tax year in which the failure to create the reserve occurred.

A shipping company opting for the TTS must comply with minimum training requirements in accordance with the guidelines issued by the director general of shipping and notified by the central government.

If the minimum training requirement is not complied with for any five consecutive previous years, the option of the company for the TTS will cease to have effect from the beginning of the tax year following the fifth consecutive tax year of the failure.

In the case of every company that has opted for the TTS, not more than 49% of the net tonnage of the qualifying ships operated by it during any tax year may be "chartered in." The term "chartered in" excludes a ship chartered in by the company on bareboat charter-cum-demise terms.

The proportion of net tonnage with respect to a tax year is calculated based on the average of the net tonnage during the tax year and is computed in the manner prescribed in consultation with the Director General of shipping. Where

the net tonnage of ships chartered in exceeds the 49% limit during any tax year, the total income of the company in relation to that tax year is computed as if the option for the TTS does not have effect for that tax year. Where the 49% limit is exceeded in any two consecutive tax years, the option for the TTS ceases to have effect from the beginning of the tax year following the second consecutive tax year in which the limit was exceeded.

In an amalgamation, the provisions of the TTS apply to the amalgamated company as if it were a qualifying company. Where the amalgamated company is not a tonnage tax company, it must opt for the TTS within three months from the date of approval of the scheme of amalgamation.

Where the amalgamating companies are tonnage tax companies, the TTS applies to the amalgamated company for the period for which the option for the TTS that has the longest unexpired period continues to be in force.

In a scheme of demerger, where the demerged company transfers its tonnage business to the resulting company before the expiry of the option for the TTS, then the TTS will apply to the resulting company for the unexpired period, if it continues to be a qualifying company. The option for the TTS with respect to a demerged company remains in force for the unexpired period of the TTS if it continues to be a qualifying company.

Where a tonnage tax company is a party to any transaction or arrangement that amounts to an abuse of the TTS as a result of which a tax advantage is obtained by a nontonnage tax company or by the tonnage tax company with respect to its nontonnage activities, the Assessing Officer may, by an order in writing, exclude such company from the TTS.

The option for the TTS is not allowed unless:

(i) The tonnage tax company maintains separate books of account in respect of the business of operating qualifying ships; and

(ii) The income tax return is accompanied by an audit report from an accountant stating that the deduction has been correctly claimed.

m. Concessions for Financial Corporations, Housing Finance and Banking Companies

The business profits of a specified entity engaged in providing long-term finance: for industrial or agricultural development or the development of infrastructure facilities in India; for purpose of housing development; or for the construction or purchase of houses in India for residential purposes are eligible for a deduction of 20% of the profits derived from such business and credited to a special reserve account created and maintained for the purpose. The deduction is restricted to the aggregate of twice the amount of paid-up capital and general reserves of the specified entity concerned. [372]

---

[372] ITA, Sec. 36(1)(viii).

---

n. Expenditure for Unlawful Purposes

Any expenditure incurred by a taxpayer for any purpose that is an offence or that is prohibited by law is not considered to have been incurred for purposes of a business or profession and no deduction or allowance is made with respect to such expenditure. [373]

---

[373] ITA, Explanation, Sec. 37(1).

---

o. Expenditure in Cash

Where a taxpayer incurs any expenditure in a sum exceeding Rs.20,000 (Rs.35,000 in the case of a payment made for plying, hiring or leasing goods carriages) with respect to which the payment, or the aggregate of payments to a person in a day, is made otherwise than by an account payee check drawn on a bank or by an account payee bank draft, no deduction is allowed with respect to such expenditure.

Where an allowance has been made in the assessment for any year of any liability incurred by a taxpayer for any expenditure and, during any subsequent previous year, the taxpayer makes payment in respect thereof, otherwise than by an account payee check drawn on a bank or an account payee bank draft, the payment so made is deemed to be profits and gains of a business or profession and accordingly chargeable to income tax as income of the subsequent year, if the payment, or the aggregate of payments made to a person in a day, exceeds Rs.20,000.

However, no disallowance will be made in such cases and in such circumstances as may be prescribed, having regard to the nature and extent of the banking facilities available, considerations of business expediency, and other relevant factors. [374]

---

[374] ITA, Sec. 40A(3).

---

p. Bad Debts

Any bad debt or part of a bad debt written off as irrecoverable in the accounts of a taxpayer will be allowed as a deduction from the income of the taxpayer's business or profession if the debt has already been taken into account as income either in the same year or in any preceding year. Money lent in the ordinary course of a business of banking or money lending is also permitted to be written off as a bad debt. [375]

[375] ITA, Sec. 36(1)(vii).

q. Securities Transaction Tax

The amount of securities transaction tax paid by a taxpayer with respect to taxable securities transactions entered into in the course of the taxpayer's business during the tax year is allowed as a deduction if the income arising from the taxable securities transactions is included in income computed under the head "Profits and gains of business and profession." [376]

[376] ITA, Sec. 36(1)(xv).

r. Provision for Bad and Doubtful Debts in the Case of Banks and Financial Institutions

By way of a provision for bad and doubtful debts, a scheduled bank, not being a bank incorporated by or under the laws of a country outside India or a nonscheduled bank, is allowed to deduct an amount not exceeding 7.5% of its gross total income before making any deduction related to the provision discussed in this section and Chapter VI-A (see 9, below) and an amount not exceeding 10% of the aggregate average advances made by its rural branches computed in a prescribed manner. A scheduled or nonscheduled bank may, at its option, be allowed a deduction, with respect to any assets classified as doubtful or loss assets in accordance with the guidelines issued by the RBI in this regard, of an amount not exceeding 5% of such advances.

A scheduled bank or nonscheduled bank is, at its option, allowed a further deduction in excess of the above specified limits of an amount that may not exceed its income derived from the redemption of securities in accordance with a scheme set up by the central government. The deduction is allowed if the income has been disclosed in the return of income under the head "Profits and gains of business or profession."

Any bank that is incorporated by or under the laws of a country outside India may deduct an amount not exceeding 5% of its total income before making any deduction under this clause and Chapter VIA (see 9, below).

A public financial institution, a state financial corporation or a state industrial investment corporation may deduct an amount not exceeding 5% of its total income before making any deduction under this clause and Chapter VIA (see 9, below). [377]

[377] ITA, Sec. 36(1)(viia).

s. Amounts not Deductible

The following amounts are nondeductible:

(i) Any interest, royalty, fees for technical services or other sum chargeable under the ITA and payable outside India or paid in India to a nonresident, not being a company or a foreign company, from which tax has not been deducted or, having been deducted, has not been paid during the previous year or in the subsequent year, is not allowed as a deduction. Where tax has been deducted or paid in any subsequent year with respect to such a sum, the sum will be allowed as a deduction in the year of payment. [378]

(ii) Any interest, commission or brokerage fees, rent, royalty, fees for professional services, fees for technical services payable to a resident, or amounts payable to a contractor or subcontractor being a resident, from which tax has not been deducted or, having been deducted, has not been paid on or before the due date specified in Section 139(1) of the ITA is not allowed as a deduction.

[378] ITA, Sec. 40(a)(i).

However, if tax is deducted or paid in any subsequent year after the due date specified in Section 139(1) of the ITA, the amount will be allowed as a deduction in the year of payment.

(iii) Any amount paid on account of fringe benefit tax, tax on the profits of a business or profession, or wealth tax. [379]

(iv) Any payment of salary payable outside India or to a nonresident, where tax has not been paid thereon or deducted therefrom in accordance with the relevant provisions of the ITA. [380]

(v) Where the taxpayer incurs any expenditure with respect to which payment has been or is to be made to any specified person and the Assessing Officer is of the opinion that the expenditure is excessive or unreasonable having regard to the fair market value of the goods, services or facilities for which the payment is made, the legitimate needs of the business or profession of the taxpayer, or the benefit derived by or accruing to him therefrom, so much of the expenditure as is considered by him to be excessive or unreasonable will not be allowed as a deduction.

---

[379] **ITA, Sec. 40(a)(ic), (ii), (iia).**

[380] **ITA, Sec. 40(a)(iii).**

The following are "specified" persons for this purpose:

(i) Where the taxpayer is an individual, any relative of the taxpayer;

(ii) Where the taxpayer is a company or a firm, a director of the company or a partner in the firm, or any relative of such director or partner;

(iii) Any individual who has a substantial interest in the business or profession of the taxpayer, or any relative of such an individual;

(iv) A company or firm having a substantial interest in the business or profession of the taxpayer, any director or partner of such company or firm, or any relative of such director or partner;

(v) A company or firm of which a director, partner or member has a substantial interest in the business or profession of the taxpayer or any director or partner of such company or firm, or any relative of such director or partner;

(vi) Any person who carries on a business or profession:

- **Where the taxpayer, being an individual, or any relative of the taxpayer, has a substantial interest in the business or profession of that person; or**

- **Where the taxpayer, being a company or a firm, any director of such company or partner of such firm, or any relative of such director or partner, has a substantial interest in the business or profession of that person.**

Note: **For this purpose, a person will be deemed to have a substantial interest in a business or profession, if:**

(i) In a case in which the business or profession is carried on by a company, such person is, at any time during the previous year, the beneficial owner of shares (not being shares entitled to a fixed rate of dividend whether with or without a right to participate in profits) carrying not less than 20% of the voting power; and

(ii) In any other case, such person is, at any time during the previous year, beneficially entitled to not less than 20% of the profits of the business or profession. [381]

---

[381] **ITA, Sec. 40A(2).**

---

t. Interest Paid with Respect to Capital Borrowed for Specific Purposes

Interest paid with respect to capital borrowed for purposes of a business or profession is allowed as a deduction in computing income from the business or profession. A deduction is not allowed with respect to interest paid on capital used to acquire an asset to extend an existing business or profession for any period beginning from the date on which the capital was borrowed to acquire the asset to the date on which the asset is first put to use. [382]

---

[382] **ITA, Sec. 36(1)(iii).**

---

u. Discount on Zero Coupon Bonds

A deduction is allowed of the *pro rata* amount of discount on a zero coupon bond, having regard to the life of the bond and calculated in the manner prescribed. [383]

---

[383] **ITA, Sec. 36(1)(iiia).**

---

6. Set-off and Carryforward of Losses and Depreciation

The ITA provides for the set-off and carryforward of losses as described in a to d, below.

a. Set-off of Losses

A taxpayer that incurs a loss in an assessment year with respect to any source under any category of income is entitled to have the amount of the loss set off against his income from any other source under the same category of income. Short-term capital losses may be set off only against short-term capital gains and long-term capital losses are set off only against long-term capital gains. [384]

---

[384] ITA, Sec. 70.

Where in a tax year, the net result of the computation under any category of income other than "Capital gains" is a loss and the taxpayer has no income under the head "Capital gains," the loss will be set off against the income, if any, assessable under any other category of income for that year. This rule is subject to the following exceptions:

(i) Losses of a "speculation business" [385] may be set off only against profits of a "speculation business;"

(ii) Losses incurred in a business of owning and maintaining race horses may be set off only against income from that business;

(iii) Losses computed under the category "Profits and gains of business or profession" may not be set off against income under the category of "Salaries;" and

(iv) Losses under the category of "Capital gains" may not be set off against income under any other category. [386]

---

[385] "Speculation business" refers to a transaction in which a contract for the purchase or sale of any commodity, including stocks and shares, is periodically or ultimately settled otherwise than by actual delivery or transfer of the commodity or scrip.

[386] ITA, Sec. 71.

---

b. Set-off and Carryforward of Unabsorbed Depreciation

Unabsorbed depreciation allowance of the current year may be set off against any business or nonbusiness income of the same tax year.

Unabsorbed depreciation allowance of past years may be set off against income under any head of income in subsequent years. [387]

---

[387] ITA, Sec. 32(2).

Note: **The order of precedence for the setoff of unabsorbed depreciation allowance and losses is:**

(i) Current year's depreciation;

(ii) Unabsorbed carryforward losses; and

(iii) Unabsorbed depreciation.

The legal fiction of the ITA is to have the unabsorbed carryforward depreciation partake of the same character as current depreciation in the following year so that it is available, unlike carryforward business losses, for set-off against other heads of income of that year. As this is the purpose for which the legal fiction was created, the fiction must be confined to that purpose. It may not be argued that, because of the legal fiction, unabsorbed carryforward losses should be given preference not only over unabsorbed carryforward depreciation but also over current year's depreciation. [388]

---

[388] *CIT v. Mother India Refrigeration Industries P. Ltd.* and *Hindustan Vacuum Glass Ltd. v. CIT* (S.C.) 155 I.T.R. 711 [1985].

The Gujarat High Court has held that unabsorbed depreciation may be carried forward and set off against income of a subsequent year even if the business ceases to exist. [389]

[389] *Anant Mills Co. Ltd. (In Liquidation) v. CIT (Gujarat)* 212 I.T.R. 72 [1995].

c. Carryforward of Losses

(1) General

Where a loss cannot be set off because of an absence or insufficiency of taxable income of the same year, it may be carried forward and set off against income of a subsequent year. Under the ITA, the following losses are permitted to be carried forward and set off:

(i) Losses of a business or profession (including losses of a speculation business);

(ii) Losses arising on the transfer of capital assets;

(iii) Losses arising from the activity of owning and maintaining race horses; and

(iv) Losses from house property.

(2) Business Losses Other than Speculation Losses

Business losses other than speculation losses may be carried forward and set off against the profits of any business or profession of the taxpayer in a subsequent year.

A loss may not be carried forward for more than the eight assessment years immediately succeeding the tax year in which the loss was first computed. [390]

[390] ITA, Sec. 72.

Note: **A loss may not be carried forward unless it is determined pursuant to a return filed by the due date. [391] In the case of a company other than a company in which the public is substantially interested, if 51% or more of the shareholding is beneficially transferred, the loss incurred in a tax year may not be carried forward and set off in subsequent years. [392]**

[391] ITA, Sec. 80.

[392] ITA, Sec. 79.

(3) Speculation Losses

Losses of a speculation business may be carried forward to subsequent years and set off only against the profits of a speculation business carried on in the year of set-off. Speculation losses may be carried forward for four assessment years immediately succeeding the tax year in which they were first computed. [393]

[393] ITA, Sec. 73.

(4) Capital Losses

Long-term capital losses may be carried forward to subsequent years and set off only against long-term capital gains. Short-term capital losses may be carried forward to subsequent years and set off against any capital gains, whether short-term or long-term. Capital losses may be carried forward for eight assessment years immediately succeeding the tax year in which they were first computed. [394]

[394] ITA, Sec. 74.

Long-term capital losses on the sale of listed securities and units may not be set off or carried forward against long-term capital gains as long-term capital gains on the sale of such securities and units are exempt under Section 10(38) of the ITA.

(5) Losses Incurred in a Business of Owning and Maintaining Race Horses

Losses incurred in a business of owning and maintaining race horses may be carried forward to a subsequent year and set off only against income from the activity of owning and maintaining race horses. Such losses may be carried forward only if the activity of owning and maintaining race horses is carried on by the taxpayer in the previous year against the income of which the brought forward losses are sought to be set off. Such losses are permitted to be carried forward for four assessment years immediately succeeding the tax year in which they were first computed. [395]

[395] ITA, Sec. 74A.

(6) Losses Incurred Under the Head "House Property"

Losses incurred under the head "House property" may be carried forward to subsequent years and set off only against "income from House property." Such losses are permitted to be carried forward for eight assessment years immediately succeeding the tax year in which they were first computed. [396]

[396] ITA, Sec. 71B.

(7) Losses Incurred in a Specified Business

Losses from a "specified" business under section 35AD of the ITA (see 5, f, above) may be set off only against profits and gains from a "specified" business. Unabsorbed losses may be carried forward to subsequent assessment years without limit. [397]

[397] ITA, Sec. 73A.

d. Carryforward and Set-off on Amalgamation or Demerger

In certain circumstances, where there has been an amalgamation of: a company owning an industrial undertaking or a ship or a hotel with another company; a banking company referred to in Clause (c) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949) with a specified bank; or one or more public sector companies engaged in the business operating aircraft, with one or more public sector companies engaged in similar business, the accumulated losses or unabsorbed depreciation of the amalgamating company are regarded as the losses or unabsorbed depreciation of the amalgamated company for the taxable year in which the amalgamation was effected. Consequently, other provisions of the ITA relating to the carryforward and set-off of losses and allowances for depreciation apply. [398]

[398] ITA, Sec. 72A.

Since the unabsorbed losses of the amalgamating company are deemed to be losses for the taxable year in which the amalgamation was effected, the amalgamated company has the right to carryforward the losses for the period of eight assessment years immediately following the assessment year relevant to the taxable year in which the amalgamation was effected.

For purposes of the above, "industrial undertaking" means any undertaking that is engaged in:

(i) The manufacture or processing of goods;

(ii) The manufacture of computer software;

(iii) The business of generating or distributing electricity or any other form of power;

(iv) The business of providing telecommunication services, whether basic or cellular, including radio paging, domestic satellite services, network of trunking, broadband network and internet services.

(v) Mining; or

(vi) The construction of ships, aircraft or rail systems.

The conditions that must be met for the provisions referred to above to apply in the assessment of the amalgamated company are as follows:

(i) The amalgamating company must be engaged in the business in which the accumulated loss occurred or the depreciation remains unabsorbed, for three or more years;

(ii) The amalgamating company must have held continuously, as of the date of amalgamation, at least three-fourths of the book value of the fixed assets held by it two years prior to the date of amalgamation;

(iii) The amalgamated company must hold continuously for a minimum period of five years from the date of amalgamation at least three-fourths of the book value of the fixed assets of the amalgamating company acquired in the scheme of amalgamation;

(iv) The amalgamated company must continue the business of the amalgamating company for a minimum period of five years from the date of amalgamation; and

(v) The amalgamated company must fulfill such other conditions as may be prescribed to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for a genuine business purpose.

If these conditions are not satisfied, the set-off of losses or allowances for depreciation granted in any tax year to the amalgamated company is deemed to be income of the amalgamated company chargeable to tax for the year in which the conditions are not satisfied.

In the case of a demerger:

(i) Where the loss or unabsorbed depreciation can be directly related to the undertakings transferred to the resulting company, it is allowed to be carried forward and set off in the hands of the resulting company; and

(ii) Where the loss or unabsorbed depreciation cannot be directly related to the undertakings transferred to the resulting company, it is apportioned between the demerged company and the resulting company in the proportion that the assets of the undertakings have been retained by the demerged company and transferred to the resulting company, and is allowed to be carried forward and set off in the hands of the demerged company or the resulting company.

The central government may, by notification, specify such conditions as it considers necessary to ensure that a demerger is for genuine business purposes.

Where there has been a business reorganization, as a result of which a firm is succeeded by a company fulfilling the conditions laid down in Clause (xiii) of Section 47 of the ITA or a proprietary concern is succeeded by a company fulfilling the conditions laid down in Clause (xiv) of Section 47 (see 4, d, above), the accumulated loss and the unabsorbed depreciation of the predecessor firm or proprietary concern is deemed to be the loss or allowance for depreciation of the successor company for purposes of the tax year in which the business reorganization was effected, and the other provisions of the ITA relating to the set-off and carryforward of losses and allowances for depreciation apply accordingly.

However, if any of the conditions laid down in Clause (xiii) or Clause (xiv) of Section 47 of the ITA are not met, the set-off of losses or allowances for depreciation granted in any tax year to the successor company will be deemed to be income of the company chargeable to tax in the year in which the conditions are not satisfied.

Where there has been a business reorganization, as a result of which a private company or an unlisted public company is succeeded by a limited liability partnership fulfilling the conditions laid down in Clause (xiiib) of Section 47 of the ITA (see 9, k, below), then the accumulated loss and the unabsorbed depreciation of the predecessor company are deemed to be the loss and allowance for depreciation of the successor limited liability partnership for the purpose of the tax year in which the business reorganization was effected and other provisions of the ITA relating to the set-off and carryforward of loss and allowance for depreciation apply accordingly.

However, if any of the conditions laid down in Clause (xiiib) of Section 47 of the ITA (see 9, k, below) are not met, then the set-off of loss or allowance for depreciation made in any tax year in the hands of the successor limited liability partnership is deemed to be income of the limited liability partnership chargeable to tax in the year in which the conditions are not satisfied.

For this purpose:

(i) "Accumulated loss" means so much of the loss of the predecessor firm or proprietary concern, private company or unlisted public company before conversion into a limited liability partnership, or the amalgamating company or the demerged company, as the case may be, under the head "Profits and gains of business or profession" (not being a loss sustained in a speculation business) as the predecessor firm, the proprietary concern, or the company or amalgamating or demerged company, would have been entitled to carry forward and set off, if the business reorganization, conversion, amalgamation or demerger had not taken place.

(ii) "Unabsorbed depreciation" means so much of the allowance for depreciation of the predecessor firm or proprietary concern, private company or unlisted public company before conversion into a limited liability partnership, or the amalgamating company or the demerged company that remains to be allowed and that would have been allowed to the predecessor firm, the proprietary concern or the company or amalgamating company or demerged company, if the business reorganization or conversion or amalgamation or demerger had not taken place.

(iii) "Specified bank" means the State Bank of India constituted under the State Bank of India Act, 1955 (23 of 1955), a subsidiary bank as defined in the State Bank of India (Subsidiary Banks) Act, 1959 (38 of 1959) or a corresponding new bank constituted under Section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 (5 of 1970) or under Section 3 of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980 (40 of 1980).

Where an undertaking entitled to a deduction is transferred before the expiry of the specified period to another Indian Company in a scheme of amalgamation or demerger:

(i) The amalgamating or demerged company will not be entitled to a deduction from profits in the tax year in which the amalgamation or demerger takes place; and

(ii) The amalgamated or resulting company will be able to claim the benefit of a deduction from profits as if the amalgamation or demerger had not taken place.

7. Tax Rates

a. Individuals

Income tax rates for individuals are as follows:

Woman resident in India under 65 years old	
Up to Rs. 190,000	**Nil**
From Rs. 190,001 to Rs. 500,000	**10% of excess over Rs. 190,000**
From Rs. 500,001 to Rs. 800,000	**Rs. 31,000 + 20% of excess over Rs. 500,000**
Above Rs. 800,000	**Rs. 91,000 + 30% of excess over Rs. 500,000**
Senior Citizen resident in India 65 years old or older	
Up to Rs. 240,000	**Nil**
From Rs. 240,001 to Rs. 500,000	**10% of excess over Rs. 240,000**
From Rs. 500,001 to Rs. 800,000	**Rs. 26,000 + 20% of excess over Rs. 500,000**
Above Rs. 800,000	**Rs. 86,000 + 30% of excess over Rs. 800,000**
Any other Individual	
Up to Rs. 160,000	**Nil**
From Rs. 160,001 to Rs. 500,000	**10% of excess over Rs. 160,000**
From Rs. 500,001 to Rs. 800,000	**Rs. 34,000 + 20% of excess over Rs. 500,000**
Above Rs. 800,000	**Rs. 94,000 + 30% of excess over Rs. 800,000**

An education tax (cess) of 3% is charged on the tax.

b. Companies

The following rates apply to companies:

Type of Company — Source of Income	Rates of Income Tax Assessment Year 2011-12 % of Total Taxable Income
Domestic company	**30%**
Foreign company — on income from royalties, fees for technical services effectively connected with a PE or fixed base, as referred to in VI, C, 7, below	**40% (on net income)**
Foreign company — on income other than that to which special rates apply (see VI, C, below)	**40%**

Companies are required to pay a surcharge if their taxable income exceeds Rs.10 million as follows:

(i) Domestic companies: 7.5%.

(ii) Other companies: 2.5%.

An education tax (cess) of 3% is charged on the aggregate tax including surcharge.

c. Minimum Alternate Tax

The book profits of a company the tax liability of which is less than 18% of its book profits will be deemed to be the company's total income chargeable to tax at the rate of 18%. "Book profits" means the net profits for the relevant tax year as shown in the profit and loss account prepared in accordance with the provisions of the Companies Act.

In preparing the annual accounts, including the profit and loss account, the accounting policies, the accounting standards adopted for preparing such accounts, including the profit and loss account and the method and rates adopted for calculating depreciation must be the same as those adopted for purposes of preparing such accounts (including the profit and loss account) and laid before the company at its annual general meeting, unless the company has adopted or adopts a financial year under the Companies Act that is different from the tax year. In the latter case, they must correspond to the accounting policies, accounting standards and rates for calculating

depreciation adopted in preparing such accounts (including the profit and loss account) for such financial year or part thereof as falls within the relevant tax years.

The book profits are to be increased by the following amounts (if these have been debited to the profit and loss account):

(i) The amount of income tax paid or payable and any provision for income tax payable, including the following:

- **Any tax on distributed profits under Section 115-O of the ITA or on distributed income under Section 115R (see 8, below);**
- **Any interest charged under the ITA;**
- **Any surcharge levied;**
- **The education cess on income tax, if any, as levied; and**
- **The secondary and higher education cess on income tax, if any, as levied;**

(ii) Amounts carried to reserves by whatever name called other than reserves of shipping companies specified under Section 33AC of the ITA;

(iii) Any amount or amounts set aside to provide for meeting liabilities, other than ascertained liabilities;

(iv) Any amount set aside by way of provision for losses of subsidiaries;

(v) The amount of dividends paid or proposed to be paid;

(vi) Expenditure attributable to income that is exempt from tax;

(vii) The amount of depreciation;

(viii) The amount of deferred tax and the provision therefor; and

(ix) The amount or amounts set aside as a provision for the diminution in value of any asset.

The "book profits" are to be decreased by the following sums (if these have been credited to the profit and loss account):

(i) Any amount withdrawn from any reserves or provisions excluding reserves created before April 1, 1997. However, a reserve created after April 1, 1997, is not required to be reduced unless the profit was increased by the reserve in calculating the minimum alternate tax in an earlier year;

(ii) The amount exempt under Section 10 of the ITA other than long-term capital gains on listed securities;

(iii) The amount of depreciation debited to the profit and loss account, excluding depreciation on account of the revaluation of assets;

(iv) The amount withdrawn from the revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of the revaluation of assets;

(v) The amount of any loss brought forward or unabsorbed depreciation, whichever is less according to the books of account (for this purpose, loss does not include depreciation). If the amount of loss brought forward or unabsorbed depreciation is zero, no reduction is required;

(vi) The profits of an industrial company commencing from the tax year in which the company became a "sick" industrial company under the provisions of the now repealed Sick Industrial Companies (Special Provisions) Act, 1985 and ending with the tax year in which the company's entire net worth equals or exceeds its accumulated losses;

(vii) The amount of deferred tax, if any.

The above provisions do not affect the determination of the amounts of unabsorbed depreciation, business loss, speculation loss or capital gains relevant to the tax year and to be carried forward to the subsequent year or years.

Every company to which this section applies must furnish a report in the prescribed form from an accountant, certifying that the book profit has been computed in accordance with the provisions of the section, along with the return of income.

Except as provided above, the other provisions of the ITA will continue to apply to such companies.

The above provisions do not apply to income from business carried on, or services rendered, by an entrepreneur or a developer, in a unit or an SEZ. [399]

[399] ITA, Sec. 115JB.

Where any tax has been paid as discussed above, the taxpayer will be entitled to a credit with respect to the tax so paid. The difference between the minimum alternate tax paid and the tax liability in accordance with the other provisions of the ITA, is considered to be the tax credit.

However, the benefit of the tax credit will not be available to a limited liability partnership where a private or unlisted company is converted into a limited liability partnership.

The tax credit is permitted only in the tax year in which tax is payable in accordance with the other provisions of the ITA and may carried forward for set-off for 10 assessment years succeeding the year in which it was first allowable. [400]

[400] ITA, Sec. 115JAA.

8. Dividends and Income Distributions

Any dividend declared, distributed or paid by a domestic company is chargeable to additional income tax, i.e., tax on distributed profits at the rate of 15% in the hands of the domestic company. A surcharge of 10% of such tax is also payable. A further education tax (cess) of 3% is charged on the aggregate tax, including the surcharge. A dividend is not again taxable in the hands of the recipient.

The amount of the dividends referred to above is reduced by the amount of the dividends, if any, received by the domestic company during the financial year, if:

(i) Those dividends are received from a subsidiary;

(ii) The subsidiary has paid tax, as described above, on those dividends; and

(iii) The domestic company is not a subsidiary of any other company.

The same dividend amount may not be taken into account for reduction more than once. [401]

[401] ITA, Sec. 115-O.

Any amount of income distributed by a mutual fund to its unit holders is chargeable to income tax at the rate of:

- **25% on income distributed by a money market mutual fund or a liquid fund;**
- **12.5% on income distributed to any person being an individual or HUF by a fund other than a money market mutual fund or a liquid fund; and**
- **20% on income distributed to any other person by a fund other than a money market mutual fund or a liquid fund.**

A surcharge of 10% is payable on the distribution tax. A further education tax (cess) of 3% is charged on the aggregate tax, including the surcharge. Such income is not again taxable in the hands of the recipient.

The distribution tax does not apply to income distributed by equity-oriented funds.

The tax on distributed profits paid by a company is treated as the final payment of tax with respect to the amount declared, distributed or paid as dividends and no further credit may be claimed by the company or by any other person with respect to the amount of tax so paid.

No deduction under any other provisions of the ITA will be allowed to the company or a shareholder with respect to the amount charged to tax as described above or the tax thereon.

Notwithstanding the above, no tax on distributed profits is chargeable with respect to the total income of an undertaking or enterprise engaged in developing, developing and operating, or developing, operating and maintaining an SEZ for any assessment year on any amount declared, distributed or paid by such developer or enterprise, by way of dividends (whether interim or otherwise) out of its current income either in the hands of the developer or enterprise, or the persons receiving the dividends. [402]

[402] ITA, Sec. 115-R.

9. Tax Concessions

a. General

As an integral part of its policy of promoting industrialization, the government of India has provided a host of tax incentives to new industries as well as to existing industries to encourage expansion and to gain the benefits of economies of scale.

In addition to a tax holiday (a 10-year tax concession for industrial undertakings, ships and hotel businesses), there are tax incentives for: industrial undertakings in free trade zones (FTZs); 100% export-oriented undertakings; investment in infrastructure projects, power generation and projects executed outside India; and hotels and foreign tourist businesses. See VI. E, below for special tax concessions available to nonresidents.

The Special Economic Zones Act, 2005, which entered into force from July 13, 2005, has significantly promoted exports and foreign direct investment into India. The Act provides for the establishment, development and management of SEZs for the promotion of exports and for matters connected therewith or incidental thereto.

The central government guidelines for designation as an SEZ are as follows:

(i) The generation of additional economic activity;

(ii) The promotion of exports of goods and services;

(iii) The promotion of investment from domestic and foreign sources;

(iv) The creation of employment opportunities;

(v) The development of infrastructure facilities; and

(vi) The maintenance of the sovereignty and integrity of India, the security of the state and friendly relations with foreign states.

An SEZ may involve both processing and nonprocessing areas, as follows:

(i) A processing area for setting up units for activities, i.e., the manufacture of goods or the rendering services;

(ii) An area exclusively for trading or warehousing purposes; or

(iii) Nonprocessing areas for activities other than those specified above in (i) and (ii).

Subject to such terms, conditions and limitations as may be prescribed, a unit in an SEZ or a developer will be exempt from the payment of taxes, duties or cess under all enactments specified in the First Schedule of the Special Economic Zones Act, 2005 and the rules drawn up thereunder.

b. Concession for Industrial Undertakings in Free Trade Zones

A taxpayer that derives profits and gains from an undertaking for the export of articles, "things" or computer software is entitled to a deduction from total income for a period of 10 consecutive assessment years beginning with the tax year relevant to the assessment year in which the undertaking begins to manufacture the articles, etc.

The amount of the deduction is an amount that bears to the profits of the business the same proportion as the export turnover with respect to the articles, etc. bears to the total turnover of the business carried on by the undertaking. Further, the deduction is allowed only if the sale proceeds of the articles, etc. are brought into India by the taxpayer in convertible foreign exchange within six months of the close of the accounting year or such further period as the competent authority may allow for this purpose.

Profits and gains derived from the on-site development of computer software (including services for the development of computer software) outside India are deemed to be profits and gains derived from the export of computer software outside India.

The deduction in computing the total income of an undertaking that begins to manufacture or produce articles or things or computer software during the tax year relevant to any assessment year commencing on or after April 1, 2003, in any SEZ is 100% of the profits and gains derived from the export of the articles, things or computer software for a period of five consecutive assessment years beginning with the assessment year relevant to the tax year in which the undertaking begins to manufacture or produce the articles, things or computer software, and, thereafter, 50% of such profits and gains for a further two consecutive assessment years.

An undertaking is entitled to a further deduction for the next three consecutive assessment years. The amount of the deduction may not exceed 50% of the amount of profits and the undertaking is required to debit the profit and loss account of the previous year with respect to which the deduction is claimed and credit the same to a reserve account (to be called the "Special Economic Zone Re-investment Allowance Reserve Account"). The deduction is subject to the

following conditions:

(i) The amount credited to the reserve account is to be used:

(a) For purposes of acquiring new machinery or plant (the asset concerned must first be put to use before the expiry of a period of three years following the previous year in which the reserve was created); and

(b) For purposes of the business of the undertaking other than for distribution by way of dividends or profits or for remittance outside India as profits or for the creation of any asset outside India, until the asset referred to in (a) is acquired.

(ii) The prescribed particulars with respect to the new machinery or plant must be furnished by the taxpayer along with the return of income for the assessment year relevant to the previous year in which the plant or machinery was first put to use.

Where the amount credited to the Special Economic Zone Re-investment Allowance Reserve Account has been used for any purpose other than those referred to above or has not been used before the expiry of the period specified above, the amount is regarded as profits of the year in which the amount is so used or the year immediately following the period of three years specified above and will be charged to tax accordingly.

Where, in computing the total income of the undertaking for any assessment year, its profits and gains were exempt under the provision applicable immediately before its substitution by the Finance Act, 2000, the undertaking will be entitled to a deduction only for the unexpired portion of the 10 consecutive assessment years referred to above.

If an undertaking initially located in an FTZ or an export processing zone (EPZ), is subsequently relocated in an SEZ as a result of the conversion of the FTZ or EPZ into an SEZ, the period of 10 consecutive assessment years referred to above is reckoned from the tax year relevant to the assessment year in which the undertaking was first set up in the FTZ or EPZ.

The above deduction will not be allowed to any undertaking for the assessment year beginning April 1, 2012, or subsequent assessment years.

An undertaking must fulfill the following conditions to claim the exemption:

(i) The undertaking must begin to manufacture or produce articles, etc.:

- **On or after March 31, 1981, in an FTZ;**
- **On or after March 31, 1994, in an Electronic Hardware Technology Park (EHTP) or a Software Technology Park (STP);**
- **On or after March 31, 2001 in an SEZ.**

(ii) The undertaking must not be formed by the splitting up or reconstruction of a business already in existence; and

(iii) The undertaking must not be formed by the transfer to a new business of machinery and plant previously used for any purpose.

The benefit from this concession is subject to the following restrictions:

(i) Any amount representing unabsorbed depreciation, unabsorbed investment allowance or unabsorbed capital expenditure on scientific research of the tax holiday period is not allowed to be carried forward or set off against the profits of any subsequent year;

(ii) Any losses relating to the business of the undertaking and any capital losses in relation to the tax holiday period of the business of the undertaking may not be carried forward or set off against the profits of any subsequent year;

(iii) The taxpayer is not entitled to claim the benefits of the tax holiday under Sections 80-IA or 80-IB of the ITA (see f, below); and

(iv) On the expiration of the tax holiday period, in computing the depreciation allowance, the written down value of any asset used for purposes of the business of the undertaking is computed as if the taxpayer had claimed and actually been allowed the deduction with respect to depreciation for each of the tax years in the holiday period.

Where there is a transfer of an undertaking to another Indian company in a scheme of amalgamation or demerger, before the expiry of the period specified:

(i) No deduction is allowed to the amalgamating or the demerged unit for the tax year in which the amalgamation or the demerger takes place; and

(ii) The concessions described here apply as they would have applied to the amalgamating or the demerged unit if the amalgamation or demerger had not taken place.

The taxpayer may choose not to avail himself of this tax concession by furnishing a declaration to this effect, in writing, along with his income tax return.

Comment: **The ITA provides this option because some taxpayers may find the general tax concessions available in relation to all undertakings more attractive than the deductions under Section 10A of the ITA described above.**

The deduction is not allowed unless the income tax return of the taxpayer is accompanied by an audit report from an accountant stating that the deduction has been correctly claimed.

The tax concessions set out above do not apply to an undertaking that begins to manufacture or produce approved articles or things, or to provide any services, on or after April 1, 2006, in any SEZ to which the Special Economic Zones Act, 2005 applies. Such undertakings are eligible for tax concessions under section 10AA of the ITA (see d, below).[403]

---

[403] **ITA, Sec. 10A.**

---

c. Concession for 100% Export-Oriented Undertakings

A taxpayer that derives profits and gains from an approved 100% export-oriented undertaking for the export of articles, things or computer software is entitled to a deduction from total income, as described below, for a period of 10 consecutive assessment years beginning with the tax year relevant to the assessment year in which the undertaking begins to manufacture the articles, etc.

The amount of the deduction is an amount that bears to the profits of the business the same proportion as the export turnover with respect to the articles, etc. bears to the total turnover of the business carried on by the undertaking. Further, the deduction is allowed only if the sale proceeds of the articles, etc. are brought into India by the taxpayer in convertible foreign exchange within six months of the close of the accounting year or such further period as the competent authority may allow for this purpose.

Profits and gains derived from the on-site development of computer software (including services for the development of computer software) outside India are deemed to be profits and gains derived from the export of computer software outside India. Where, however, in computing the total income of the undertaking for any assessment year, its profits and gains were exempt under the provision applicable immediately before its substitution by the Finance Act, 2000, the undertaking is entitled to a deduction only for the unexpired portion of the 10 consecutive assessment years referred to above.

The deduction will not be allowed to any undertaking for the assessment year beginning on April 1, 2012 or subsequent assessment years.

An undertaking must fulfill the following conditions to be able to claim the deduction:

(i) The undertaking must manufacture or produce articles, things or computer software;

(ii) The undertaking must not be formed by the splitting up or reconstruction of a business already in existence; and

(iii) The undertaking must not be formed by the transfer to a new business of machinery and plant previously used for any purpose.

No deduction is available to a taxpayer who does not furnish his return of income within the time prescribed under Section 139 of the ITA (see 11, c, below).

The benefit from this concession is subject to the following restrictions:

(i) Any amount representing unabsorbed depreciation, unabsorbed investment allowance or unabsorbed capital expenditure on scientific research of the tax holiday period is not allowed to be carried forward or set off against the profits of any subsequent year;

(ii) Any losses relating to the business of the undertaking and any capital losses in relation to the tax holiday period of the business of the undertaking are not permitted to be carried forward or set off against the profits of any subsequent year;

(iii) The taxpayer is not entitled to claim the benefits of the tax holiday under Section 80-IA or Section 80-IB of the ITA (see f, below); and

(iv) On the expiration of the tax holiday period, in computing the depreciation allowance, the written down value of any asset used for the purpose of the business of the undertaking is computed as if the taxpayer had claimed and been actually allowed the deduction with respect to depreciation for each of the assessment years in the tax holiday period.

Where there is a transfer of an undertaking to another Indian company in a scheme of amalgamation or demerger, before the expiry of the period specified:

(i) No deduction is allowed to the amalgamating or the demerged unit for the tax year in which the amalgamation or the demerger takes place; and

(ii) The concessions described here apply as they would have applied to the amalgamating or the demerged unit if the amalgamation or demerger had not taken place.

The taxpayer may choose not to avail himself of this tax concession by furnishing a declaration to this effect, in writing, along with his income tax return.

Comment: **The ITA provides this option because some taxpayers may find the general tax concessions available in relation to all undertakings more attractive than the provisions of Section 10B of the ITA.**

The deduction is not allowed unless the income tax return of the taxpayer is accompanied by an audit report from an accountant stating that the deduction has been correctly claimed. [404]

---

[404] ITA, Sec. 10B.

---

d. Special Provisions with Respect to Newly Established Units in Special Economic Zones

A unit set up in an SEZ that begins to manufacture or produce articles or things, or to provide services on or after April 1, 2005, is entitled to a deduction of:

(i) 100% of the profits and gains derived from the export of articles or things or from providing services, for a period of five consecutive tax years from the tax year in which the unit begins to manufacture or produce such articles or things, or to provide services, and 50% of such profits and gains for a further five tax years; and

(ii) For the next five consecutive tax years, so much of the amount not exceeding 50% of the profit as is debited to the profit and loss account of the tax year for which the deduction is to be allowed and credited to a reserve account (to be called the "Special Economic Zone Re-investment Reserve Account") to be created and utilized for purposes of the business of the taxpayer in the manner laid down.

The amount credited to the Special Economic Zone Reinvestment Reserve Account is to be utilized:

(i) For purposes of acquiring machinery or plant that is first put to use before the expiry of a period of three years following the tax year in which the reserve was created; and

(ii) Until the acquisition of the machinery or plant as aforesaid, for purposes of the business of the undertaking other than for distribution by way of dividends or profits, for remittance outside India as profits or for the creation of any asset outside India.

The taxpayer is required to submit prescribed particulars of new machinery or plant along with the return of income for the tax year in which such machinery or plant was first put to use.

Where a Special Economic Zone Reinvestment Reserve Account has been utilized for a purpose not mentioned above or not utilized before the expiry of three years, the amount so utilized or not utilized is deemed to be profit in the year in which the amount was so utilized or, where not utilized, in the year immediately following the period of three years, and will be charged to tax accordingly.

A unit that already availed itself of a deduction under Section 10A of the ITA (see b, above) for 10 consecutive tax years is not eligible for the deduction described here.

Where a unit initially located in an FTZ or an EPZ is subsequently located in an SEZ by reason of the conversion of the FTZ or EPZ into an SEZ, the period of 10 consecutive tax years referred to above will be computed from the tax year in which the unit began to manufacture, or produce or process such articles, things or services in the FTZ or EPZ.

A unit initially located in an FTZ or an EPZ that is subsequently located in an SEZ by reason of the conversion of the FTZ or EPZ into an SEZ and that has completed the period of 10 consecutive tax years referred to above is not eligible for the deduction from April 1, 2006.

An undertaking must fulfill the following conditions to be able to claim the deduction:

(i) The undertaking must begin to manufacture or produce articles, etc., on or after March 31, 2006 in an SEZ;

(ii) The undertaking must not be formed by the splitting up or reconstruction of a business already in existence; and

(iii) The undertaking must not be formed by the transfer to a new business of machinery and plant previously used for any purpose.

Where a unit is transferred, before the expiry of the period specified, to another undertaking, being a unit, in a scheme of amalgamation or demerger:

(i) No deduction is allowed to the amalgamating or the demerged unit, being a company, for the tax year in which the amalgamation or the demerger takes place; and

(ii) The concessions described here apply as they would have applied to the amalgamating or the demerged unit, being a company, as if the amalgamation or demerger had not taken place.

Losses of the unit, in so far as such loss relates to the business of the undertaking being a unit, will be allowed to be carried forward or set off.

The deduction is not allowed unless the income tax return of the taxpayer is accompanied by an audit report from an accountant stating that the deduction has been correctly claimed.

The amount of the deduction is an amount that bears to the profits of the business of the undertaking, the same proportion as the export turnover with respect to such articles or things or services bears to the total turnover of the business carried on by the undertaking. [405]

---

[405] ITA, Sec. 10AA.

---

e. Concessions for Public Financial Institutions, Banks, etc.

Notwithstanding the other taxing provisions of the ITA, where the income of a public financial institution, a scheduled bank, a state financial corporation, a state industrial investment corporation or a public company includes interest on such categories of bad or doubtful debts as may be prescribed in terms of the guidelines issued by the RBI or the National Housing Bank, respectively, such income is chargeable to tax in the year in which it is credited to the profit and loss account or when it is received, whichever is earlier.

For this purpose "public company" means a company:

(i) That is a public company as defined under the Companies Act;

(ii) The main object of which is to carry on the business of providing long-term finance for the construction or purchase of houses in India for residential purposes; and

(iii) That is registered in accordance with the Housing Finance Companies (NHB) Directions, 1989 under the National Housing Bank Act, 1987. [406]

---

[406] ITA, Sec. 43D.

---

f. Tax Holiday

(1) Industrial Undertakings and Enterprises Engaged in Infrastructure Development

Industrial undertakings and enterprises engaged in infrastructure development are entitled to a benefit by way of a deduction of 100% of business profits for 10 consecutive assessment years within a block of 15 years, commencing from the year in which the activity begins, except undertakings or enterprises described below in (i), for which the deduction is 100% of business profits for five years and 30% of the business profits for the following five years. For industrial undertakings or enterprises described below in (iv), the block is extended to 20 years for activities other than port, airport, inland waterway, inland port activities or navigational channels in the sea.

Industrial undertakings that are eligible for the deduction are those engaged in:

(i) Providing telecommunications services, whether basic or cellular, including radio paging, domestic satellite services, network of trunking, broadband network and internet services;

(ii) Developing, operating and maintaining an industrial park or SEZ notified by the central government in

accordance with the scheme drawn up in this regard;

(iii) Generating or generating and distributing power, or transmitting or distributing power by laying a network of new transmission or distribution lines, or undertaking the substantial renovation and modernization of existing transmission or distribution lines; or

(iv) Developing any infrastructure facility; operating and maintaining any infrastructure facility; or developing, operating and maintaining any infrastructure facility. [407]

---

[407] An "infrastructure facility" for this purpose means: (i) A road including a toll road, a bridge or a rail system; (ii) a highway project including housing or other activities that are an integral part of the highway project; (iii) a water supply project, a water treatment system, an irrigation project, a sanitation and sewerage system, or a solid waste management system; or (iv) a port, an airport, an inland waterway, an inland port or navigational channel in the sea.

The following conditions must be fulfilled for the deduction to be made available:

(a) As regards an undertaking or enterprise referred to above in (i) (telecommunications services), the undertaking or enterprise must begin to provide telecommunications services, whether basic or cellular, including radio paging and domestic satellite services, or broadband network or internet services, at any time after March 31, 1995 and before April 1, 2005.

(b) As regards an undertaking or enterprise referred to above in (ii), the undertaking must develop, develop and operate, or maintain and operate an industrial park or SEZ notified by the central government for the period beginning after March 31, 1997, and ending before April 1, 2011 (2009 in case of a SEZ), in accordance with the scheme drawn up by the government.

(c) As regards an undertaking or enterprise referred to above in (i) (telecommunications) or (iii) (power transmission/distribution lines), the undertaking or enterprise must not have been formed by:

- **The splitting up or reconstruction of a business already in existence; or**
- **The transfer to a new business of machinery or plant previously used for any purpose.**

(d) With regard to an undertaking or enterprise referred to above in (iii) (power transmission/distribution lines), the undertaking or enterprise must:

- **Begin to generate power, or generate and distribute power after March 31, 1993, and before April 1, 2011;**
- **Commence the transmission or distribution of power by laying a network of new transmission or distribution lines at any time after March 31, 1999, and before April 1, 2011; and**
- **Undertake substantial renovation and modernization of an existing network of transmission or distribution lines at any time after April 1, 2004, and before April 1, 2011. An increase in the plant and machinery in the network of transmission or distribution lines by at least 50% of the book value of such plant and machinery as of April 1, 2004, is treated as "substantial renovation and modernization."**

(e) As regards an undertaking or enterprise referred to above in (iv) (infrastructure facility), the undertaking or enterprise must:

- **Be owned by an Indian company or a consortium of Indian companies;**
- **Have entered into an agreement with the central government, a state government, a local authority or a statutory body for developing, maintaining and operating a new infrastructure facility; and**
- **Have commenced operating and maintaining the infrastructure facility on or after April 1, 1995.**

The following are the important considerations for eligibility for the above tax concessions.

The profits and gains of the business to which the above concession applies must, for purposes of determining the quantum of the deduction for the assessment year immediately succeeding the initial assessment year or any subsequent assessment year, be computed as if the business were the only source of income of the taxpayer during the tax year relevant to the initial assessment year and to every subsequent assessment year up to and including the assessment year for which the determination is to be made.

The deduction is not allowed unless the return of income of the taxpayer is accompanied by an audit report, in the prescribed form, duly verified by an accountant and stating that the deduction has been correctly claimed.

Where, in the opinion of the Assessing Officer, the computation of the profits and gains of the eligible business in the

manner specified above presents exceptional difficulties, the Assessing Officer may compute the profits and gains on such reasonable basis as he may deem fit.

Where any amount of profits and gains of an undertaking or enterprise is claimed and allowed as described above for any assessment year, a deduction to the extent of such profits and gains will not be allowed under any other provision of the ITA and will in no case exceed the profits and gains of the eligible business of the undertaking or enterprise.

The central government may, after making such inquiry as it may think fit, direct, by notification in the Official Gazette, that this exemption will not apply to any class of industrial undertaking or enterprise with effect from such date as it may specify in the notification.

Where, prior to April 1, 2007, there was a transfer of an undertaking to another Indian company in a scheme of amalgamation or demerger, before the expiry of the period specified:

(i) No deduction was allowed to the amalgamating or the demerged unit for the tax year in which the amalgamation or the demerger took place; and

(ii) The concessions described here applied as they would have applied to the amalgamating or the demerged unit if the amalgamation or demerger had not taken place. [408]

---

[408] ITA, Sec. 80IA.

---

(2) Other Industrial Undertakings

An industrial undertaking, an enterprise engaged in the shipping business or the business of a hotel, a company engaged in scientific and industrial R&D or in the commercial production or refining of mineral oil in any part of India, an undertaking developing and building housing projects, an undertaking deriving profit from the integrated business of handling, storing and transporting food grains, or an undertaking deriving profits and gains from building, owning and operating a multiplex theater or a convention center, is eligible from the year of commencement of its business or the year of approval for a deduction from its business profits, as follows:

(i) In the case of an industrial undertaking, the deduction is 30% of profits for a period of 10 years. In the case of an industrial undertaking located in an industrially backward state specified in the Eighth Schedule to the ITA (see the Worksheets), the deduction is 100% of profits for the initial five years and 30% of the profits for the next five years. In the case of an industrial undertaking located in a category A or category B industrially backward district, the deduction is increased to 100% of the profits for the initial five years or three years, and 30% of the profits for the next five years.

(ii) In the case of profits from the operation of a ship, the deduction is 30% of the profits for a period of 10 years.

(iii) In the case of a hotel located in a hilly or rural area or a place of pilgrimage, the deduction is 50% of the profits for a period of 10 years. In the case of a hotel in any other location, the deduction is 30% of the profits for a period of 10 years.

(iv) In the case of a company engaged in scientific and industrial R&D, the deduction is 100% for 10 years from the year in which the company is approved by the prescribed authority.

(v) In the case of an undertaking engaged in the commercial production or refining of mineral oil or the commercial production of natural gas in any part of India, the deduction is 100% of the profits for the initial seven years.

(vi) In the case of an undertaking engaged in developing and building housing projects, the deduction is 100% of the profits from the business.

(vii) In the case of an undertaking deriving profit from the business of processing, preserving and packaging fruits or vegetables, meat and meat products, or poultry, marine or dairy products, or from the integrated business of handling, storing and transporting food grains, the deduction is 100% of the profit for the first five tax years and 30% of the profit for the next five years.

(viii) In the case of a multiplex theater, the deduction is 50% of the profits and gains derived from the business for a period of five consecutive years beginning from the initial assessment. However, the deduction is not available to a multiplex theater located at a place within the municipal jurisdiction (whether known as a municipality, municipal corporation, notified area committee or cantonment board, or by any other name) of Calcutta, Chennai, Delhi or Mumbai.

(ix) In the case of a convention center, the deduction is 50% of the profits and gains derived from the business of building, owning and operating the convention center for a period of five consecutive years beginning from the initial assessment year.

(x) In the case of a hospital in a rural area, the deduction is 100% of the profits and gains derived from the business of operating and maintaining the hospital for a period of five consecutive years beginning from the initial assessment year.

(xi) In the case of a hospital commencing to function between April 1, 2008, and March 31, 2013, that is located anywhere in India other than the specified excluded areas, the deduction is 100% of the profits and gains derived from the business of operating and maintaining the hospital for a period of five consecutive assessment years, beginning from the initial assessment year.

The following conditions must be fulfilled for the deduction to be available:

(i) An industrial undertaking:

(a) Must not have been formed by the splitting up or reconstruction of a business already in existence;

(b) Must not have been formed by the transfer to a new business of machinery or plant previously used for any purpose;

(c) Not being an industrial undertaking referred to below in (f) or (h), must manufacture articles or things other than those specified in the list in the Eleventh Schedule to the ITA (see the Worksheets), or must operate one or more cold storage plants, in any part of India;

(d) Being an industrial undertaking that manufactures or produces articles or things, must employ 10 or more workers, if the manufacturing process is carried on with the aid of power, or 20 or more workers if the process is carried on without the aid of power;

(e) Must have begun to manufacture or produce articles or things, or to operate a plant or plants after March 31, 1991 and before April 1, 1995, or within such further period as the central government may notify;

(f) Being a small scale undertaking other than an industrial undertaking referred to below in (g) or (h), must have begun to manufacture or produce articles or things, or to operate its cold storage plant or plants after March 31, 1995, and before April 1, 2002;

(g) Being an industrial undertaking located in an industrially backward state specified in the Eighth Schedule to the ITA (see the Worksheets), must have begun to manufacture or produce articles or things, or to operate its cold storage plant or plants after March 31, 1993, and before April 1, 2004;

(h) Being an industrial undertaking located in such an industrially backward district as the central government may notify, having regard to prescribed guidelines, as an industrially backward district of category A or category B, must have begun to manufacture or produce articles or things, or to operate its cold storage plant or plants after September 30, 1994, and before April 1, 2004;

(i) Being an undertaking carrying on an integrated business of handling, storing and transporting food grains, must begin to operate such business on or after April 1, 2001; or

(j) Must have set up and must operate a cold chain facility for agricultural produce at any time after March 31, 1999, and before April 1, 2004.

(ii) A ship:

(a) Must be owned by an Indian company and wholly used for its business;

(b) Before its acquisition, must not have been owned or used in Indian territorial waters by a person resident in India; and

(c) Must have been brought into use by the Indian company after March 31, 1991, and before April 1, 1995.

(iii) A hotel:

(a) Must not have been formed by the splitting up or reconstruction of a business already in existence, or by the transfer to a new business of any building previously used as a hotel, or of any plant and machinery used for any purpose;

(b) Must be owned by (and the business must be carried on by) a company registered in India with a paid up capital of not less than Rs.500,000;

(c) If located in a hilly or a rural area, or a place of pilgrimage, or such other place other than a place within the jurisdiction of Calcutta, Chennai, Delhi or Mumbai as the central government may specify

having regard to the need for the development of infrastructure for tourism in any place and other relevant considerations, must have started functioning at any time after March 31, 1997, and before April 1, 2001;

(d) If located in a place other than a place referred to above in (c), and not being located at a place within the municipal jurisdiction of Calcutta, Chennai, Delhi or Mumbai, must have started functioning at any time after March 31, 1997, and before April 1, 2001; and

(e) Must for the time being be approved by the prescribed authority.

(iv) A company engaged in scientific R&D:

(a) Must be registered in India;

(b) Must have as its object the carrying on of scientific and industrial R&D;

(c) Must have been approved by the prescribed authority at any time after March 31, 2000, but before April 1, 2007; and

(d) Must fulfill such other conditions as may be prescribed.

(v) An enterprise:

(a) Located in the North-Eastern Region must have commenced the commercial production of mineral oil before April 1, 1997;

(b) Located in any other part of India must have commenced commercial production of mineral oil after March 31, 1997;

(c) That is an undertaking other than an undertaking referred to above in (a) or (b), must have commenced the refining of mineral oil in any part of India after September 30, 1998 but not later than March 31, 2012;

(d) Engaged in the commercial production of natural gas in blocks licensed under the New Exploration Licensing Policy (NELP) announced by the government of India on February 10, 1999, must begin commercial production of natural gas on or after April 1, 2009;

(e) Engaged in the commercial production of natural gas in blocks licensed under Round IV of the bidding for award of exploration contracts for Coal Bed Methane blocks must begin commercial production after March 31, 2009.

Note: **In respect of the above, all blocks licensed under a single contract that have been awarded under the NELP announced by the government of India on February 10, 1999, or have been awarded in pursuance of any law for the time being in force or by the central or state government or in any other manner, will be treated as a single undertaking/enterprise.**

(vi) In the case of an undertaking engaged in developing and building housing projects approved by the local authority before March 31, 2008:

(a) If the undertaking has commenced development and construction of the project after October 1, 1998:

• The construction must have been completed before March 31, 2008, if the local authority approved the project before April 1, 2004;

• Where the local authority approves the project after March 31, 2004, but before April 1, 2005, the construction must be completed within a period of four years from the end of the financial year in which the project is so approved by the local authority;

• Otherwise, the construction must be completed within a period of five years from the end of the financial year in which the project is approved by the local authority.

(b) Subject to certain exceptions, the undertaking must ensure that the project is on a plot of land with a minimum size of one acre and:

• That a residential unit has a maximum built up area of 1,000 square feet where the residential unit is situated in the city of Delhi or Mumbai or within 25 kilometers from the municipal limits of either of these cities, and of 1,500 square feet in any other place;

• That the built-up area of the shops and other commercial establishments included in the housing project does not exceed 3% of the aggregate built-up area of the housing project or 5,000 square feet,

whichever is greater; and

• That no person other than an individual is allotted more than one residential unit in the housing project.

If a residential unit in the housing project is allotted to an individual, no other residential unit may be allotted to the following persons: the spouse or the minor children of the individual; a HUF of which the individual is the *karta* (manager); or any person representing the individual, the spouse or minor children of the individual, or a HUF of which the individual is the *karta*.

(vii) An undertaking engaged in the business of processing, preserving and packaging meat products or poultry, or marine or dairy products, must have begun business operations before April 1, 2009.

(viii) In the case of a multiplex theater:

(a) The theater must have been constructed at any time during the period beginning on April 1, 2002, and ending on March 31, 2005;

(b) The business of the multiplex theater must not have been formed by the splitting up or reconstruction of a business already in existence or by the transfer to a new business of any building, or machinery or plant previously used for any purpose; and

(c) The taxpayer carrying on the business of the multiplex theater must furnish, along with his return of income, a report of an audit in prescribed form duly signed and verified by an accountant.

For purposes of the above, "multiplex theater" means a building of a prescribed area, comprised of two or more cinema theaters and commercial shops of such size and number and having such other facilities and amenities as may be prescribed.

(ix) In the case of a convention center:

(a) The center must have been constructed at any time during the period beginning on April 1, 2002, and ending on March 31, 2005;

(b) The business of the convention center must not have been formed by the splitting up or reconstruction of a business already in existence or by the transfer to a new business of any building, or any machinery or plant previously used for any purpose; and

(c) The taxpayer carrying on the business of the convention center must furnish along with his return of income, a report of an audit in prescribed form duly signed and verified by an accountant.

For purposes of the above, "convention center" means a building of a prescribed area, comprised of convention halls to be used for purposes of holding conferences and seminars, being of such size and number and having such other facilities and amenities, as may be prescribed.

(x) In the case of a hospital in a rural area:

(a) The hospital must have been constructed at any time during the period beginning on October 1, 2004 and ending on March 31, 2008;

(b) The hospital must have at least 100 beds for patients;

(c) The construction of the hospital must comply with the extant regulations of the local authority; and

(d) The taxpayer must furnish, along with his return of income, a report of an audit in prescribed form duly signed and verified by an accountant.

(xi) In the case of a hospital located anywhere in India other than in a specified excluded area:

(a) The hospital must be constructed at any time during the period beginning on April 1, 2008 and ending on March 31, 2013;

(b) The hospital must have at least 100 beds for patients;

(c) The construction of the hospital must comply with the extant regulations of the local authority; and

(d) The taxpayer must furnish, along with his return of income, a report of an audit in prescribed form duly signed and verified by an accountant. [409]

[409] ITA, Sec. 80IB.

(3) Certain Undertakings or Enterprises in Special Category States

Industrial undertakings and enterprises engaged in the manufacture or production of specified articles or things and located in specified areas are entitled to a deduction from profits, as specified below.

To be eligible, an undertaking/enterprise must:

(i) Have begun or begin to manufacture or produce any article or thing, not being any article or thing specified in the Thirteenth Schedule to the ITA (see the Worksheets);

(ii) Have undertaken substantial expansion, in the case of a unit referred to above in (i); or

(iii) Have begun or begin to manufacture or produce or undertake substantial expansion in any EPZ, Integrated Infrastructure Development Centre, Industrial Growth Centre, Industrial Estate, Industrial Park, STP, Industrial Area, or Theme Park, as notified by the CBDT in accordance with the scheme drawn up and notified by the central government in this regard in the state of Himachal Pradesh or the state of Uttaranchal, during the period from January 7, 2003 to March 31, 2012.

To be eligible, the undertaking/enterprise must:

(i) Have begun or begin to manufacture or produce any article or thing specified in the Fourteenth Schedule to the ITA (see the Worksheets) or commence any operation specified in that Schedule; or

(ii) Have undertaken substantial expansion, in the case of a unit referred to above in (i) during the period:

- **From December 23, 2002, to March 31, 2012, in the State of Sikkim;**
- **From January 7, 2003, to March 31, 2012, in the State of Himachal Pradesh or the State of Uttaranchal; or**
- **From December 24, 1997, to March 31, 2007, in any of the North-Eastern states.**

The deduction available is as follows:

(i) In the case of an undertaking or enterprise in the state of Sikkim or any of the North-Eastern States, 100% of profits and gains for 10 assessment years commencing with the initial assessment year; and

(ii) In the case of an undertaking or enterprise in the state of Himachal Pradesh or Uttaranchal, 100% of profits and gains for five assessment years commencing with the initial assessment year and, thereafter, 25% (or 30% where the taxpayer is a company) of profits and gains.

For purposes of the above:

(i) "Industrial Area," "Industrial Estate," "Industrial Growth Centre," "Industrial Park," "Integrated Infrastructure Development Centre" and "Theme Park" mean such areas, estates, centers and parks as the CBDT may, by notification in the Official Gazette, specify in accordance with the scheme drawn up and notified by the central government;

(ii) "Initial assessment year" means the assessment year relevant to the previous year in which the undertaking or enterprise begins to manufacture or produce articles or things, or commences operations or completes substantial expansion;

(iii) "North-Eastern States" means the states of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura;

(iv) "Software Technology Park" means any park set up in accordance with the Software Technology Park Scheme notified by the Government of India in the Ministry of Commerce and Industry; and

(v) "Substantial expansion" means an increase in investment in plant and machinery of at least 50% of the book value of plant and machinery (before taking depreciation in any year) as of the first day of the tax year in which the substantial expansion is undertaken.

The following conditions must be fulfilled by the undertaking or enterprise for the deduction to be available:

(i) It must not have been formed by the splitting up or reconstruction of a business already in existence. This condition does not apply when an undertaking is split or reconstructed as a result of specified natural calamities, accident, fire, explosion, or action by an enemy; and

(ii) It must not have been formed by the transfer to a new business of machinery or plant previously used for any purpose.

No deduction is allowed to the taxpayer with respect to such profits and gains under any other provisions of the ITA. [410]

---

[410] ITA, Sec. 80IC.

---

(4) Industrial Undertaking or Enterprise Engaged in the Development of a Special Economic Zone

Industrial undertakings and enterprises engaged in the business of developing SEZs are entitled to a deduction of 100% of profits derived from such business for 10 consecutive tax years. Such deduction may, at the option of the taxpayer, be claimed for any 10 consecutive tax years out of 15 years beginning from the year in which the SEZ is notified by the central government: where an undertaking or enterprise that develops an SEZ on or after April 1, 2005, transfers the operation and maintenance of the SEZ to another developer, the deduction will be allowed to the transferee developer for the remaining period in the 10 consecutive tax years as if the operation and maintenance had not been so transferred to the transferee developer. [411]

---

[411] ITA, Sec. 80IAB.

---

(5) Industrial Undertakings Engaged in the Business of Hotels and Convention Centers in Specified Areas

Industrial undertakings engaged in the business of hotels or convention centers in specified areas or hotels in specified districts with World Heritage Sites are entitled to a deduction of an amount equal to 100% of the profits and gains derived from such business for five consecutive assessment years beginning from the tax year in which the hotel concerned starts functioning or the convention center commences commercial operations. To be entitled to the deduction:

(i) An undertaking engaged in a hotel business located in a specified area must have constructed the hotel and must have started functioning at any time during the period beginning on April 1, 2007 and ending on July 31, 2010;

(ii) An undertaking engaged in the business of building, owning and operating a convention center located in a specified area must have constructed the convention centre during the period beginning on the April 1, 2007 and ending on the July 31, 2010; and

(iii) An undertaking engaged in a hotel business located in a specified district having a World Heritage Site must have constructed the hotel and must have started or must start functioning at any time during the period beginning on April 1, 2008, and ending on March 31, 2013.

An undertaking must fulfill additional specified conditions to claim the deduction.

The deduction is not allowed unless the income tax return of the taxpayer is accompanied by an audit report made by an accountant stating that the deduction is correctly claimed.

No deduction is allowed to the taxpayer with respect to such profits and gains under any other provisions of the ITA. [412]

---

[412] ITA, Sec. 80ID.

---

(6) Undertakings Engaged in Business in the North Eastern States

Industrial undertakings engaged in specified businesses in any of the North Eastern states are entitled to a deduction of 100% of the profits and gains derived from such business for 10 consecutive tax years commencing from the initial assessment year.

To be entitled to the deduction, an undertaking must have begun or must begin, during the period beginning on April 1, 2007 and ending before April 1, 2017, in any of the North-Eastern States:

(i) To manufacture or produce any eligible article or thing;

(ii) To undertake substantial expansion to manufacture or produce any eligible article or thing; or

(iii) To carry on any eligible business.

An undertaking must fulfill additional specified conditions to claim the deduction.

No deduction is allowed to the taxpayer with respect to such profits and gains under any other provisions of the ITA. [413]

[413] **ITA, Sec. 80IE.**

g. Concessions for Investor Protection Funds

Income derived by Investor Protection Funds set up by recognized stock exchanges in India, whether jointly or separately, is exempt from tax to such extent as the central government may, by notification in the official gazette, specify for this purpose. [414]

[414] **ITA, Sec. 10(23EA).**

h. Concessions for Venture Capital Funds/ Undertakings

Income derived by a venture capital company or a venture capital fund set up to raise funds for investment in a venture capital undertaking is exempt from tax. However, income from dividends (other than exempt dividends), interest and long-term capital gains of an infrastructure capital company will be taken into account in computing book profit for the purpose of minimum alternate tax liability.

For purposes of qualifying for the exemption:

(i) "Venture capital company" means a company that:

- **Has been granted a certificate of registration under the Securities Exchange Board of India Act, 1992, and regulations adopted thereunder; and**
- **Fulfils such conditions as may be specified, with the approval of the central government, by the SEBI, by notification in the official gazette, for this purpose.**

(ii) "Venture capital fund" means a fund:

- **Operating under a trust deed registered under the provisions of the Registration Act, 1908;**
- **That has been granted a certificate of registration under the Securities Exchange Board of India Act, 1992, and regulations adopted thereunder; and**
- **That fulfils such conditions as may be specified, with the approval of the central government, by the SEBI, by notification in the official gazette, for this purpose.**

(iii) "Venture capital undertaking" means a domestic company:

- **Whose shares are not listed on a recognized stock exchange in India; and**
- **That is engaged in the business of: nanotechnology; information technology relating to hardware and software development; seed R&D; biotechnology; R&D of new chemical entities in the pharmaceutical sectors; the production of bio-fuels; building and operating a composite hotel-cum-convention center with a seating capacity of more than 3,000; developing, operating and maintaining any infrastructure facility as defined in Section 80IA of the ITA; or the dairy or poultry industry.** [415]

[415] **ITA, Sec. 10(23FB).**

i. Concession with Respect to Profits from Collecting and Processing Biodegradable Waste

A taxpayer is entitled to a deduction from the profits derived from the business of collecting and processing, or treating biodegradable waste for generating power, producing bio-fertilizers, bio-pesticides or other biological agents or bio-gas, or making pellets or briquettes for fuel or organic manure, to the extent of the whole of such profits for a period of five consecutive years beginning with the tax year in which the business commences. [416]

[416] ITA, Sec. 80JJA.

j. Concessions for the Employment of New Workmen

An Indian company is entitled to a deduction from profits or gains derived from an industrial undertaking engaged in the manufacture or production of any article or thing, of an amount equal to 30% of the additional wages paid to new regular workmen employed during the tax year for three tax years including the tax year in which the employment is provided, subject to the following conditions:

(i) The industrial undertaking may not be formed by the splitting up or reconstruction of an existing undertaking or amalgamation with another industrial undertaking; and

(ii) The taxpayer must furnish, along with his return of income, a report made by an accountant in the prescribed form.

"Additional wages" means the wages paid to new workmen in excess of 100 workmen employed during the tax year. However, in the case of an existing undertaking, "additional wages" are zero if the increase in the number of regular workmen employed during the year is less than 10% of the existing number of workmen employed in the undertaking on the last day of the preceding year.

"Regular workmen" does not include casual workmen, workmen employed by way of contract labor or any other workmen employed for a period of less than 300 days during the tax year. [417]

[417] ITA, Sec. 80JJAA.

k. Special Privileges for Business Reorganizations

No capital gain chargeable to tax under the ITA arises:

(i) In the case of any transfer, in a demerger, of a capital asset by the demerged company to the resulting Indian company; [418]

(ii) In the case of any transfer, in a demerger, of a capital asset, being a share or shares held in an Indian company, by a demerged foreign company to the resulting foreign company, if:

- At least 75% of the shareholders of the demerged foreign company remain shareholders of the resulting foreign company; and
- The transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated. [419]

(iii) In the case of any transfer or issue of shares by the resulting company in a scheme of demerger to the shareholders of the demerged company, if the transfer or issue is made in consideration of the demerger of an undertaking; [420]

(iv) If a firm is succeeded by a company in the business carried on by it and, as a result, the firm sells or otherwise transfers any capital asset or intangible asset to the company, subject to the following conditions:

- All the assets and liabilities of the firm relating to the business immediately before the succession must become assets and liabilities of the company;
- All the partners of the firm immediately before the succession must become shareholders of the company in proportion to the amounts standing to the credit of their capital accounts in the books of the firm on the date of succession;
- The partners of the firm may not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company; and
- The aggregate shareholding in the company of the partners of the firm may not be less than 50% of the total voting power in the company and their shareholding must continue to be such for a period of five years from the date of succession. [421]

(v) In the case of the conversion of a private or unlisted public company into a limited liability partnership, where the company sells or otherwise transfers any capital asset or intangible asset, or a shareholder sells or transfers shares of the company, subject to the following conditions:

- All the assets and liabilities of the company immediately before the conversion become the assets and

liabilities of the limited liability partnership;

• All the shareholders of the company immediately before the conversion become the partners of the limited liability partnership and their capital contribution and profit-sharing ratio in the limited liability partnership are in the same proportion as their shareholding in the company on the date of conversion;

• The shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of a share in the profit and a capital contribution in the limited liability partnership;

• The aggregate of the profit sharing ratio of the shareholders of the company in the limited liability partnership is not less than 50% at any time during the period of five years from the date of conversion;

• The total sales, turnover or gross receipts in the business of the company in any of the three tax years preceding the tax year in which the conversion takes place do not exceed Rs. 6 million; and

• No amount is paid, either directly or indirectly, to any partner out of the balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion. [422]

(vi) If a sole proprietary concern is succeeded by a company in the business carried on by it and, as a result, the sole proprietary concern sells or otherwise transfers any capital asset or intangible asset to the company, subject to the following conditions:

• All the assets and liabilities of the sole proprietary concern relating to the business immediately before the succession must become assets and liabilities of the company;

• The shareholding of the sole proprietor in the company may not be less than 50% of the total voting power in the company and his or her shareholding must continue to remain such for a period of five years from the date of succession; and

• The sole proprietor may not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company. [423]

---

[418] ITA, Sec. 47(vi)(b).

[419] ITA, Sec. 47(vi)(c).

[420] ITA, Sec. 47(vi)(d).

[421] ITA, Sec. 47(xiii).

[422] ITA, Sec. 47(xiiib).

[423] ITA, Sec. 47(xiv).

However, where any of the conditions laid down above in (iv), (v) and (vi) are not fulfilled, the benefit of which the firm or the sole proprietor has availed itself or himself is deemed to be profits and gains chargeable to tax in the tax year in which the conditions were not fulfilled. [424]

---

[424] ITA, Sec. 47A(3).

Any accumulated loss or unabsorbed depreciation of the predecessor firm or proprietary concern is deemed to be a loss or allowance for depreciation of the successor company for the year in which the reorganization was effected, and the other provisions of the ITA relating to the set-off and carryforward of losses and depreciation (see 6, above) apply accordingly.

l. Stock Lending Schemes

No capital gains arise on any transfer in a scheme for the lending of any securities under an agreement or arrangement that the taxpayer has entered into with the borrower of the securities and that is subject to the guidelines issued by the SEBI in this regard. [425]

---

[425] ITA, Sec. 47(xv).

---

m. Concession for Certain Income of Offshore Banking Units and International Financial Services

In the case of any scheduled bank or any bank incorporated under the laws of a country outside India and having an Offshore Banking Unit (OBU) in a SEZ or a unit of an International Financial Services Centre that includes any income

from its OBU or from business specified in the Banking Regulation Act with an undertaking located in a SEZ or any other undertaking that develops, operates and maintains a SEZ, or from any unit in an International Financial Services Centre, subject to compliance with prescribed conditions:

(i) 100% of such income is allowed as deduction for five consecutive assessment years beginning with the year in which permission from the appropriate authority is obtained; and

(ii) 50% of such income is allowed as deduction during the next five consecutive assessment years. [426]

---

[426] **ITA, Sec. 80LA.**

---

n. Special Provisions Relating to Tax on Income Received from Venture Capital Companies and Venture Capital Funds

Any income received by a person out of investments made in a venture capital company or venture capital fund will be chargeable to tax in the same manner as if it were the income that would have been received by the person had he made investments directly in the venture capital undertaking.

The person responsible for making payment of the income on behalf of the venture capital company or venture capital fund and the venture capital company or venture capital fund must furnish, within such time as may be prescribed, to the person receiving the income and to the prescribed income tax authority, a statement in the prescribed form and verified in the prescribed manner, giving details of the nature of the income paid during the tax year and such other relevant details as may be prescribed.

The income paid by the venture capital company or venture capital fund will be deemed to be of the same nature and in the same proportion in the hands of the person receiving the income, as if it had been received by, or had accrued to, the venture capital company or the venture capital fund during the tax year.

If these specified provisions apply, other provisions of the ITA will not apply to income paid by a venture capital company or venture capital fund.

For this purpose, venture capital company, venture capital fund and venture capital undertaking will have the meanings respectively assigned to them in Section 10 (23FB) of the ITA. [427]

---

[427] **ITA, Sec. 115U.**

---

10. Advance Tax and Tax Deducted at Source

a. Advance Tax

All taxpayers (whether individuals or legal entities) whose tax payable for any year amounts to Rs.10,000 or more are required to pay such tax in advance in installments. [428] **A taxpayer who is liable to pay advance tax is required to estimate his current income from all sources including capital gains and to pay advance tax thereon.**

---

[428] **ITA, Sec. 208.**

In the case of companies, advance tax is payable in four installments, as follows:

(i) At least 15% of the advance tax payable must be paid by June 15;

(ii) At least 45% of the advance tax payable must be paid by September 15;

(iii) At least 75% of the advance tax payable must be paid by December 15; and

(iv) At least 100% of the advance tax payable must be paid by March 15.

Advance tax in the case of other taxpayers is payable in three installments, as follows:

(i) At least 30% of the advance tax payable must be paid by September 15;

(ii) At least 60% of the advance tax payable must be paid by December 15; and

(iii) At least 100% of the advance tax payable must be paid by March 15. [429]

---

[429] **ITA, Sec. 211.**

Interest is payable by a taxpayer if:

(i) The tax paid in installments as described above is less than 90% of the final tax payable; [430] and

(ii) An installment of advance tax payable as described above and computed based on the tax due as per the return of income (as reduced by taxes deducted at source) is less than the installment of advance tax actually paid as described above. [431]

---

[430] ITA, Sec. 234B.

[431] ITA, Sec. 234C.

Tax is required to be computed on current income (estimated by the taxpayer) at the rates in force during the financial year. From the tax so computed, tax deducted at source must be deducted to arrive at the advance tax payable. [432]

---

[432] ITA, Sec. 209.

Every person who is liable to pay advance tax (whether or not he has previously been assessed by way of regular assessment) will, of his own accord, pay installments of advance tax as above.

The installments of advance tax may be recomputed in the case of a revision in the estimate of the current income of the taxpayer and payments of the recomputed amount should be paid in the remaining installment or installments accordingly. [433]

---

[433] ITA, Sec. 210.

---

b. Tax Deducted at Source

Every person making certain specified payments (including payments of salary and interest) is required to deduct tax at source at prescribed rates.

Individuals and HUFs are required to deduct tax at source on certain payments only if total sales, gross receipts or turnover from the business or profession carried on by them exceed the monetary limits specified IN Section 44AB(a)/(b) of the ITA during the immediately preceding financial year. [434]

---

[434] ITA, Secs. 192–195.

---

(1) Foreign Companies

Tax is deducted at the following rates for the assessment year 2011-12:

Source of Income	% of total taxable income
Royalties and fees for technical services effectively connected with a PE or fixed base and referred to in VI, C, 7, below	40% of net income
Royalties and fees for technical services	10%
Interest	20%
Long-term capital gains other than gains on listed securities	20%
Short-term capital gains on listed securities	15%
Any other income	40%

The above rates are increased by a surcharge of 2.5% of the income tax payable if the taxable income exceeds Rs.10 million.

An education tax (cess) of 3% is charged on the aggregate tax including the surcharge.

(2) Nonresident Individuals

In the case of nonresident taxpayers other than companies, tax is deducted at the following rates for the assessment year 2010-11:

Source of Income	% of total taxable income
Long-term capital gains other than gains on listed securities	20%
Short-term capital gains on listed securities	15%

Dividends (other than dividends referred to at 8, above)	30%
Interest	20%
Royalties and fees for technical services	10%
Any other Income	30%

(3) Residents

Tax is required to be deducted at source as indicated in (a) to (o), below.

(a) Salaries

Tax is deducted at source in equal monthly installments based on estimated taxable salary at the rates of tax for individuals given in 7, a, above. [435]

[435] ITA, Sec. 192.

(b) Interest on Securities

Tax is deducted at source at the following rates, either at the time of credit to the account of a resident payee or to any other account by whatever name called, or at the time of payment, whichever is earlier, from interest on securities: [436]

[436] ITA, Sec. 193.

Particulars	Income tax assessment year 2011–12
Interest paid to companies	10%
Interest paid to other persons	10%

Tax is not required to be deducted at source in (among other cases) the case of:

(i) Interest payable on National Defense bonds, National Savings certificates and other specified central/state government securities;

(ii) Interest payable on debentures of public quoted companies, where the interest is paid by an account payee check and the aggregate amount of the interest during the taxable year does not exceed Rs.2,500;

(iii) Interest payable to the Life Insurance Corporation of India with respect to any securities owned by it or in which it has a full beneficial interest;

(iv) Interest payable to the General Insurance Corporation of India, the United India Insurance Company Limited, the Oriental Insurance Company Limited, the New India Assurance Company Limited, and the National Insurance Company Limited with respect to any securities owned by these companies or companies in which these companies have a full beneficial interest;

(v) Interest payable to any other insurer with respect to any securities owned by it or in which it has full beneficial interest;

(vi) Interest payable on any security issued by a company where the security is in dematerialized form and is listed on a recognized stock exchange in India in accordance with the Securities Contracts (Regulation) Act, 1956, and the rules adopted thereunder; and

(vii) Interest payable to a resident individual who furnishes a declaration in writing in the prescribed form that his or her total income does not exceed the exemption limit.

(c) Other Interest

Tax is deducted at source at the following rates, either at the time of credit to the account of a resident payee or any other account by whatever name called, or at the time of payment, whichever is earlier, from payment of any other interest: [437]

[437] ITA, Sec. 194A.

Particulars	Income tax assessment year 2011-12
Interest paid to companies	10%
Interest paid to other persons	10%

Tax is not required to be deducted at source from (among other things):

(i) Interest credited or paid by the central government under various provisions of the ITA;

(ii) The aggregate amount of interest on time deposits during the year with individual branches of a banking company or a cooperative society engaged in the business of banking, or a public company registered in India that has as its main object the object of providing long-term finance for the construction or purchase of residential dwellings, provided the interest does not exceed Rs.10,000 (Rs.5,000 in the case of a public company, as referred to above);

(iii) The aggregate amount of other interest during the year, provided it does not exceed Rs.5,000;

(iv) Interest paid by a firm to a partner of the firm;

(v) Interest on deposits with the post office or under any notified scheme drawn up by the central government;

(vi) Interest paid by a cooperative society to a member or to any other cooperative society;

(vii) Interest paid on the compensation amount awarded by the Motor Accidents Claims Tribunal, where the aggregate amount of such income exceeds Rs.50,000;

(viii) Interest paid by an infrastructure capital company or infrastructure capital fund, or a public sector company, or a scheduled bank in relation to a zero coupon bond issued after May 31, 2005; and

(ix) Interest payable to a resident individual who furnishes a declaration in writing in the prescribed form that his or her estimated total income does not exceed the exemption limit.

(d) Payments to Contractors and Subcontractors

Tax is deducted at source from payments under a contract (including a sub-contract) for carrying out any work, including the supply of labor for carrying out any work, at the rate of:

(i) 1% where payment is being made or credit is being given to an individual or a HUF;

(ii) 2% where payment is being made or credit is being given to a person other than an individual or a HUF.

These provisions apply to all types of contracts for carrying out any work, including advertising contracts, broadcasting contracts, telecasting contracts, contracts for the carriage of goods and passengers by any mode of transport other than railway, catering contracts, manufacturing or supplying a product according to the requirement or specification of a customer by using material purchased only from that customer.

Where any sum is paid or credited for carrying out any work, tax will be deducted at source on the invoice value excluding the value of material, only if such value is mentioned separately in the invoice, otherwise tax will be deducted on the entire invoice amount.

No deduction will be made from any sum credited or paid or likely to be credited or paid during the previous year to the account of a contractor during the course of a business of plying, hiring or leasing goods carriages, on his furnishing his Permanent Account Number (PAN) to the person paying or crediting the sum, subject to compliance with certain conditions.

Tax is not required to be deducted at source where the consideration for the contract or the sub-contract does not exceed Rs.30,000. However, if the aggregate amount credited or paid to the contractor or sub-contractor is likely to exceed Rs.75,000, tax is required to be deducted at source either at the time of credit to the account of the payee or to any other account by whatever name called, or at the time of payment, whichever is earlier. [438]

---

[438] ITA, Sec. 194C.

(e) Rent

Tax is deducted at source at the following rates either at the time of credit to the account of the payee or any other account by whatever name called, or at the time of payment, whichever is earlier: [439]

---

[439] ITA, Sec. 194I.

Particulars	Income tax assessment year 2011-12
For the use of machinery, plant or equipment	2%
For the use of any land or building (including a factory building) or land appurtenant to a building (including a factory building) ,or furniture or fittings	10%

Tax is not required to be deducted if the rent paid or credited during the taxable year does not exceed Rs.180,000.

"Rent" means any payment, by whatever name called, under any lease, sub-lease, tenancy or other agreement or arrangement for the use of (either separately or together): land; a building (including a factory building); land appurtenant to a building (including a factory building); machinery; plant; equipment; furniture; or fittings, regardless of whether any or all of the above are owned by the payee.

(f) Fees Paid for Professional and Technical Services

Tax is required to be deducted at source at the rate of 10% of an amount paid as professional or technical fees either at the time of credit to the account of the payee or any other account by whatever name called, or at the time of payment, whichever is earlier, if the aggregate amount of such fees exceeds Rs.30,000 in a taxable year. [440]

[440] ITA, Sec. 194J.

(g) Commission or Brokerage Fees

Tax is deducted at source at the rate of 10% at the time of credit to the account of the resident payee or any other account by whatever name called, or at the time of payment, whichever is earlier, from commission or brokerage fees if the aggregate amount of such fees exceeds Rs.5,000 in a taxable year.

No tax is required to be deducted from commission or brokerage fees paid for services in the course of buying or selling securities, or in relation to any transaction in securities. [441]

[441] ITA, Sec. 194H.

(h) Income from Dividends

Tax is deducted at source at the following rates from income from dividends (other than dividends referred to at 8, above) if the aggregate of the amounts paid or credited to the account of a resident payee, exceeds Rs.2,500 in a taxable year: [442]

[442] ITA, Sec. 194.

Particulars	Income tax assessment year 2011-12
Income paid to companies	10%
Income paid to other persons	10%

(i) Winnings from Lotteries, Crossword Puzzles, Card Games and Other Games

Tax is deducted at source at the rate of 30% from income from winnings from lotteries, crossword puzzles, card games and other games, if the aggregate of the amounts paid or credited exceeds Rs.10,000 in a taxable year. [443]

[443] ITA, Sec. 194B.

(j) Insurance Commissions

Tax is deducted at source at the rate of 10% from income from insurance commissions (from soliciting or procuring insurance business) if the aggregate of the amounts paid or credited to the account of a resident payee exceeds Rs.20,000 in a taxable year. [444]

[444] ITA, Sec. 194D.

(k) Winnings from Horse Races

Any person, being a bookmaker or a person to whom a license has been granted by the government under any law for horse racing on any race course or for arranging for wagering or betting on any race course, who is responsible for paying to any person any income by way of winnings from any horse race in an amount exceeding Rs.5,000 will, at the time of payment, deduct tax at the rate of 30%. [445]

[445] ITA, Sec. 194BB.

(l) Payments with Respect to Deposits Under the National Saving Scheme or a Deferred Annuity Plan

Tax is required to be deducted at source at the rate of 20% from income referred from a scheme or a deferred annuity plan of the Life Insurance Corporation of India, notified by the government, if the aggregate of the amount paid

exceeds Rs.2,500 in a tax year. No tax is to be deducted if the payment is made to the heirs of the taxpayer. [446]

[446] ITA, Sec. 194EE.

(m) Payments on Account of the Repurchase of Units by a Mutual Fund or the Unit Trust of India

Tax is required to be deducted at source at the rate of 20% from income paid on the repurchase of units of an Equity Linked Saving Scheme under any plan formulated by the central government and duly notified. [447]

[447] ITA, Sec. 194F.

(n) Commission on the Sale of Lottery Tickets

Where any income is payable by way of commission, remuneration or prize (by whatever name called) to any person who is or has been stocking, distributing, purchasing or selling lottery tickets, the person responsible for making the payment must deduct income tax at the rate of 10% at the time of credit to the account of the payee or any other account, by whatever name called, or at the time of payment, whichever is earlier. [448]

[448] ITA, Sec. 194G.

(o) Payment of Compensation on the Acquisition of Certain Real Property

Any person responsible for paying to a resident any sum being in the nature of compensation or enhanced compensation, or consideration or enhanced consideration, on account of the compulsory acquisition of any real property (other than agricultural land) is required to deduct tax at the rate of 10% if the aggregate of the amount paid or credited exceeds Rs.100,000, at the time of credit to the account of the payee or any other account, by whatever name called, or at the time of payment, whichever is earlier. [449]

[449] ITA, Sec. 194LA.

(p) Requirement to Furnish a Permanent Account Number

Any person entitled to receive any sum or income or amount from which tax is deductible at source must furnish his PAN to the person responsible for deducting the tax, failing which tax will be deducted at the highest of the following rates:

(i) The rate specified in the relevant provision of this Act;

(ii) The rate or rates in force; or

(iii) The rate of 20%. [450]

[450] ITA, Sec. 206AA.

(q) Deduction of Tax at a Lower Rate

Unless otherwise stated, where in the case of any income of any person or any sum payable to any person, income tax is required to be deducted at the time of credit or at the time of payment at the rates set out above, the Assessing Officer is satisfied that the total income of the recipient justifies the deduction of income tax at any lower rates or no deduction of income tax, the Assessing Officer will, on an application made by the taxpayer in this behalf, give to him such certificate as may be appropriate. [451]

[451] ITA, Sec. 197.

(4) Offshore Funds, Income from Notified Bonds/Shares and Foreign Institutional Investors

Tax is deducted at the rate of 10% from income from, or long-term capital gains from the transfer of, units purchased in foreign currency by an offshore fund. [452]

[452] ITA, Sec. 196B.

Tax is deducted at source at the rate of 10% from income payable to nonresidents by way of interest or dividends

(other than dividends referred to at 8, above) or long-term capital gains from the transfer of bonds or GDRs issued in accordance with a scheme notified in the Official Gazette by the central government. [453]

[453] ITA, Sec. 196C.

Tax is deducted at the rate of 20% from the income of foreign institutional investors by way of interest or dividends (other than those referred to in 8, above) from securities. No tax is deducted from income by way of capital gains arising to foreign institutional investors from the transfer of securities. [454]

[454] ITA, Sec. 196D.

(5) Nonresident Sportsmen or Sports Associations

Where the total income of a nonresident sportsman (including an athlete) who is not a citizen of India includes any income received or receivable by way of participation in India in any game or sport, or advertisement, or by virtue of the contribution of articles relating to any game or sport in India in newspapers, etc., or the total income of a nonresident sports association or institution includes any amount guaranteed to be paid or payable to such association or institution in relation to any game or sport played in India, the income tax payable by the taxpayer will be the aggregate of:

(i) The amount of income tax calculated on the income referred to above at the rate of 10%; and

(ii) The amount of income tax with which the taxpayer would have been chargeable had the total income of the taxpayer been reduced by the amount of income referred to above.

However, no deduction with respect to any expenditure or allowance will be allowed under any provision of ITA in computing such income.

The taxpayer need not furnish a return of income under Section 139(1) of the ITA, if:

(i) His total income during the previous year consisted only of the income referred to above; and

(ii) Tax from such income has been deducted at source under Section 194E of the ITA. [455]

[455] ITA, Sec. 115BBA.

(6) Payment of Tax Deducted at Source

Tax deducted at source must be paid into the Government Treasury within the following time limits:

(i) In the case of payments of salary, within one week from the date of payment;

(ii) In other cases, within one week from the last day of the month in which the deduction is made.

Where the amount is credited as payable on the date on which the accounts of the person crediting the account are drawn up, the tax must be paid to the Treasury within two months of the end of the month in which the amount is credited.

(7) Other Provisions Relating to the Deduction of Tax at Source

All sums deducted in accordance with the above will, for purposes of computing the income of a taxpayer, be deemed to be income received, except for tax deducted at source on nonmonetary perquisites received by an employee from an employer. [456]

[456] ITA, Sec. 198.

Any deduction made in accordance with the above provisions and paid to the central government will be treated as a payment of tax on behalf of the person from whose income the deduction was made. [457]

[457] ITA. Sec. 199.

Where any person who is required to deduct any sum in accordance with the above provisions does not deduct, or does not pay, or after so deducting fails to pay, the whole or any part of the tax, that person will, without prejudice to any other consequences that he may incur, be deemed to be in default with respect to such tax and will be subject to penal provisions, as applicable. For the penalty to apply, the Assessing Officer must be satisfied that the person has

failed to deduct and pay the tax without good and sufficient reason. [458]

[458] ITA, Sec. 201.

(8) Submission of Returns

The various returns and statements with respect to taxes withheld during the year to be submitted quarterly to the income tax authorities and the due dates for submission are as follows:

Section of ITA	Type of payment	Return form number
192	Salary	24Q
193	Interest on securities, such as debentures, etc.	26Q
194	Dividends	26Q
194A	Interest other than interest on securities	26Q
194B	Winning from lotteries or crossword puzzles	26Q
194C	Payments to contractors or subcontractors	26Q
194D	Insurance commission	26Q
194H	Commission and brokerage fees	26Q
194I	Rent	26Q
194J	Fees for professional or technical services	26Q
194K	Income from units	26Q
195	Interest on securities, dividends and other sums paid to a nonresident or a person not ordinarily resident	27Q

Returns must be submitted on or before the 15th of the month following the quarter for the first three quarters, and on or before the 15th of June for the last quarter ending in March.

Returns of tax deducted at source are to be submitted to the Assessing Officer, designated by the Chief Commissioner or the Commissioner of Income Tax, within whose jurisdiction the office of the person responsible for deducting the tax is situated. In all other cases (i.e., where there is no designated Assessing Officer), returns are to be submitted to the Assessing Officer within whose jurisdiction the office of the person responsible for deducting tax is situated.

11. Tax Administration in India

a. Income Tax Authorities

At the apex of the Income Tax Department is the CBDT (the "Board"). The Board is part of the Ministry of Finance and administers the direct taxes, namely income tax and wealth tax.

The following authorities administer the law on a day-to-day basis: [459]

[459] ITA, Sec. 116.

(i) The Director General of Income Tax or Chief Commissioners of Income Tax;

(ii) The Directors of Income Tax, Commissioners of Income Tax or Commissioners of Income Tax (Appeals);

(iii) The Additional Directors of Income Tax, Additional Commissioners of Income Tax or Additional Commissioners of Income Tax (Appeals);

(iv) The Joint Directors of Income Tax or Joint Commissioners of Income Tax;

(v) The Deputy Directors of Income Tax, Deputy Commissioners of Income Tax or Deputy Commissioners of Income Tax (Appeals);

(vi) The Assistant Directors of Income Tax or Assistant Commissioners of Income Tax;

(vii) The Income Tax Officers;

(viii) The Tax Recovery Officers; and

(ix) The Inspectors of Income Tax.

The Board assigns and supervises the functions of these authorities.

b. Administration of the Income Tax Act

The Board may issue binding orders, instructions and directions to other income tax authorities for the proper administration of the ITA. However, the Board may not issue instructions so as to require any income tax authority to make a particular assessment or to dispose of a particular case in a particular manner or interfere with the discretion of the Commissioner (Appeals) in exercise of the appellate functions. [460]

[460] ITA, Sec. 119.

c. Assessment Procedures

Individuals whose total income exceeds the maximum amount not chargeable to tax must, on or before the due date, furnish a return of income for the previous year. Every company is required to furnish a return of income irrespective of the amount of its income. [461]

[461] ITA, Sec. 139(1).

The due dates and prescribed forms for furnishing returns of income (including a return for a loss incurred) are as follows:

Taxpayer	Due date	Form no.
Company	September 30 of the assessment year	ITR 6 (see the Worksheets)
Taxpayers whose accounts are required to be audited and working partners of such entities	September 30 of the assessment year	ITR-3, ITR 4 and ITR-5
Taxpayers whose total income includes income from a business or profession but whose accounts are not required to be audited	July 31 of the assessment year	ITR-3 and ITR-4
Taxpayers whose total income does not include income from a business or profession	July 31 of the assessment year	ITR-1 or ITR-2

A notice requiring the submission of a return by a specified date may be served on a taxpayer that has not filed a return within the prescribed time. [462]

[462] ITA, Sec. 142(1).

A taxpayer that has not furnished a return within the time allowed under Section 139(1) of the ITA or the time allowed under a notice issued under Section 142(1) of the ITA is permitted to furnish a return for any previous year within one year from the end of the relevant assessment year or before the completion of the assessment, whichever is earlier. [463]

[463] ITA, Sec. 139(4).

Where a return is not furnished within the time permitted under Section 139(1) of the ITA, the taxpayer is liable to pay interest at 1.25% per month on the tax payable, as reduced by the advance tax paid and taxes deducted at source. [464]

[464] ITA, Sec. 234A.

A taxpayer that has furnished a return under Section 139(1) or Section 142(1) of the ITA discovers an omission or a wrong statement in that return is permitted to furnish a revised return within one year from the end of the relevant assessment year or before completion of the assessment, whichever is earlier. [465] A taxpayer may not file a revised return unless the original return is furnished under Section 139(1) or as required under Section 142(1).

[465] ITA, Sec. 139(5).

An income tax return must be accompanied by audited accounts, tax deduction certificates, a statement of accounts, and a statement showing a computation of tax payable as stipulated under the Explanation to Section 139(9) of the ITA. If these documents are not filed, the Assessing Officer may treat the return as a defective/invalid return and the provisions of the ITA apply as if the taxpayer had failed to furnish a return. However, where the return of income is not accompanied by a tax deduction certificate, the return of income will not be regarded as defective if:

(i) The person has not received the tax deduction certificate until after the date of filing the return; and

(ii) The certificate is produced within a period of two years from the end of the assessment year in which the income was assessable.

The Assessing Officer may inform a taxpayer of a defect in a return and stipulate a time within which the taxpayer is required to rectify the defect. On such rectification being made before the assessment is completed, the Assessing Officer may treat the return concerned as a valid return. [466]

---

[466] ITA, Sec. 139(9).

The return of income will be signed and verified:

(i) In the case of an individual:

• By the individual himself;

• Where the individual is absent from India, by the individual himself or by some person duly authorized by him in this behalf;

• Where the individual is mentally incapable of attending to his affairs, by his guardian or any other person competent to act on his behalf; and

• Where, for any other reason, it is not possible for the individual to sign the return, by any person duly authorized by him in this behalf.

In a case referred to below in (ii) or (iv), the person signing the return must hold a valid power of attorney from the individual, which must be attached to the return, allowing the person to do so.

(ii) In the case of a company, by the managing director, or where for any unavoidable reason the managing director is unable to sign and verify the return, or where there is no managing director, by any director. Where the company is not resident in India, the return may be signed and verified by a person who holds a valid power of attorney from the company, which must be attached to the return, allowing the person to do so.

(iii) In the case of a firm, by the managing partner, or where for any unavoidable reason the managing partner is unable to sign and verify the return, or where there is no managing partner as such, by any partner, not being a minor; and

(iv) In the case of a limited liability partnership, by the designated partner, or where for any unavoidable reason the designated partner is unable to sign and verify the return, or where there is no designated partner as such, by any partner. [467]

---

[467] ITA, Sec. 140.

A person who has taxable income in any assessment year is required to apply to the relevant Assessing Officer for the allotment of a PAN. A person carrying on a business or profession, the sales, turnover or gross receipts of which are likely to exceed Rs.500,000 in any taxable year, is required to apply to the income tax officer for the allotment of a PAN even if his total income is below the taxable limit. The Assessing Officer may also allot a PAN to any other person by whom tax is payable. Every person receiving any sum or income or amount that is subject to deduction of tax at source is required to indicate his PAN to the person responsible for deducting the tax. [468]

---

[468] ITA, Sec. 139A.

A person is required to quote his PAN in all documents pertaining to the transactions specified below:

(i) The sale or purchase of any real property valued at Rs.500,000 or more;

(ii) The sale or purchase of a motor vehicle, as defined in Clause (28) of Section 2 of the Motor Vehicle Act, 1988, which requires registration by a registering authority under Chapter IV of that Act;

(iii) A time deposit exceeding Rs.50,000 with a banking company to which the Banking Regulation Act, 1949 applies (including any bank or banking institution referred to in Section 51 of that Act);

(iv) A deposit exceeding Rs.50,000 in any account with the Post Office Saving Bank;

(v) A contract with a value exceeding Rs.100,000 for the sale or purchase of securities as defined in Clause (h) of Section 2 of the Securities Contracts (Regulation) Act, 1956;

(vi) The opening of an account with a banking company to which the Banking Regulation Act, 1949 applies (including any bank or banking institution referred to in Section 51 of that Act);

(vii) The making of an application for the installation of a telephone connection (including a cellular telephone connection);

(viii) Payments to hotel and restaurants against their bills of amounts exceeding Rs.25,000 at any one time;

(ix) Payments in cash for demand drafts or pay orders of amounts totaling Rs.50,000 or more in any one day;

(x) Deposits in cash totaling Rs.50,000 or more in any one day;

(xi) Payments of Rs.25,000 or more at any time in cash in connection with travel to any foreign country;

(xii) The making of an application to a bank for the issue of a credit card;

(xiii) Payments of Rs.50,000 or more to a mutual fund for its units;

(xiv) Payments of Rs.50,000 or more to a company for its own shares;

(xv) Payments of Rs.50,000 or more to a company or institution to acquire debentures or bonds issued by it; and

(xvi) Payments of Rs.50,000 or more to the RBI to acquire bonds issued by it.

Any person who has not been allotted a PAN and who enters into any transaction specified above must make a declaration in the prescribed form giving therein the particulars of the transaction. [469]

---

[469] Income-tax Rules, Rule 114B.

The ITA provides for the CBDT to make rules for a class or classes of persons who may not be required to furnish documents, statements, receipts, certificates, audit reports or any other documents that are otherwise required to be furnished along with the return (other than those required to be filed along with a return filed in electronic form), but who may have to produce them at the demand of the Assessing Officer. [470]

---

[470] ITA, Sec. 139C.

The CBDT may also make rules providing for:

(i) A class or classes of persons required to furnish returns in electronic form;

(ii) The form and the manner in which returns in electronic form may be furnished;

(iii) The documents, statements, receipts, certificates and audited reports that need not be furnished along with returns in electronic form but that may have to be produced before the Assessing Officer on demand;

(iv) The computer resources or electronic records to which returns in electronic form may be transmitted. [471]

---

[471] ITA, Sec. 139D.

Where any tax is payable by a taxpayer based on a return furnished under Sections 139, 142, 148, 153A or 158BC of the ITA (after deducting advance tax and tax deducted at source), the tax and interest, if any (known as "self-assessment tax"), is required to be paid before the return is filed; the income tax return is to be accompanied by proof of payment of both tax and interest. [472]

---

[472] ITA, Sec. 140A.

The Assessing Officer may serve notice on any person who has not furnished a return under Section 139(1) of the ITA requiring him to furnish a return within a specified time. Notice may also be served on a person who has furnished a

return under Section 139 of the ITA requiring him to produce accounts and such other information as is required. However, the Assessing Officer may not ask for the production of accounts relating to more than three years before the previous year. [473]

---

[473] ITA, Sec. 142(1).

Where a return has been filed under Section 139 of the ITA or in response to a notice under Section 142(1) of the ITA, the return is processed and the income or loss calculated based on the information provided in the return of income, after making any adjustments on account of arithmetical errors or an incorrect claim apparent from the records. Thereafter, the Assessing Officer grants a refund due based on the return or sends a notice to the taxpayer specifying the amount of tax or interest payable based on the return, after giving credit for the taxes paid and deducted at source from the income of the taxpayer. The notice of interest or tax payable may not be sent to the taxpayer more than one year after the end of the financial year in which the return is made. [474]

---

[474] ITA, Sec. 143(1).

In general, the return furnished by the taxpayer is accepted unless the Assessing Officer serves a notice on the taxpayer requiring him to submit evidence in support of the return to verify its correctness or completeness and the tax paid. This notice may be served on a taxpayer within six months of the end of the tax year in which the return of income is filed. [475]

---

[475] ITA, Sec. 143(2).

After considering the evidence submitted by the taxpayer, the Assessing Officer may make an order in writing assessing the total income or loss of the taxpayer and determine the sum payable by him or the refund due to him based on that assessment. [476]

---

[476] ITA, Sec. 143(3).

The Assessing Officer is vested with broad powers to make a "best judgment" assessment. Such an assessment may be made if a taxpayer fails to file a return or comply with a notice to furnish information under Section 142(1) or 143(2) of the ITA. [477]

---

[477] ITA, Sec. 144.

***Comment:* An officer making an assessment to the best of his judgment must not act vindictively or capriciously or with a view to punishing a taxpayer for noncompliance.**

The Supreme Court has explained the provisions comprehensively. [478] It has been observed by the Court that an officer is to make an assessment to the best of his judgment against a person who is in default in supplying information. The officer must not act dishonestly, vindictively or capriciously because he must exercise judgment in the matter. He must make what he honestly believes to be a fair estimate of the proper figure of assessment and, for this purpose, must take into consideration local knowledge and repute with regard to the taxpayer's circumstances, and his own knowledge of previous returns and assessments of the taxpayer and all other matters that he thinks will assist him in arriving at a fair and proper estimate. Although there must necessarily be guesswork in the matter, it must be honest guesswork.

---

[478] *CIT v. Laxminarain Badridas* (S.C.) 5 I.T.R. 524 [1978].

The Supreme Court has further held [479] that the authority making a best judgment assessment must make an honest and fair estimate of the income of the taxpayer and, though it may not be possible to avoid arbitrariness, the estimate must not be capricious, but should have a reasonable nexus to the available material and the circumstances of the case.

---

[479] *Brij Bhushan Lal Parduman Kumar v. CIT* (S.C.) 115 I.T.R. 524 [1978].

The ITA sets out the following time limits for the completion of assessments and reassessments: [480]

---

[480] ITA, Sec. 153(1).

(i) An order under Section 143 or 144 of the ITA: within 21 months from the end of the assessment year in which the income was first assessable. However, in cases where reference has been made to a Transfer

Pricing Officer (see VIII, below), the time limit stated above will be 33 months;

(ii) An order for reassessment: within nine months from the end of the tax year in which the notice under Section 148 of the ITA (see e, below) was served. However, in cases where reference has been made to a Transfer Pricing Officer (see VIII, below), the time limit stated above will be 21 months.

d. Alternative Dispute Resolution Mechanism

The Assessing Officer has the power to issue a draft order of assessment to an "eligible taxpayer" (see below), in the case of any variation in the return filed that is prejudicial to the interest of the taxpayer.

On receipt of the draft order, the eligible taxpayer must, within 30 days of receipt by him of the draft order: either file his acceptance of the variation with the Assessing Officer; or file his objections, if any, to the variation with the Dispute Resolution Panel and the Assessing Officer.

The Assessing Officer may complete the assessment based on the draft order, if the taxpayer indicates his acceptance or does not file any objection within the period referred above.

The Dispute Resolution Panel will, on receipt of any objection, issue directions after considering the following:

(i) The draft order;

(ii) The objections filed by the taxpayer;

(iii) The evidence furnished by the taxpayer;

(iv) The report, if any, of the Assessing Officer, the Valuation Officer, the Transfer Pricing Officer or any other authority;

(v) Records relating to the draft order;

(vi) Evidence collected, or caused to be collected, by it; and

(vii) The result of any enquiry made, or caused to be made, by it.

Before issuing any direction, the Dispute Resolution Panel may make further enquiry or cause the Assessing Officer authority to make enquiry and report the outcome to it. The Dispute Resolution Panel may confirm, reduce or enhance the variation proposed in the draft order. The Panel will issue no direction unless an opportunity of being heard on the direction is given to the taxpayer or the Assessing Officer, where the direction is prejudicial to the interest of respectively the taxpayer or the revenue.

If the members of the Dispute Resolution Pane differ in opinion on any point, the difference of opinion is resolved in accordance with the opinion of the majority of the members.

Any direction issued by the Dispute Resolution Panel is binding on the Assessing Officer. A direction must be issued within nine months from the end of the month in which the order was issued to the eligible taxpayer.

"Eligible taxpayer" means:

(i) Any person in whose case a variation referred to above arises as a consequence of an order of a Transfer Pricing Officer passed under sub-section (3) of Section 92CA of the ITA; and

(ii) Any foreign company. [481]

---

[481] **ITA, Sec. 144C.**

---

e. Reassessment Procedures

Under Section 147 of the ITA, an Assessing Officer is empowered to assess or reassess a taxpayer's income in cases where he has reason to believe that any taxable income has escaped assessment for any assessment year. Once an assessment has been reopened, any other income that has escaped assessment and that later comes to the notice of the Assessing Officer in the course of the proceeding under Section 147 may also be included in the assessment. Where an assessment has been made under Section 143(3) of the ITA for the relevant assessment year (see c, above), no action will be taken under this section after the expiry of four years from the end of the relevant assessment year, unless any income chargeable to tax has escaped assessment for that assessment year by reason of a failure on the part of the taxpayer to make a return under Section 139 of the ITA or in response to a notice issued under Section 142(1) or Section 148 of the ITA or to disclose fully and truly all material facts necessary for his assessment, for that assessment year.

Under the ITA, the following are deemed to be cases in which income escapes assessment:

(i) Where no income tax return has been furnished by the taxpayer, even though the taxpayer's total income is over the taxable limit;

(ii) Where an income tax return has been furnished by the taxpayer, but no assessment has been made and the taxpayer is found to have understated his income or claimed excessive losses, deductions, etc., in the return; and

(iii) Where an assessment has been made, but income has been underassessed or has been assessed at too low a rate, or excessive loss, relief, depreciation allowance or other allowance under the ITA has been allowed. [482]

---

[482] ITA, Sec. 147.

Before making any assessment, reassessment or recomputation under Section 147 of the ITA, the Assessing Officer is required to serve the taxpayer with a notice requiring him to furnish, within such period as may be specified in the notice, an income tax return. Before issuing the notice, the Assessing Officer is required to record his reasons for doing so. [483]

---

[483] ITA, Sec. 148.

The time limits for issuing a notice under Section 148 of the ITA are as follows:

(i) Four years from the end of the relevant assessment year; or

(ii) If the undeclared or understated income is likely to be Rs.100,000 or more, six years from the end of the relevant assessment year.

If the person on whom a notice for reassessment is to be served is a person treated as the agent of a nonresident and the assessment, reassessment or recomputation to be made in pursuance of the notice is to be made on him as the agent of the nonresident, the notice may not be issued after the expiry of a period of two years from the end of the relevant assessment year. [484]

---

[484] ITA, Sec. 149.

The Assessing Officer is required to make an order for assessment, reassessment or recomputation under Section 147 of ITA within nine months from the end of the financial year in which notice under Section 148 of ITA is served. [485]

---

[485] ITA, Sec. 153(2).

---

f. Rectification of Mistakes

The income tax authorities are empowered to rectify any mistake apparent from the records and to amend any order passed by them. Such mistakes may be rectified by the authorities either on their own initiative or on an application being made by the taxpayer. [486]

---

[486] ITA, Sec. 154.

Where the rectification has the effect of increasing a tax liability or reducing a refund, the Assessing Officer is required to issue to the taxpayer a notice of his intention to rectify the order and to give the taxpayer a reasonable opportunity of being heard.

An order rectifying a mistake is required to be passed within a period of four years from the end of the financial year in which the order sought to be amended was passed.

With respect to an application for rectification made by a taxpayer after June 1, 2001, the Assessing Officer is under an obligation to pass an order within six months from the end of the month in which the application for rectification is received by the income tax authority.

g. Appeals Procedure

A taxpayer may appeal against an order of the Assessing Officer, including a best judgment assessment, within 30 days from: the date of service of the notice or demand relating to the assessment or penalty; or the date on which the announcement of the order sought to be appealed is served. The appeal should be filed before the Commissioner (Appeals) and accompanied by the prescribed fee.

The Commissioner (Appeals) may admit an appeal after the expiry of the specified period, if he is satisfied that the appellant had sufficient cause for not presenting it within that period.

No appeal will be admitted unless, at the time the appeal is filed:

(i) Where a return has been filed, the taxpayer has paid the tax due on the income returned; or

(ii) Where no return has been filed, the taxpayer has paid the advance tax payable by him.

There is a prescribed form and manner of verification for appeals. The Commissioner (Appeals) fixes a place and date for the hearing where the taxpayer has a right to be heard, either in person or through an authorized representative. At the hearing, the Commissioner (Appeals) may allow the appellant to pursue additional grounds of appeal not specified in the grounds of appeal filed, if the Commissioner is of the view that the omission was not willful or unreasonable. [487]

---

[487] ITA, Secs. 249 and 250.

The Commissioner (Appeals) has the power to confirm, reduce, increase or annul the assessment or penalty. He may not, however, increase assessed income or a penalty, or reduce the amount of a refund without giving the taxpayer an opportunity to show cause against such increase or reduction. [488]

---

[488] ITA, Sec. 251.

Note: **The Commissioner (Appeals) may also decide any matter arising out of the proceeding, notwithstanding that the matter was not raised in the appeal by the taxpayer. In other words, the entire case is opened up and the Commissioner (Appeals) may change any matter previously settled with the Assessing Officer.**

The taxpayer and the Assessing Officer have rights of appeal to the Appellate Tribunal against an order of the Commissioner (Appeals). The taxpayer may also appeal to the Appellate Tribunal against a revisional order of the Commissioner (see h, below). The appeal must be made within 60 days of receipt of the order sought to be appealed. The other party (i.e., the Assessing Officer, if the taxpayer has filed the appeal), notwithstanding that he may not have appealed against the order, may file a memorandum of cross objections within 30 days from the receipt of notice that an appeal has been filed with the Appellate Tribunal. Both parties are permitted to present oral arguments before the Appellate Tribunal. The Appellate Tribunal is the final authority on questions of fact. [489]

---

[489] ITA, Sec. 253.

The taxpayer or the Commissioner may, within 120 days of the order of the Appellate Tribunal, appeal against it to the National Tax Tribunal. Such an appeal may be made only on a question of law, not on a question of fact. [490] An appeal to the Supreme Court may be made in any case certified by the National Tax Tribunal to be a fit one for appeal to the Supreme Court. [491] When the National Tax Tribunal refuses to certify a case, the Supreme Court may grant special leave to appeal. [492]

---

[490] ITA, Sec. 256.

[491] ITA, Sec. 261.

[492] ITA, Sec. 257.

Prior to the National Tax Tribunal Act, 2005 (which was published in the Gazette of India on December 31, 2005), cases involving substantial questions of law were heard by the High Court instead of the National Tax Tribunal. All matters pending before the High Court must be transferred to the National Tax Tribunal. This applies with respect to both direct and indirect taxes. It should be noted, however, that although the National Tax Tribunal Act, 2005 received assent from the President on December 28, 2005, a writ petition has been filed before the courts objecting to the formation of a National Tax Tribunal. Until such time as the National Tax Tribunal is functional, appeals will lie to the jurisdictional High Courts.

h. Revisional Powers of Commissioner

The Commissioner of Income Tax is empowered to examine an order passed by an Assessing Officer and if, in his opinion, the order passed is prejudicial to the interests of the revenue, he may pass an order enhancing or modifying the assessment, or canceling the assessment and directing a fresh assessment. The Commissioner is required to give reasonable opportunity to the taxpayer of being heard before passing such a "revisional order." The Commissioner may pass a revisional order within a period of two years from the end of the tax year in which the order sought to be revised was made. [493]

[493] **ITA, Sec. 263.**

A taxpayer may also make an application to the Commissioner of Income Tax for the revision of an order passed by an Assessing Officer. The application must be made within one year from the date of communication of the order sought to be revised or the date on which the taxpayer otherwise came to know of it, whichever is earlier. The Commissioner is also empowered to revise an order *suo moto*. However, in such a case, he must revise the order within one year from the date of the original order. The Commissioner may not revise an order before expiration of the time for appeal to the Deputy Commissioner (Appeals), the Commissioner of Income Tax (Appeals) or the Appellate Tribunal, or if any appeal is pending before the Deputy Commissioner (Appeals), or where the order has been made the subject of an appeal to the Commissioner (Appeals) or to the Appellate Tribunal. [494]

[494] **ITA, Sec. 264.**

Comment: **Generally, when there are two or more orders, some passed by lower authorities such as the Commissioner or the Tribunal, and some passed by higher authorities such as the High Court or the Supreme Court with respect to the same assessment year, there is a fusion or merger of the two or more orders. This principle is called the doctrine of merger. However, the Supreme Court has observed:** [495]

[495] ***State of Madras v. Madurai Mills Co. Ltd.*, AIR 1967 SC 681.**

> **"The doctrine of merger is not a doctrine of rigid and universal application and it cannot be said that wherever there are two orders, one by the inferior tribunal and the other by a superior tribunal, passed in an appeal or revision, there is a fusion or merger of two orders irrespective of the subject matter of the appellate or revisional order and the scope of the appeal or revision contemplated by the particular statute. In our opinion, the application of the doctrine depends on the nature of the appellate or revisional order in each case and the scope of the statutory provisions conferring the appellate or revisional jurisdiction."**

The Bombay High Court has held that the part of an order of the Income Tax Officer that has not been affected by the Appellate Assistant Commissioner's order does not merge with the Appellate Assistant Commissioner's order. That part of the order of the Income Tax Officer remains intact and continues to have an independent existence. [496]

[496] ***CIT v. Sakseria Cotton Mills Ltd. (Bombay)* 124 I.T.R. 570 [1980].**

i. Advance Rulings

An advance ruling means:

(i) A determination by the Authority in relation to a transaction that has been undertaken or is proposed to be undertaken by a nonresident applicant;

(ii) A determination by the Authority in relation to the tax liability of a nonresident arising out of a transaction that has been undertaken or is proposed to be undertaken by a resident applicant with the nonresident; such a determination will include the determination of any question of law or fact specified in the application; or

(iii) A determination or decision by the Authority with respect to an issue relating to the computation of total income that is pending before any income tax authority or the Appellate Tribunal; such a determination or decision will include the determination of, or a decision with respect to, any question of law or fact relating to the computation of total income specified in the application. [497]

[497] **ITA, Sec. 245N.**

An applicant wishing to obtain an advance ruling may make an application to the Authority in the prescribed form (see the Worksheets), along with payment of the prescribed fee, stating the question on which the advance ruling is sought. [498]

[498] **ITA, Sec. 245Q.**

After examining the application and any requested records, the Authority may either accept or reject the application. The Authority will not accept an application where the question raised:

(i) Is already pending in a case of the applicant before any income tax authority, the Appellate Tribunal or any court;

(ii) Involves a determination of the fair market value of any property; or

(iii) Relates to a transaction that, *prima facie*, is designed to avoid income tax.

An application is not rejected unless the applicant has been given an opportunity to be heard. Where an application is accepted, the Authority examines the materials placed before it and, if so requested by the applicant, provides the applicant with the opportunity to be heard. The Authority pronounces its ruling in writing within six months of receipt of the application. [499]

---

[499] ITA, Sec. 245R.

The ruling pronounced is binding only on the applicant with respect to the transaction in relation to which the ruling was sought, and on the Commissioner and the income tax authorities subordinate to him. The advance ruling is binding unless there is a change in law or the facts. [500]

---

[500] ITA, Sec. 245S.

Where the Authority finds that a ruling pronounced by it was obtained by the applicant through fraud or the misrepresentation of facts, it may declare the ruling void. Consequently, all provisions of the ITA will apply to the applicant retrospectively as if the ruling had never been issued. [501]

---

[501] ITA, Sec. 245T.

---

j. Provisions for the Assessment of Undisclosed Income

Based on a search initiated under the provisions of the ITA, or on books of account or other documents requisitioned, the Assessing Officer may assess undisclosed income in accordance with the provisions of Chapter XIV of the ITA.

The salient features of this assessment procedure are as follows:

(i) The total undisclosed income of the person concerned will be assessed for the six tax years preceding the tax year in which the search was conducted and also the period of the current tax year, up to the date of the search.

(ii) The Assessing Officer will assess or reassess the total income with respect to each assessment year falling within the six years referred to above in (i).

(iii) The undisclosed income of the taxpayer with respect to an assessment will be chargeable to tax at the rates applicable to the relevant year for which the income is determined. [502]

(iv) On determining the undisclosed income of the six years, the Assessing Officer will issue an order of assessment and determine the sum payable by the person based on that assessment.

---

[502] ITA, Sec. 153A.

With respect to each assessment year falling within the six assessment years referred to above, or with respect to the assessment year relevant to the previous year in which the search was conducted or the requisition made, the time limit for completion of the assessment is a period of 21 months from the end of the financial year in which the last of the authorizations for search or requisition was executed. [503]

---

[503] ITA, Sec. 153B.

However, where the last authorization for search was executed after April 1, 2005, and, during the course of the proceedings for the assessment/reassessment of total income, reference is made to a Transfer Pricing Officer (see VIII, below), the 21 month period is increased to 33 months.

If, during the search or requisition, the Assessing Officer finds:

(i) Any money, bullion, jewelry or other valuable article or thing, or books of account or documents that are seized or requisitioned; and

(ii) If money, etc. belongs to a person other than the person searched or requisitioned, the money, etc. will be handed over to the Assessing Officer having jurisdiction over that other person and that Assessing

Officer will proceed against that other person in accordance with the provisions of Section 153A of the ITA. [504]

---

[504] ITA, Sec. 153C.

---

k. Refunds

A taxpayer who satisfies the Assessing Officer that the amount of tax paid by him or on his behalf, or treated as paid by him or on his behalf, for any assessment year exceeds the amount with which he is properly chargeable under the ITA for that year, the taxpayer will be entitled to claim a refund of the excess, within a period of one year from the last day of the assessment year in which the income with respect to which the claim was made was assessable.

Where, as a result of any order passed in appeal or any other proceedings under the ITA, a refund of any amount becomes due to a taxpayer, that amount will be refunded to the taxpayer by the Assessing Officer without the taxpayer having to make any claim in this regard.

In any claim for refund, it is not open to a taxpayer to question the correctness of the assessment or any other decided matter that has become final and conclusive or to ask for a review of the assessment or other matter. The taxpayer's claim is restricted to the refund of the tax wrongly paid or paid in excess.

Where a refund of any amount becomes due to a taxpayer, the taxpayer will be entitled to receive, in addition to that amount, simple interest calculated in the following manner:

(i) At a rate of 0.5% for every month or part of a month comprised in the period from April 1 of the assessment year to the date on which the refund is granted, if the refund is of tax collected at source paid, advance tax paid or tax deducted at source paid. However, no interest will be payable, if the amount of the refund is less than 10% of the tax determined under Section 143(1) or 143(3) of the ITA.

(ii) At a rate of 0.5% for every month or part of a month comprised in the period or periods from the date of payment of the tax or penalty to the date on which the refund is granted, if the refund is of any kind other than that indicated above in (i).

In the case of a delay in a refund of more than three months from the end of the month in which total income is determined (where the total income of the taxpayer does not solely consist of interest on securities or dividends) or from the end of the month in which the claim for refund is made (in any other case), the central government will pay the taxpayer simple interest at a rate of 15% on the amount directed to be refunded from the date immediately following the expiry of the period of three months to the date of the order granting the refund.

Where, under any provision of the ITA, a refund is due to a taxpayer, the Assessing Officer, the Deputy Commissioner (Appeals), the Commissioner (Appeals), the Chief Commissioner or the Commissioner may, in lieu of paying the refund, set-off the refund amount against any amount due from the taxpayer under the ITA. [505]

---

[505] ITA, Sec. 237 to 245.

---

l. Penalties

The ITA allows the Assessing Officer, the Commissioner or other officer to penalize a taxpayer that defaults in complying with the provisions of the ITA. A taxpayer is subject to a penalty if he:

(i) Fails to furnish returns or comply with notices, or conceals income, etc.;

(ii) Fails to keep, maintain or retain books of account, documents, etc.;

(iii) Fails to keep and maintain information and document with respect to international transactions;

(iv) Fails to disclose all his income, where a search has been initiated;

(v) Fails to have his accounts audited;

(vi) Fails to furnish a report of an accountant, under Section 92E of the ITA, with respect to international transactions entered into;

(vii) Fails to deduct or collect tax at source as required under the provisions of the ITA;

(viii) Fails to comply with the provisions of Section 269SS or Section 269T of the ITA relating to the acceptance or repayment of loans or deposits by any means other than by way of an account payee check;

(ix) Fails to furnish a return of income, an annual information return or a return of fringe benefits;

(x) Fails to furnish information or documents with respect to international transactions entered into;

(xi) In relation to any proceedings before any authority under the ITA, refuses or fails to respond to any questions, sign statements, furnish information, allow inspections, etc.;

(xii) Fails to apply for and obtain a PAN or a tax deducted at source number; or

(xiii) Fails to pay advance tax or makes a false estimation in relation to advance tax.

Each of the relevant provisions sets out the quantum of penalty, subject to limits. The Commissioner has discretionary power to reduce or waive a penalty or grant immunity from a penalty to the taxpayer, subject to the fulfillment of specific conditions.

No penalty for such a failure may be imposed on a taxpayer, if he proves that there was reasonable cause for the failure. In addition, no order imposing a penalty may be issued against a taxpayer without giving him a reasonable opportunity to be heard [506]

---

[506] ITA, Chapter XXI, Secs. 271 to 275.

---

m. Offences and Prosecutions

A taxpayer may be punished with a rigorous imprisonment term, as determined on a case-by-case basis, if the taxpayer:

(i) Fails to obey an order referred to in Section 132(3) of the ITA relating to search and seizure;

(ii) Fails to comply with the provisions of Section 132(1)(iib) of the ITA relating to search and seizure;

(iii) Fails to disclose all his income by fraudulently removing, concealing, transferring or delivering property or an interest in property to any person, with the intention of thwarting tax recovery;

(iv) Fails to comply with the provisions of Sections 178(1) and 178(3) of the ITA relating to liquidation of a company;

(v) Fails to pay tax to the credit of the central government as required by the ITA;

(vi) Fails to pay the tax collected at source;

(vii) Fails to pay tax and willfully attempts to evade tax, a penalty or interest imposable under the ITA;

(viii) Willfully fails to furnish returns of income;

(ix) Willfully fails to furnish returns of income in search cases;

(x) Willfully fails to produce accounts and documents;

(xi) Fails to provide a true statement in verification or delivers an account that is false or known to be false;

(xii) Fails to make true disclosure in the books of account, willfully and with an intent to enable any other

person to evade any tax, interest or penalty imposable under the ITA; or

(xiii) Abets any other person in making and delivering, or induces any other person to make and deliver, a declaration of income chargeable to tax that is false or known to be false.

If a taxpayer is convicted of any offence specified above in (v), (vii), (viii), (xi) or (xiii) for a second or further time, he will be punishable for the second and for every subsequent offence with imprisonment for a term ranging from six months to seven years, and with a fine.

The Commissioner has the discretionary power to grant to the taxpayer immunity from prosecution for any offence under the ITA, subject to fulfillment of specific conditions.

No punishment for any of the above failures may be imposed on a taxpayer, if he proves that there was reasonable cause for having committed the failure. [507]

---

[507] ITA, Secs. 275A to 278AB.

B. Wealth Tax

Wealth tax in India is levied under the Wealth Tax Act, 1957. The tax is payable each year on taxable wealth. Liability to wealth tax depends on residential status and citizenship.

Resident Indian citizens and companies pay tax on global wealth. Individuals who are "resident but not ordinarily resident," and nonresident individuals and companies are taxed on their wealth in India, their foreign wealth being entirely exempt.

Foreign citizens, whether resident in India or abroad, pay wealth tax only on net wealth in India. Foreign wealth is exempt.

Residential status for wealth tax purposes is determined in the same way as for purposes of income tax.

Wealth tax is payable on the aggregate value of chargeable assets as reduced by the value of debts owed on the valuation date. The valuation date is uniformly fixed at March 31.

The following specified assets, net of debts, are chargeable to wealth tax:

(i) Residential houses and guest houses, except the following, which are exempt:

- **Any house allotted by a company to an employee earning remuneration of less than Rs.500,000 per annum;**
- **Any house used for residential or commercial purposes that forms part of stock-in-trade (inventory);**
- **Any house that a taxpayer occupies for purposes of a business or profession carried on by him;**
- **Any residential property that has been let out for a minimum period of 300 days in the tax year;**
- **Any property in the nature of a commercial establishment or complex; and**
- **Any farm house within 25 kilometers (approximately 15 miles) of the limits of any local municipality;**

(ii) Motor cars, other than those run on hire or held as stock-in-trade (inventory);

(iii) Jewelry or bullion other than stock-in-trade (inventory);

(iv) Yachts, boats and aircraft (other than those used for commercial purposes);

(v) Urban land; and

(vi) In the case of an individual or a HUF, cash on hand in excess of Rs.50,000.

No other assets are chargeable to wealth tax. The total value of the assets listed above in excess of Rs.3 million is subject to wealth tax at the rate of 1%.

The value of assets, other than cash, is the estimated price the assets would fetch if sold in the open market. Detailed

rules are specified for the valuation of certain assets.

A debt is a sum of money that is payable or will become payable under a current obligation that has accrued and is subsisting. However, certain debts located outside India in the case of noncitizens and nonresidents, or residents who are "not ordinarily resident," are not deductible. Also nondeductible are debts secured on, or incurred in relation to, exempted assets, and taxes disputed in appeal and outstanding for more than 12 months.

Wealth tax returns are due at the same time each year as income tax returns, and wealth tax is payable along with the returns.

The procedural requirements relating to the filing of returns, assessments, appeals, etc. under the Wealth Tax Act are similar to those under the ITA.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VI. Special Provisions Applicable to Nonresidents

A. Residence

1. Individuals

A nonresident individual is an individual who is not a resident individual. For the definition of a resident individual, see V, A, 2, a, above.

2. Companies

A nonresident company is a company that is not a resident company. For the definition of a resident company, see V, A, 2, c, above. In particular, a foreign company would be nonresident if part of its management and control were situated outside India.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VI. Special Provisions Applicable to Nonresidents

B. Scope of Income Chargeable to Tax

A nonresident (whether an individual or a legal entity) is taxed on all income in a tax year, from whatever source derived, that:

(i) Is received or deemed to be received in India; or

(ii) Accrues or arises, or is deemed to accrue or arise, in India. [508]

---

[508] **ITA, Sec. 5.**

Note: **Income arising or accruing outside India is not deemed to be received in India by reason only of the fact that it is taken into account in a balance sheet prepared in India.**

Income taxed on the basis that it accrues or arises, or is deemed to accrue or arise, in India is not taxed again on the basis that it is received or deemed to be received in India.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VI. Special Provisions Applicable to Nonresidents

C. Computation of Taxable Income: Special Provisions

Except as otherwise provided, the special provisions for computing taxable income described in 1 to 7, below, apply with respect to nonresident individuals and foreign companies.

1. Business of Mineral Oil Exploration

Income of a nonresident from the business of providing services and facilities or leasing plant and machinery in connection with prospecting for, or the extraction or production of, mineral oils, is computed at a flat rate of 10% of the amounts paid or payable (whether in or out of India) for providing services and facilities, or leasing plant and machinery, in connection with mineral oil prospecting/extraction/production in India, and of the amount received or

deemed to be received in India for providing services and facilities, or leasing plant and machinery, in connection with mineral oil prospecting/extraction/production outside India. A nonresident that claims that the profit is lower than the deemed income indicated above is required to maintain the prescribed books of account and other documents, and to have them audited. [509]

[509] ITA, Sec. 44BB.

Note: **"Plant" includes ships, aircraft, vehicles, drilling units, scientific apparatus and equipment used for exploration for mineral oils. "Mineral oils" include petroleum and natural gas. The above provisions do not apply if the provisions of Section 42, 44D, 44DA or 115A of the Income Tax Act of 1961 (ITA) apply to the taxpayer or if the central government has granted an exemption, reduction in rate, or other modification with respect to income tax payable by any person in connection with the above business under the powers vested in it.**

2. Business of Operating Aircraft

Income of a nonresident from the operation of aircraft is computed at a flat rate of 5% of the amount paid or payable to the taxpayer or any person on behalf of the taxpayer for the transportation of passengers, livestock, mail or goods from any place in India, and of the amount received or deemed to be received in India by or on behalf of the taxpayer on account of such transportation from any place outside India. [510]

[510] ITA, Sec. 44BBA.

3. Shipping Business

Income of a nonresident from the business of operating ships is computed at a flat rate of $7^{1}/_{2}$% of the amount paid or payable (whether in or out of India) to or on behalf of the taxpayer for the transportation of passengers, livestock, mail or goods shipped at any port in India, and of the amount received or deemed to be received in India by or on behalf of the taxpayer on account of such transportation at any port outside India, and includes any amount paid or payable as demurrage charges, or received or deemed to be received as handling charges or any other amount of similar nature. [511]

[511] ITA, Sec. 44B.

4. Business of Civil Construction for Turnkey Power Projects

Income of a foreign company engaged in the business of civil construction, the erection of plant or machinery, or the testing and commissioning thereof in connection with turnkey power projects approved by the central government is computed at a flat rate of 10% of the amount paid or payable (whether in or outside India) on account of such business. A nonresident that claims that the profit is lower than the deemed income indicated above is required to maintain the prescribed books of account and other documents, and to have them audited. [512]

[512] ITA, Sec. 44BBB.

5. Head Office Expenses

A nonresident carrying on any business or profession in India through a branch, office, etc., is entitled to a deduction in computing its taxable profits with respect to general administrative expenses incurred by its foreign head office, to the extent such expenses are related to its business or profession in India. [513] The deduction with respect to head office expenses is limited to the lesser of:

[513] ITA, Sec. 44C.

(i) 5% of the adjusted total income; or

(ii) Such head office expenditure incurred by the taxpayer as is attributable to the business or profession in India.

Where the adjusted total income of the taxpayer is a loss, the amount above under (i) will be computed at the rate of 5% of the average adjusted total income of the taxpayer.

The "adjusted total income" means the total income computed in accordance with the provisions of the ITA but without giving effect to carried forward depreciation, investment allowance, losses, etc.

"Head office expenditure" means executive and general administrative expenditure incurred by the assessee outside India, including expenditure incurred with respect to:

(i) Rent, rates, taxes, repairs or insurance of any premises outside India used for purposes of the business or profession;

(ii) Salary, wages, annuity, pension, fees, bonus, commission, gratuity, perquisites or profits in lieu of or in addition to salary, whether paid or allowed to any employee or other person employed in, or managing the affairs of, any office outside India;

(iii) Traveling by any employee or other person employed in, or managing the affairs of, any office outside India; and

(iv) Such other matters connected with executive and general administration as may be prescribed.

6. Income from Prospecting for Mineral Oils

The central government is authorized by the ITA to enter into an agreement with any person for prospecting for, or the extraction or production of, mineral oils (which include petroleum and natural gas) and to grant certain allowances to that person against the profits or gains of the business. Such an agreement must be approved by parliament before becoming effective.

A taxpayer may claim allowances specified in the agreement in relation to:

(i) Abortive exploration expenses;

(ii) Drilling and exploration expenses after the commencement of commercial production; and

(iii) The depletion of mineral oil in the mining area.

These expenses may be in lieu of or in addition to the permissible deductions under the provisions of the ITA. In such joint ventures, a nominee of the central government, such as a corporation established under a special statute, may be a participant instead of the government itself. [514]

---

[514] ITA, Sec. 42.

Comment: **This special incentive for oil exploration and development is taken into account in negotiations with foreign oil companies and is made a part of any overall agreement.**

7. Royalties and Fees for Technical Services

The income of a nonresident (not being a company) or a foreign company by way of royalties or fees for technical services must be computed under the head "Profits and gains of business or profession" and is taxed at the rate of 40% on a net basis if the royalties or fees for technical services are:

(i) Received from the government or an Indian concern after March 31, 2003;

(ii) In connection with business of a permanent establishment (PE) in India or for the performance of professional services from a fixed place in India; and

(iii) Paid as a result of a right, property or contract that is effectively connected with the PE or fixed place.

However, the nonresident is not entitled to deduct the following:

(i) Any expenditure or allowance that is not wholly and exclusively incurred for the business of the PE or fixed place in India; or

(ii) Any amounts paid (otherwise than towards reimbursement of actual expenses) by the PE to its head office or to any of its other offices.

The provisions of Section 44BB of the ITA (see above) will not apply to any income charged under this section.

The nonresident is also required to maintain the prescribed books of account and to have them audited for purposes of claiming deductions available under the heading "Profits and gains of business or profession." [515]

---

[515] ITA, Sec. 44DA.

D. Rates of Tax

1. Individuals

The income tax rates for nonresident individuals are as follows:

Taxable Income	Rates of Income Tax Assessment Year
	2011-2012
Rs.	
Up to Rs. 160,000	Nil
From Rs. 160,001 to Rs. 500,000	10% of excess over Rs. 160,000
From Rs. 500,001 to Rs. 800,000	Rs. 34,000 + 20% of excess over Rs. 500,000
Above Rs. 800,000	Rs. 94,000 + 30% of excess over Rs. 800,000

An education tax (cess) of 3% is charged on the aggregate tax.

2. Companies

The following rates apply to nonresident companies:

Source of Income	% of total taxable income
Royalties and fees for technical services effectively connected with a PE or fixed base, as discussed in 7, above.	40% of net income
Royalties and fees for technical services	10%
Interest and dividends	20%
Long-term capital gains other than gains on listed securities	20%
Short-term capital gains on listed securities	15%

The rate on long-term gains on listed securities is 0% [516] and that on short-term gains other than gains on listed securities is 40% (part of other income.

[516] ITA, Sec. 10(38).

Nonresident companies whose income exceeds Rs.10 million are required to pay a surcharge of 2.5% of their income tax liability for the assessment year 2011-12.

An education tax (cess) of 3% is charged on the aggregate tax including the surcharge.

E. Special Concessions for Foreign Enterprises/Foreign Nationals

1. Tax on Dividend, Royalties, Fees for Technical Services and Income from Units

Dividends (other than those referred to at V, A, 8, above) received by a foreign company from shares held in Indian companies are taxed at a flat rate of 20%. [517]

[517] ITA, Sec. 115A(1)(a)(A).

Royalties and fees for technical services (other than those referred to in C, 7, above) receivable by a foreign company are taxable at a flat rate of 10%. [518]

[518] ITA, Sec. 115A(1)(b)(AA) and (BB).

Interest received by a foreign company from the government or an Indian company on monies borrowed or debt incurred in foreign currency is taxed at a flat rate of 20%. [519]

[519] ITA, Sec. 115A(1)(a)(B).

Income with respect to units of a mutual fund purchased in foreign currency is taxed at a flat rate of 20%. [520]

[520] ITA, Sec. 115A(1)(a)(C).

No further deductions may be claimed in computing the income referred to above.

A taxpayer whose income comprises only the income indicated above (except royalties and fees for technical services), where tax has been properly deducted at source from such income, is not required to file a return of income.

2. Interest on Deposits, etc.

The following Interest is exempt:

(i) Interest payable by a scheduled bank to a nonresident or to 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 Reserve Bank of India (RBI); [521]

(ii) Interest received by a nonresident, or a person who is not ordinarily resident, in India on a deposit made in an Offshore Banking Unit (OBU), as referred to in Section 2(u) of the Special Economic Zones Act, 2005. [522]

[521] ITA, Sec. 10(15)(iv).

[522] ITA, Sec. 10(15(viii).

3. Tax Paid on Behalf of a Foreign Company

Tax paid by the government or an Indian concern on behalf of a foreign company deriving income from royalties or fees for technical services is not included in the total income of the foreign company, provided the income by way of royalties or fees for technical services is derived by the foreign company under an agreement in conformity with the Industrial Policy, or is otherwise approved by the government, and the payment of tax is made pursuant to one of the terms of the agreement. However, the tax so paid will have to be included in the total income of the foreign company if it is paid under an agreement entered into on or after June 1, 2002. [523]

[523] ITA, Sec. 10(6A).

Tax paid by the government or an Indian concern on behalf of a foreign company or a nonresident not being a company is not included in the total income of the foreign company or nonresident, if the income (other than salary, royalties and technical fees) is derived by the foreign company or nonresident under an approved agreement between the government of India and the government of a foreign state or an international organization. The tax payment must also be made pursuant to one of the terms of the approved agreement. However, the tax so paid will have to be included in the total income of the foreign company if it is paid under an agreement entered into on or after June 1, 2002. [524]

[524] ITA, Sec. 10(6B).

Tax paid by an Indian concern on behalf of a foreign enterprise is not included in the total income of the foreign enterprise if the income is derived by the foreign enterprise under an agreement approved by the central government from an Indian concern (that is engaged in the business of operating aircraft), as consideration for the acquisition of an aircraft or aircraft engine (other than by way of payment for providing spares, facilities or services in connection with the operation of leased aircraft) on lease. [525]

[525] ITA, Sec. 10(6BB).

Income by way of royalties or fees for technical services received by a foreign company is exempt from tax if the income is received under an agreement entered into with the government of India for providing services in or outside India in projects in connection with the security of India. [526]

[526] ITA, Sec. 10(6C).

4. Income of Offshore Funds

Where the income of an overseas financial organization (an "offshore fund") includes income received with respect to

units of specified mutual funds purchased in foreign currency or long-term capital gains arising from the transfer of such units, such income is taxed at the rate of 10%, and the other income of the foreign organization is taxed at the normal rates.

No deductions are allowed against income received with respect to such units or on the transfer of such units. [527]

[527] ITA, Sec. 115AB.

5. Income of Foreign Institutional Investors

Income from securities listed on a recognized stock exchange (other than income referred to at 4, above, and dividends referred to at V, A, 8, above) of a foreign institutional investor notified in the Official Gazette by the central government is taxed at the rate of 20%. However, short-term capital gains arising from the transfer of listed securities are taxed at the rate of 15%. The short-term capital gains arising from the transfer of other securities are taxed at the rate of 30% and the long-term capital gains at the rate of 10%. No deductions are allowed against such income. [528]

[528] ITA, Sec. 115AD.

Long-term capital gains for this purpose means capital gains on securities held for not less than one year. The other income of a foreign institutional investor is taxed at normal rates.

6. Income or Capital Gains from Bonds or Global Depository Receipts Purchased in Foreign Currency or Dividends on Global Depository Receipts Purchased in Foreign Currency

The following income of nonresidents from investments purchased in foreign currency is taxable at the rate of 10% and no deductions are allowed against such income: [529]

[529] ITA, Sec. 115AC.

(i) Interest on bonds of an Indian company issued in accordance with a notified scheme or on bonds of a public sector company sold by the government;

(ii) Dividends (other than dividends referred to at V, A, 8, above) on global depository receipts (GDRs) of an Indian company issued in accordance with a notified scheme or on GDRs issued against the shares of a public sector company sold by the government;

(iii) Dividends (other than dividends referred to at V, A, 8, above) on GDRs reissued in accordance with a notified scheme; and

(iv) Long-term capital gains arising from the transfer of bonds or GDRs.

7. Foreign Technicians and Academics

A limited exemption from Indian income tax is extended to foreign technical and academic personnel, as described in a and b, below.

a. Employees of Foreign Enterprises

An individual who is not a citizen of India is exempt from tax on his remuneration received as an employee of a foreign enterprise for services rendered by him during his stay in India if: the foreign enterprise is not engaged in any trade or business in India; the individual's stay in India does not exceed a period of 90 days in the tax year; and the remuneration is not liable to be deducted from the income of the employer chargeable under the ITA. [530]

[530] ITA, Sec. 10(6)(vi).

b. Consultants

Any remuneration or fees received by a consultant out of funds made available to any international organization under a technical assistance grant agreement between the organization and a foreign government, and any other income accruing or arising to the consultant outside India on which income tax or social security tax is payable in the country of the consultant's origin, is exempt from tax. [531]

[531] ITA, Sec. 10(8A).

Similarly, in the case of an individual who is assigned duties in India in connection with any technical assistance program or project in accordance with an agreement entered into by the central government and an international

organization, remuneration received by the individual from a consultant as referred to above, and any other income accruing or arising to the individual outside India, is exempt from tax provided: the individual is an employee of the consultant referred to above and is either not a citizen of India or, being a citizen of India, is not ordinarily resident in India; and the contract of service of the individual is approved by the prescribed authority before commencement of the individual's service. [532]

---

[532] **ITA, Sec. 10(8B).**

Note: **The Authority for Advance Ruling has held that a person's special knowledge and experience would determine whether the person is a technician. The Authority has further ruled that the intention of the legislature was to grant exemption liberally with respect to foreign technicians.**

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VI. Special Provisions Applicable to Nonresidents

F. Tax Deducted at Source

For a discussion of the deduction of tax at source from payments to foreign companies, nonresident individuals, offshore funds and foreign institutional investors, and nonresident sportsmen or sports associations, see V, A, 10, above.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VI. Special Provisions Applicable to Nonresidents

G. Submission of Returns

See V, A, 11, c, above.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VI. Special Provisions Applicable to Nonresidents

H. Special Provision for the Computation of the Total Income of Nonresidents

No deduction with respect to any expenditure or allowance will be allowed in computing the investment income of a nonresident Indian from a foreign exchange asset, i.e., any income derived (other than dividends referred to in Section 115-O of the ITA).

If, in the case of a taxpayer who is a nonresident of India:

(i) The taxpayer's gross total income consists only of investment income or income by way of long-term capital gains or both, the taxpayer will not be allowed any deduction under Chapter VI-A of the ITA (see V, A, 9, above), or the benefit of indexation (see V, A, 4, d, above) in computing income under the head "Capital gains;"

(ii) The taxpayer's gross total income includes any income referred to above in (i), the gross total income will be reduced by the amount of such income and the deductions under Chapter VI-A will be allowed as if the gross total income so reduced were the gross total income of the taxpayer. [533]

---

[533] **ITA, Sec. 115D.**

---

1. Tax on Investment Income and Long-Term Capital Gains

Where the total income of a taxpayer who is a nonresident of India includes any investment income or long-term capital gains on the transfer of an asset other than a specified asset, and long-term capital gains on a specified asset, the tax payable by him will be the aggregate of:

(i) The amount of income tax calculated on the investment income and the long-term capital gain on an asset other than a specified asset, if any, included in the total income, at the rate of 20%;

(ii) The amount of income tax calculated on the long-term capital gains, if any, on the specified assets

included in the total income, at the rate of 10%; and

(iii) The amount of income tax to which he would have been chargeable had his total income been reduced by the amount of the income referred to above in (i) and (ii). [534]

---

[534] ITA, Sec. 115E.

---

2. Capital Gains on the Transfer of Foreign Exchange Assets Not to Be Taxed in Certain Cases

If a taxpayer who is a nonresident Indian, on making a long-term capital gain from the transfer of a foreign exchange asset (the "original asset"), invests the whole or any part of the net consideration in any specified asset (the "new asset"), within a period of six months after the date of the transfer of the original asset, the capital gain will be dealt in the following manner:

(i) If the cost of the new asset is not less than the net consideration received with respect to the original asset, the whole of the capital gain will be exempt; and

(ii) If the cost of the new asset is less than the net consideration received with respect to the original asset, so much of the capital gain, as bears to the whole capital gain the same proportion as the cost of acquisition of the new asset bears to the net consideration, will be exempt.

However, if the new asset is transferred or converted (otherwise than by transfer) into money within a period of three years from the date of its acquisition, the amount of capital gain exempted as described above in (i) or (ii), will be deemed to be income chargeable under the head "Capital gains" relating to long-term capital gains of the previous year in which the new asset is transferred or converted (otherwise than by transfer) into money. [535]

---

[535] ITA, Sec. 115F.

---

3. Return of Income Not to Be Filed in Certain Cases

A nonresident Indian need not furnish a return of his income under Section 139(1) of the ITA if:

(i) His total income during the previous year consists only of investment income or income by way of long-term capital gains or both; and

(ii) Tax on such income has been deducted at source. [536]

---

[536] ITA, Sec. 115G.

---

4. Benefit to be Available in Certain Cases Even After a Taxpayer Becomes Resident

Where a person who is a nonresident Indian in any previous year becomes assessable as resident in India with respect to the total income of any subsequent year, on his furnishing to the Assessing Officer a declaration in writing along with his return of income under Section 139 of the ITA, for the assessment year for which he is so assessable, the provisions discussed in this section will continue to apply to him in relation to investment income derived from a foreign exchange asset for that assessment year and for every subsequent assessment years until the transfer or conversion (otherwise than by transfer) into money of that asset. [537]

---

[537] ITA, Sec. 115H.

---

5. Provisions Not to Apply if a Taxpayer so Chooses

A nonresident of India may elect not to be governed by the provisions discussed at 1 through 4, above for any assessment year by furnishing his return of income for that assessment year under Section 139 of the ITA and declaring in the return that the above provisions do not apply to him for that assessment year. If he does so, then the provisions will not apply to him for that assessment year and his total income for that assessment year will be computed and tax on such total income charged in accordance with the other provisions of the ITA. [538]

---

[538] ITA, Sec. 115-I.

A. General

India imposes the following indirect taxes:

(i) Excise duty;

(ii) Customs duty;

(iii) Octroi;

(iv) Stamp duty,

(v) Sales tax/value added tax (VAT),

(vi) Service tax; and

(vii) Securities transaction tax.

The two main enactments governing indirect taxation in India are the Central Excise Act, 1944 (CEA) and the Customs Act, 1962, which are administered by the central government. At the state level, the important indirect taxes are the sales tax and octroi (entry tax).

Indirect taxes have an important bearing on the cost component of many products.

B. Excise Duty

1. Power to Levy Excise Duty

Excise duty is levied and collected by the central government under the powers vested in it by the Constitution of India and is also referred to as "central excise."

The CEA is the statute providing for the charging of excise duty on tobacco and manufactured goods, except alcoholic liquors for human consumption, opium and narcotics. The power to impose excise duty on alcoholic liquors for human consumption, opium and narcotics is granted to the states by the Indian Constitution.

Excise duty is a duty or tax levied on the manufacture or production of goods in India. The term "manufacture" is defined to include any process incidental or ancillary to the completion of a manufactured product. Through a deeming fiction, the CEA extends the scope of the term "manufacture" to include certain processes or activities such as repacking, re-labeling, declaring or altering the retail sales price, etc. in relation to certain specified goods, that would not otherwise amount to manufacture under the principles evolved by the courts or in the conventional sense of the term. [539]

---

[539] Central Excise Act, 1944 (CEA), Sec. 2(f).

---

2. Charge of Excise Duty

Excisable goods are those specified in the First and Second Schedules to the Central Excise Tariff Act, 1985 (CETA). [540]

---

[540] CEA, Sec. 2(d).

There are three basic conditions for the charging of excise duty: [541]

---

[541] CEA, Sec. 3.

(i) The duty must be on goods;

(ii) The goods must be excisable; and

(iii) The goods must be manufactured or produced in India.

The following duties are levied if the conditions above are fulfilled:

(i) Excise duty at the rates specified in the First Schedule to the CETA; or

(ii) Special excise duty at the rates specified in the Second Schedule to the CETA.

Unless all the above conditions are satisfied, excise duty may not be levied. The word "goods" has not been defined under the CEA, but the Constitution of India defines goods to include all materials, commodities and articles. The effective rate of duty may be lower, pursuant to a general or specific notification issued by the central government in this regard granting whole or partial relief from duty. [542]

---

[542] CEA, Sec. 5A.

Excise duty is payable by the manufacturer but is, commercially, recovered from the buyer as a part of the consideration for the sale of the goods concerned. The duty to pay is fastened on manufacturing, but for administrative purposes the duty is collected at the time of clearance.

Excise duty exemptions are available to 100% Export Oriented Undertakings (EOUs) and units in Special Economic Zones (SEZs).

3. Basis of Charge

The excise duty charge is on one of the following bases:

(i) Specific duty: payable based on units of weight, length, thickness and similar measurements.

(ii) *Ad valorem* duty: payable based on assessable value. Duty on most items is determined on an *ad valorem* basis. Since July 1, 2000, the concept of transaction value has been brought into the central excise law as a precursor to the introduction of a fully-fledged VAT. Duty in most cases is levied based on the "transaction value" of the excisable goods, which is the value/price: (a) for delivery at the time and place of removal; (b) where the buyer is not a related person; and (c) price is the sole consideration. "Transaction value" means the price actually payable on the sale of goods and includes, in addition to the amount charged as price, any amount that the buyer is liable to pay to, or on behalf of, the taxpayer, but does not include excise duty, sales tax or other taxes. [543]

(iii) As a percentage of "tariff" value: "tariff" value is a notional value fixed by the government for determining the duty payable. Different tariff values may be determined for different classes of goods manufactured by different categories of manufacturers and sold to different categories of buyers. Tariff values, however, are very rarely fixed. The Supreme Court has upheld the constitutional validity of this provision. [544]

(iv) Duty based on maximum retail price: maximum retail price-based valuation is applicable to goods covered under the Standards of Weights and Measures Act, 1976 and notified by the central government in this regard. The valuation has to be done based on the retail sale price declared on the package less allowable deductions and abatements. [545]

(v) Duty based on annual production capacity: under Section 3A of the CEA, the central government may notify specify goods with respect to which the payment of duty is based on the production capacity without any reference to actual production.

(vi) Compounded levy scheme: normal excise procedures may sometimes not be practicable when there are numerous small manufacturers of certain products. Rule 15 of the Central Excise Rules provides that the central government may notify specified goods with respect to which a manufacturer may have the option of paying duty based on specified factors relevant to the production of such goods and at specified rates.

---

[543] CEA, Sec. 4.

[544] *Century Manufacturing Co. Limited v. Union of India* (1922) 60 ELT 3.

[545] CEA, Sec. 4A.

Excise duty is payable at the time of the removal of the goods from the factory or warehouse. Having to pay duty separately on each consignment may be avoided by maintaining a deposit account with the excise authorities.

4. Administration

The CEA grants power to the government to draw up rules for prescribing procedures. [546] Various rules have been prescribed by the government for administering the CEA. Rules play an important part in the administration of the CEA, as the scheme for levying excise is very much procedure oriented. Most instances of penalties being imposed and benefits being lost are the result of procedures not being followed. The relevant provisions are as follows:

---

[546] CEA, Sec. 37.

(i) The Central Excise Rules, 2002: these rules provide for various procedures to be followed, the determination, assessment and collection of duty, the clearance and storage of goods, the manner of payment of duty, the filing of returns, registration, the maintenance of records, invoicing, rebates, remission, refund procedures and export without payment of duty.

(ii) The Central Excise Appeal Rules, 2001: these rules prescribe the procedures to be followed with regard to filing appeals before the relevant statutory authorities.

(iii) Notifications: the central government has the power to issue notifications exempting certain goods fully or partially from excise duty. Notifications require the approval of Parliament and are treated as a part of the CEA.

(iv) CETA: the CETA prescribes different duty rates for different categories of items. Initially, when the Central Excise and Salt Act, 1944 (CESA now known as the CEA) was enacted in 1944, the tariff items were included in the CESA itself, which made it complicated and unsystematic. The CETA was enacted in 1986 and classifies goods under 96 chapters with a specific code assigned to each item. The CETA is based on the International Convention on the Harmonized System of Nomenclature (HSN). The CETA is only based on the HSN and does not reproduce it.

(v) The Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000: These rules provide the basis for determining the value of goods for purposes of excise duty, where transaction value cannot be determined or where goods are not sold but used/consumed in the manufacture of other goods.

(vi) The Central Value Added Tax (CENVAT) Credit Rules, 2004: to avoid a cascading effect, a scheme known as CENVAT has been in force since April 1, 2000. Under the CENVAT Scheme, a manufacturer may avail itself of a credit for central excise duties or additional duties of customs, including the education cess paid on specified inputs and capital goods used in the manufacture of excisable goods, and utilize it in discharging the duty on finished excisable goods. The credit mechanism has been further expanded to allow the inter-sectoral credit of tax paid on goods and services. The rules prescribe the procedure for obtaining the CENVAT credit (i.e., the duty paid on inputs) against the liability on the final goods.

(vii) The Central Excise (Settlement of Cases) Rules, 2007: these rules prescribe the procedural aspects relating to applications to the settlement commission with respect to any proceeding pending before the Central Excise Officer having jurisdiction over the matter concerned.

(viii) The Authority for Advance Ruling relating to customs and central excise for foreign investors: the Customs (Advance Rulings) Rules, 2002 and the Central Excise (Advance Rulings) Rules, 2002 allow a nonresident investor setting up a joint venture in India in collaboration with a nonresident or a resident, or a resident setting up a joint venture in India in collaboration with a nonresident or a wholly-owned subsidiary company of a foreign holding company, to seek, in advance, a ruling from the Authority. Such a ruling may be only with respect to:

- The classification of goods; and
- The principles of valuation and the applicability of duty exemption notifications that are relevant in determining the liability to duty with respect to an "activity" (i.e., the import, export, production or manufacture of goods) proposed to be undertaken by the venture.

The statute requires the Authority to give an advance ruling within three months. The objective is to provide certainty as to the liability to duty of the applicant, as a ruling is binding on the applicant, the matter referred to the Authority for ruling and the jurisdictional commissioner (subject to the law and facts remaining unchanged) and may not be appealed.

5. Export Concessions and Procedures

There are basically two ways in which exporters may avail themselves of concessions with respect to goods exported. In the first, the duty is paid and a refund is subsequently claimed when the goods are exported. In the second, the

goods are exported under bond without the payment of excise duty — on completion of the export, the bond is released. Regular exporters generally have a continuing bond for the purpose.

The government has devised various schemes whereby inputs may be obtained free of excise duty or a refund of excise duty may be obtained in relation to exports. These are:

(i) The setting up of Free Trade Zones (FTZs) where duty free imports are permitted and finished goods may be exported without payment of duty subject to prescribed procedures being followed. If goods are not exported, the manufacturer may sell up to 25% of production (in terms of value) in the domestic market. Such goods are liable to excise duty at specified rates;

(ii) The setting up of 100% EOUs;

(iii) The Duty Drawback Scheme (see C, 7, b, below);

(iv) Permission to obtain CENVAT credits (see 6, below) on inputs for other similar final products; and

(v) A refund of the duty on inputs if the CENVAT credit cannot be used.

6. Central Value Added Tax Credit Scheme

To avoid a cascading effect, a scheme known as CENVAT has been in force since April 1, 2000. Under the CENVAT Scheme, a manufacturer may avail itself of a credit for central excise duties or additional duties of customs, including the education cess paid on specified inputs and capital goods used in the manufacture of excisable goods, and utilize it in discharging its duty on finished excisable goods. The credit mechanism has been further expanded to allow a credit for tax paid on goods and services (see G, below).

C. Customs Duty

1. Scope and Coverage of Customs Law

The Customs Act, 1962 provides for the levy and collection of duty on imports as well as exports of goods. [547]

[547] Customs Act, 1962, Sec. 12.

Goods under the Customs Act, 1962 include:

(i) Vessels, aircraft and vehicles;

(ii) Stores;

(iii) Baggage;

(iv) Currency and negotiable instruments; and

(v) Any other kind of movable property. [548]

[548] Customs Act, 1962, Sec. 2(22).

The rates of customs duty are prescribed in the Customs Tariff Act, 1975, read with the relevant exemption notifications. Import duty is levied on most products, whereas the levy of export duty is restricted to a very few products. The Customs Act is a tool with which the government regulates imports and exports in line with government policy. In addition, the provisions of the customs law are also referred to in other acts, such as the Foreign Trade (Development & Regulation) Act and the Foreign Exchange Management Act. The scope and applicability of the customs law is governed by various acts, rules, regulations and notifications.

2. Taxable Event

Goods become liable to import duty or export duty where there is an import into or export out of India. Import is defined as bringing (goods) into India from a place outside India. [549] Export is defined as taking (goods) out of India to a place outside India. [550] For these purposes, India includes the territorial waters of India. [551] The territorial waters extend 12 nautical miles into the sea from the base line on the coast of India.

[549] Customs Act, 1962, Sec. 2(23).

[550] Customs Act, 1962, Sec. 2(18).

[551] Customs Act, 1962, Sec. 2(27).

3. Customs Tariff Act, 1975

The Customs Tariff Act, 1975 gives the classification of, and rates of duties for, imports and exports under two Schedules. The Act also provides for additional duty (countervailing duty), special additional duty, safeguard duty, preferential duty, and anti-dumping and protective duties.

4. Rules and Regulations

Under the Customs Act, 1962, the central government is empowered to make rules and regulations consistent with the provisions of the Act. The important rules so made are:

(i) The Customs Valuation (Determination of Price of Imported Goods) Rules, 2007, which provide the basis for valuing imported goods for purposes of determining the duty payable;

(ii) The Customs Valuation (Determination of Price of Exported Goods) Rules, 2007, which provide the basis for valuing exported goods for purposes of determining the duty payable;

(iii) The Customs and Central Excise Duties and Service Tax Drawback Rules, 1995, which provide the basis for calculating the rates of duty drawback on exports. Drawback in relation to any goods manufactured in India and exported means the rebate of duty or tax chargeable on any imported or excisable materials or taxable services used as input services in the manufacture of such goods;

(iv) The Baggage Rules, 1998, which provide the rules and allowances for the bringing in of baggage from abroad by Indians and visitors;

(v) The Customs (Advance Rulings) Rules, 2002: Authority for Advance Ruling relating to customs and central excise for foreign investors. The Customs (Advance Rulings) Rules, 2002 and the Central Excise (Advance Rulings), 2002 allow a nonresident investor setting up a joint venture in India in collaboration with a nonresident or a resident, or a resident setting up a joint venture in India in collaboration with a nonresident or a wholly-owned subsidiary company of a foreign holding company, to seek a ruling from the Authority in advance. Such rulings may be with respect only to:

- **The classification of goods; and**

- **The principles of valuation and the applicability of duty exemption notifications that are relevant in determining the liability to duty with respect to an "activity" (i.e., the import, export, production or manufacture of goods) proposed to be undertaken by the venture. The statute requires the Authority to give an advance ruling within three months. The objective is to provide certainty as to the liability to duty of the applicant, as a ruling is binding on the applicant, the matter referred to the Authority for ruling and the jurisdictional commissioner (subject to the law and facts remaining unchanged) and may not be appealed.**

(vi) The Customs (Appeals) Rules, 1982, which prescribe the procedures to be followed with regard to filing appeals before the relevant statutory authorities;

(vii) The Customs (Settlement of Cases) Rules, 2007, which prescribe the procedural aspects relating to applications to the settlement commission with respect to any proceeding pending before the Customs Officer having jurisdiction over the matter concerned;

(viii) The Customs (Import of Goods at Concessional Rate of Duty for Manufacturing Excisable Goods) Rules, 2007, which apply to an importer who intends to avail itself of the benefit of an exemption notification issued under sub-section (1) of Section 25 of the Customs Act, 1962 (under which goods of a specified description may be exempt from customs duty), where the benefit of the exemption is dependent on the use of the imported goods covered by the notification for the manufacture of an excisable commodity;

(ix) The Project Import Regulations, 1986. Heavy customs duty on machinery imported for a project to be executed in India could make the start-up project costs very high and the project unviable. These regulations prescribe procedures for project imports required for initial set-up or substantial expansion at concessional customs duty rates;

(x) The Customs House Agents Licensing Regulations, 1984, which regulate clearing and forwarding agents;

(xi) The Notifications. Pursuant to the powers vested in it by the Customs Act, the central government has specified certain goods as exempt from customs duty and prohibited certain goods from being imported

into or exported from India.

5. Types of Customs Duty

Tariff rates for customs duty are prescribed in the Customs Tariff Act, 1975. The different types of duty are:

(i) Basic customs duty. This is the basic duty levied under Section 12 of the Customs Act. Duty is levied at the rates specified in the First and Second Schedules to the Customs Tariff Act, 1975. The duty payable is measured as a percentage of the transaction value determined under Section 14(1) of the Customs Act. This value is the price actually paid or payable for the goods when sold for export to India for delivery at the time and place of importation or for the export from India for delivery at the time and place for exportation, and includes other components of costs to the extent and in the manner specified in rules made in this behalf. Different rates have been prescribed for different items.

(ii) Additional customs duty (also known as CVD). This additional duty is levied under Section 3(1) of the Customs Tariff Act. The additional duty is equal to the excise duty levied on a like product manufactured or produced in India. If a like product is not produced or manufactured in India, the base for the levy of CVD is the excise duty that is leviable on the class or description of articles to which the imported article belongs. If different rates are leviable on the product, the highest rate will be taken. CVD is levied on the total of value of the goods plus the basic customs duty payable.

(iii) Special additional duty. In addition to CVD, which is chargeable on all goods, the central government may, by notification, levy a special additional duty. The rate is notified by the central government, having regard to the maximum sales tax, local tax or any other charges for the time leviable on a like article, on its sale or purchase in India. The purpose of this duty is to counterbalance the effect of sales tax, local tax or other charges leviable on the articles of the category to which the imported article belongs that are normally applicable to a purchase or sale that has taken place in India.

Articles that are chargeable to additional duties levied under Section (3)(1) of the Additional Duties of Excise (Goods of Special Importance) Act, 1957 are not subject to special additional duty.

(iv) Protective duty. The Tariff Commission established under the Tariff Commission Act, 1951 may recommend to the central government the imposition of protective duty to provide protection to certain industries. The central government, on being satisfied that such a need exists, may by notification levy a duty on certain imported goods. Parliamentary approval is required to give effect to the proposals with regard to protective duty on the goods to which the notification relates. The determination of the extent of the protection to be given by way of protective duty takes into consideration the following factors:

- **The protective duty should not be so severe as to discourage imports; and**
- **The protective duty should be sufficiently attractive to encourage imports to bridge the gap between the demand and supply of the relevant articles in the market.**

(v) CVD on subsidized goods. If a country pays a subsidy for exports to India to its exporters, the central government can, under Section 9 of the Customs Tariff Act, impose a CVD up to the amount of that subsidy. The duty is in addition to any other duty chargeable under the Customs Act. The central government has the power to issue a notification to impose such duty, which will cease to have effect on the expiry of five years from the date of imposition.

(vi) Safeguard duty. Safeguard duty is imposed for purposes of protecting the interests of a domestic industry. It is product specific, i.e., the safeguard duty is applicable only to those certain articles with respect to which it is imposed. The duty is in addition to any other duty chargeable under the Customs Act. Duty imposed under this section is in force for a period of four years from the date of its imposition. The central government continuously reviews the situation and will extend the imposition if it determines that the domestic industry concerned is under threat. Unless specifically made applicable, safeguard duty does not apply to articles imported by a 100% EOU or any unit in an FTZ or SEZ.

(vii) Anti-dumping duty. Large overseas companies with undisposed stocks may export or "dump" such goods into the country at unreasonably low prices, which may cripple the working of the local industry. Anti-dumping duty is country specific, i.e., it is imposed on imports from a particular country. The central government may by notification impose anti-dumping duty to the extent of the "margin of dumping," where the products concerned are sold at prices lower than the normal value. The margin of dumping is the difference between the normal value of the products and the price at which they are brought into the country. The normal value is the comparable price in the ordinary course of the trade. The central government is empowered to draw up rules for determining the normal value and export pricing to determine the margin of dumping. The duty is in addition to any other duty chargeable under the Customs Act. Duty imposed under this section is in force for a period of four years from the date of its imposition. Unless specifically made applicable, safeguard duty does not apply to articles imported by a 100% EOU or any unit in an FTZ or SEZ.

Section 9B of the Customs Tariff Act restricts the imposition of dumping duties on imports from World Trade Organization (WTO) countries and countries given the status of "Most Favored Nation" under an agreement. In the case of goods exported by such countries, the central government would issue a notification imposing duty only if the import of the articles would cause material injury to an industry established in India, or would materially retard the establishment of an industry in India.

An appeal against an order of determination or review thereof regarding the existence, degree and effect of any subsidy or dumping in relation to the import of any article may be made to the Appellate Tribunal.

6. Valuation for Customs Duty

Customs duty is payable on a value known as the "customs value" or the "assessable value." This value is a deemed value that does not depend on the price stated in the invoice and may be either a value as defined in Section 14(1) of the Customs Act or a tariff value specified in Section 14(2) of the Customs Act. Value is determined in accordance with the rules drawn up by the central government known as the Customs Valuation (Determination of Price for Imported Goods) Rules, 1988. These rules are based on the General Agreement on Tariffs and Trade (GATT) valuation code and may not supersede the provisions of the Act relating to valuation. The rules are for imported goods only and are statutorily required to be followed. The rules contain exhaustive notes that facilitate their correct application.

7. Export Promotion Schemes

a. Advance Authorization

Inputs required to manufacture export products may be imported without the payment of customs duty under Advance Authorization. Advance Authorization may be granted to merchant exporters or manufacturer exporters importing inputs, fuel, oil and catalysts. Since the raw materials may be imported before the export of the final products, the authorization issued for the purpose is called "Advance Authorization."

b. Duty Drawback

In accordance with Rule 2(a) of the Customs, Central Excise and Service Tax Drawback Rules, 1995, drawback in relation to any goods manufactured in India and exported, is the rebate of duty or tax chargeable on the imported or excisable materials used or taxable services used as input services in the manufacture of those goods. The drawback rate is fixed on the basis of the industry average for various products. The central government is authorized to issue notifications prohibiting drawback in certain cases. The drawback rules also provide for some disallowances.

c. Export Oriented Units/Special Economic Zones

The EOU scheme enables a manufacturer to import inputs without paying customs duty and export the final products subject to compliances. EOUs must have net foreign exchange earnings (NFE). Indigenous goods may be obtained without the payment of excise duty, subject to certain conditions. EOUs may sell up to 50% of the Free-on-Board (FOB) value of their previous year exports in the Domestic Tariff Area (DTA).

The Software Technology Park (STP), Electronic Hardware Technology Park (EHTP) and Bio-Technology Park (BTP) schemes are similar to the EOU scheme.

SEZs are in the nature of a separate "island" outside the jurisdiction of the country. Goods, including capital goods, may be imported without the payment of duty and services without the payment of service tax. SEZs are governed by the Special Economic Zones Act and the rules drawn up thereunder. Supplies to an SEZ from anywhere outside the SEZ (i.e., the DTA) are considered to be exports and qualify for export benefits. Supplies to the DTA from an SEZ are considered to be imports and normal customs duty is payable by the importer. An SEZ has full freedom of operations within the SEZ and all facilities for import and export are provided within the SEZ itself.

SEZ units may be set up for manufacturing goods or rendering services or for purposes of trading.

SEZs and units in SEZs are exempt from all taxes such as, customs duty, excise duty, central sales tax, VAT, service tax, income tax, etc. (See further at V, A, 9, b, above.)

d. Duty Free Import Authorization

This scheme was introduced in 2006 and is similar to the Advance Authorization scheme. Material imported under Duty Free Import Authorization (DFIA) is transferable on fulfillment of the export obligation, unlike under the Advance Authorization scheme, which does not allow for transfers. DFIA is issued to allow the duty free import of inputs, fuel, oil, energy sources, and catalysts required for export products. DFIA is initially issued with "actual user condition." Imports are exempted from basic customs duty, additional customs duty/excise duty, the education cess, and safeguard and anti-dumping duty, if any.

e. Duty Entitlement Pass Book Scheme

The objective of this scheme is to neutralize the incidence of the customs duty on the import content of an export product. The neutralization is provided by way of the granting of a credit for duty against the export product.

The scheme is similar to the CENVAT credit scheme, where the exporter gets credit when he exports the goods. The credit is based on prescribed rates and may be utilized for the payment of customs duty on imported goods including capital goods, which are freely importable.

An exporter may take either the Duty Entitlement Pass Book (DEPB) credit or the duty drawback, but not both.

The credit under this scheme may be transferred, subject to certain conditions.

f. Export Promotion Capital Goods Scheme

The Export Promotion Capital Goods Scheme (EPCG) scheme enables an Indian manufacturer to obtain capital goods at a lower or nil rate of customs duty, against commitment of an export obligation, subject to certain conditions.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VII. Indirect Taxation

D. Octroi

Octroi is a tax levied on the entry of goods within certain city limits.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis
VII. Indirect Taxation

E. Stamp Duty

1. General

The Indian Stamp Act, 1899 is a fiscal enactment governing the levying of tax in the form of stamp duties on instruments recording transactions. The primary object of the Stamp Act is to raise revenue for the state. The Stamp Act extends to the whole of India, except the states of Jammu and Kashmir. The state governments have in some cases enacted separate state stamp laws. However, the provisions of these state laws are mostly identical to those of the Indian Stamp Act, 1899.

There is a distribution of power to legislate regarding stamp duties between the center and the states. The Central Parliament has the exclusive power to fix the rates of duty with respect to bills of exchange, cheques, promissory notes, bills of lading, transfers of shares, debentures, proxies and receipts. The states have the exclusive power to legislate in the matter of rates of stamp duty with respect to all other documents. [552]

---

[552] List II, entry 63 of Schedule VII to the Constitution of India.

The Bombay Stamp Act and certain provisions of the Indian Stamp Act apply to the state of Maharashtra. The instruments executed in the state and listed in the Schedule to the Act are chargeable to stamp duty at the applicable rate. Instruments executed outside the state are liable to duty only on their receipt in the state, provided it relates to property situated in the state or a matter or thing to be done in the state. All other instruments would be charged under the Indian Stamp Act, or not at all.

2. Application of the Stamp Act to Instruments

The following principles govern the application of the Stamp Act to instruments:

(i) Subject to certain exemptions, stamp duty is leviable on an instrument and not on a transaction; [553]

(ii) Stamp duty is payable on an instrument according to its tenor, that is, it is the real nature of the transaction that determines the stamp duty; and

(iii) A transaction may be structured in such a manner that a lower rate of duty is attracted.

---

[553] Indian Stamp Act, 1899, Sec. 3.

An instrument is defined to include every document by which any right or liability is or is purported to be created, transferred, limited, extended, extinguished or recorded. However, it does not include a bill of exchange, cheque, promissory note, bill of lading, letter of credit, policy of insurance, transfer of share, debenture, proxy and receipt that are under the purview of the Stamp Act as applicable to Maharashtra. [554]

---

[554] Indian Stamp Act, 1899, Sec. 2(14).

---

3. Instruments Chargeable with Stamp Duty

An instrument is chargeable with stamp duty of the amount indicated in Schedule I to the Stamp Act, which gives a list of instruments liable to stamp duty. Instruments not mentioned in Schedule I are not subject to stamp duty. The liability of an instrument to stamp duty is determined by the Stamp Act in force at the time. Instruments in favor of the government, instruments for the sale, transfer or other disposition of a ship, bills of exchange and promissory notes executed out of India and acted upon outside India, or instruments in favor of a developer or unit, in connection with the carrying out of the purposes of a SEZ, and instruments executed outside India and relating to property situated outside India or to some other matter or thing done or to be done outside India, are not liable to stamp duty. Exemptions from stamp duty have been granted under other laws such as the Land Acquisition Act, 1894, the Indian Works of Defense Act, the Central Co-operative Societies Act, 1912, and the Co-operative Societies Acts in the various states. No revenue stamp is required to be obtained in a payment voucher if the payment does not exceed Rs.5,000.

4. Multifarious and Multi-description Instruments

In many cases, a single transaction such as a sale, mortgage or settlement may be completed by several instruments. In such cases only the principal instrument, as determined by the parties to the transaction, is chargeable to duty with the duty prescribed and the other instruments will be subject to duty of Rs.1 instead of the duty prescribed. [555]

[555] Indian Stamp Act, 1899, Sec. 4.

A multifarious instrument, that is, an instrument in which several distinct matters or transactions are embodied, is chargeable with the aggregate amount of duties with which separate instruments with respect to each distinct matter would have been chargeable. [556]

[556] Indian Stamp Act, 1899, Sec. 5.

An instrument so drawn up as to come within two or more descriptions in Schedule I to the Act (that is, a multi-description instrument) that does not contain several matters, as in the case of a multifarious instrument, is chargeable with the highest duty that may be applicable. [557]

[557] Indian Stamp Act, 1899, Sec. 6.

5. Payment of Stamp Duty

Stamp duty is generally paid at the stamp office and the payment should be indicated on the relevant instruments by means of stamps, whether adhesive or impressed. [558] However, certain instruments, such as notarial acts, transfers of shares in any incorporated company, bills of exchange and promissory notes, may be stamped using adhesive stamps. Such adhesive stamps must be cancelled once affixed to the instruments concerned, to prevent them from being used more than once. [559]

[558] Indian Stamp Act, 1899, Sec. 10.

[559] Indian Stamp Act, 1899, Secs. 11 and 12.

Stamp duty is generally payable by the person drawing, making or executing an instrument, unless otherwise determined by a contract. [560] The law relating to stamp duty in force in the state where the instrument is executed normally determines the stamp duty. Where stamp papers are used, such stamp papers must be in the name of one of the parties to the transaction. The date of issue of the stamp paper may not be more than six months prior to the date of the transaction.

[560] Indian Stamp Act, 1899, Sec. 29.

6. Valuation

The Stamp Act provides directions for valuation in certain cases, for example, where the consideration is stated in a currency other than Indian Rupees, where instruments are connected with stock or other marketable securities, where instruments are executed to secure an annuity, and where the value of the subject matter is indeterminate. In such cases, stamp duty is payable based on such valuation. [561]

[561] Indian Stamp Act, 1899, Secs. 20, 21 and 22.

7. Other Matters

The cost of the stamp duty is a matter of agreement between the parties to the transaction. However, the Act provides for methods of breaking a deadlock in specified cases.

Some of the important articles governing stamp duty on certain documents are mentioned in Schedule I to the Stamp

Act. Depending on the instrument, the duty may be payable based on the true market value of the property, area, or any other criterion.

Any person may apply to the Collector of Stamps for adjudication of the stamp duty payable on an instrument.

All instruments chargeable with duty and executed by any person in Maharashtra will be stamped before or at the time of execution or immediately thereafter, or on the next working day following the day of execution.

An instrument that is inadequately or not stamped is inadmissible as evidence for any purpose. Such an instrument may be admissible only on payment of the requisite amount of duty along with interest at 2% per month, subject to the penalty not exceeding twice the amount of the duty.

F. Sales Tax, Value Added Tax, etc.

1. Central Sales Tax

a. General

Every dealer is liable to pay tax under the Central Sales Tax (CST) Act, on sales of goods (other than electrical energy) effected by him in the course of inter-state trade or commerce during the year. The tax is payable if the sale or purchase:

(i) Occasions the movement of goods from one state to another; or

(ii) Is effected by a transfer of documents of title to the goods during their movement from one state to another.

Further, a dealer is liable to pay tax on the sale of taxable goods effected by him in the course of inter-state trade or commerce, notwithstanding that the turnover limit of sales or purchases for registration and liability for tax has not been exceeded under the relevant state tax laws.

No tax is payable on a transaction of sale in the course of the import of goods into India or a transaction of sale in the course of the export of goods outside India. Further, no tax is payable on a transaction of penultimate sale, i.e. the last sale preceding the sale occasioning the export of goods.

b. Deemed Sale

"Sale," together with its grammatical variations and cognate expressions, means any transfer of property in goods by one person to another for cash or deferred payment, or for any other valuable consideration, and includes:

(i) A transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;

(ii) A transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;

(iii) A delivery of goods on hire-purchase or any system of payment by instalments;

(iv) A transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;

(v) A supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration; and

(vi) A supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service is for cash, deferred payment or other valuable consideration.

A sale does not include a mortgage or hypothecation of, or a charge or pledge on, goods.

c. Registration

A single inter-state sale of any amount effected by a dealer attracts tax liability under the CST Act and consequential liability for obtaining a certificate of registration. The application for registration must be made within 30 days from the date on which the first inter-state sale is effected. However, dealers registered under the State Sales Tax Act may obtain registration even without effecting any inter-state sale. Dealers effecting sales in the course of inter-state trade are required to obtain a declaration in Form 'C' from the purchaser of the goods if they are to be able to apply a

concessional rate.

d. Rates of Tax

Rates of tax on sales in the course of inter-state trade or commerce are prescribed by the CST Act, as follows:

	With form "C"	Without form "C"
Goods specified in registration certificate of the registered dealer	2% or local rate, whichever is lower	Local rate
All other sales	—	Local rate

The transfer of goods from one state to another to a person's own place of business is exempt from the levy of tax. A declaration in Form 'F' must be obtained from the branch concerned.

The purchasing dealer is required to obtain these forms from the prescribed authority under his seal and signature. The dealer issuing the forms will keep a record of the forms used by him.

Form 'C' declarations may be issued by dealers registered under the CST Act, in respect only of those goods that are included in the relevant list of their registration certificate under the CST Act, for resale, for packing, for use in the manufacture or processing of goods for sale, for use in mining, for use in the telecom industry, or for use in the generation or distribution of electricity or any other form of power.

The tax is to be collected by the registered dealer who sells goods in the course of inter-state trade or commerce and is paid to the government treasury, along with a return, within such time as may be prescribed by the state government in the local act.

2. Value Added Tax Act

a. General

The Maharashtra Value Added Tax Act, 2002 (MVAT Act) came into force on April 1, 2005. Under the MVAT Act, a dealer is liable to pay tax based on sales or purchases turnover within the state. The term "dealer" includes: a person who buys or sell goods in the state whether for commission, remuneration or otherwise in the course of his business, or in connection with or incidental to, or consequential to his engagement in such business; a broker; a commission agent; an auctioneer; a public charitable trust; a club; an association of persons; a department of the union government or a state government; the Customs department; a port trust; a railway; an insurance or financial corporation; a transport corporation; a local authority; a shipping or construction company; an airline; an advertising agency; and any corporation, company, body or authority that is owned by, constituted by or subject to the administrative control of, the central government, any state government or any local authority.

However, agriculturists, educational institutions and transporters are deemed not to be dealers, subject to their fulfilling specified conditions.

b. Taxability and Registration

Every dealer whose sales turnover and turnover of taxable goods (purchased or sold) exceeds the limits specified in the table below is required to obtain registration under the MVAT Act within 30 days from the date of becoming liable to VAT and will be liable to pay VAT.

The turnover limits for purposes of liability/registration are as follows:

Category of dealer	Total turnover (including both tax-free and taxable sales) Rs.	Turnover of taxable goods purchased or sold Rs.
Importer	1 million	10,000
Others	5 million	10,000

Both conditions have to be satisfied for purposes of liability/registration under the above categories.

Representative rates of tax are as follows:

Nature of goods	Rate of tax
Essential commodities	Nil
Gold, silver, precious stones, pearls, etc.	1%
Declared goods, industrial inputs, and other such specified goods	4%
Molasses and certain tobacco products, including cigars and cigarettes	20%
Foreign liquor, country liquor and liquor imported from foreign countries	Specified rates
Certain petroleum products	Varies from 10% to 33% (in a few cases, a specific duty of Rs.1 per liter is also applicable

All other goods, not covered above (the "Revenue Neutral Rate")	**12.50%**

Every registered dealer is required to file a correct, complete and internally consistent return, in the prescribed form, by the due date.

The tax payable, if any, as per the return, is paid into the government treasury along with the return.

c. Refund and Set-Off

A dealer is entitled to claim a refund of an excess payment made with respect to the period for which a return has been filed, or may carry forward such excess towards adjustment of the tax payable under the return to be filed for any subsequent period.

Refunds may be adjusted in a subsequent month's return. However, refunds may not be adjusted against the liability of the subsequent year.

All registered dealers are entitled to set-off the VAT paid on inputs, such as raw materials, finished goods and packing material, within the State of Maharashtra against their output tax liabilities.

The set-off is subject to the following:

(i) Set-off is allowed only to a registered dealer;

(ii) A valid tax invoice is necessary to claim set-off;

(iii) Proper accounts must be maintained;

(iv) A set-off with respect to eligible goods has to be claimed in the tax period in which the goods were purchased; and

(v) In the case of a newly registered dealer, set-off may be claimed with respect to goods (including capital assets) purchased before the date of registration within the same financial year, provided the goods so purchased are not sold or disposed of before the date of registration.

No set-off is admissible with respect to:

(i) Purchases of motor vehicles (being passenger vehicles);

(ii) Purchases of motor spirit (other than by a dealer in motor spirit);

(iii) Purchases of crude oil used by an oil refinery for refining;

(iv) Purchase of consumables or capital assets by a job worker (labor job) whose only sales are waste or scrap obtained from such labor job;

(v) Purchases made by a dealer holding an Entitlement Certificate under a Package Scheme of Incentives;

(vi) Purchases of goods of an incorporeal or intangible nature other than import licenses, export permits or licenses or quotas, credit of duty entitlement pass books (see C, 7, e, above), SIM cards, software in the hands of a software dealer, or copyright that are resold within 12 months of the date of purchase;

(vii) Purchases by way of works contracts in building construction;

(viii) Purchases of building materials that are not resold but used in the activity of building construction;

(ix) Purchases of Indian made foreign liquor or of country liquor if the dealer has opted for a composition scheme;

(x) Certain purchases of capital assets by a hotelier;

(xi) Purchases of mandap, tarpaulin, pandal, shamiana, decoration, etc. if the dealer has opted for a composition scheme;

(xii) Purchases by a dealer for corresponding sales of food, beverages, bakery items, foreign liquor, or second-hand passenger motor vehicles, where the dealer has opted for a composition scheme; or

(xiii) Purchases of motor spirits by a dealer for corresponding sales at a retail outlet of motor spirits, other than aviation turbine fuel and aviation gasoline.

If, during a tax period (month/quarter/six months), the tax on total sales turnover is less than the amount of input tax credit, the excess credit amount may either be adjusted by the dealer against his tax liability under the CST Act

for the same period or may be carried forward to the next period. The excess credit may be carried forward in this manner through the end of the accounting year. The balance, if any, thereafter may be claimed from the department as a refund.

No tax is payable on the export of goods from India. However, a set-off is available of input tax paid on purchases, from within the state, used in such exports. The VAT paid on purchases (inputs) may be adjusted against the VAT/CST liability or claimed as a refund.

3. Works Contracts Tax

States also levy tax on transactions that are "deemed sales," such as works contracts and leases (see 4, below). A works contract essentially comprises a contract for carrying out work involving the supply of labor and material property that passes during execution of the contract.

The rate of tax on such deemed sales of goods used in the execution of works contract is the same as that prescribed in the relevant Schedules for the respective goods. However, the sale price of such goods has to be determined in accordance with the provisions contained in the MVAT Rules.

Accordingly, the value, at the time of transfer, of goods (whether in the form of goods or some other form) involved in the execution of works contract has to be determined by deducting the following from the value of the entire contract if they are related to the works contract:

(i) Labor and service charges for the execution of the works contract;

(ii) Amounts paid by way of price for sub-contract to sub-contractors, if any;

(iii) Charges for planning or designing and architect's fees;

(iv) Charges for obtaining, on hire or otherwise, machinery and tools for the execution of the works contract;

(v) The cost of consumables, such as water, electricity or fuel used in the execution of the works contract, the property in which is not transferred in the course of the execution of the works contract;

(vi) The cost of establishment of the contractor to the extent it relates to the supply of the labor and services referred to above;

(vii) Other similar expenses that relate to the supply of the labor and services referred to above, where the labor and services are provided subsequent to the transfer of the property concerned; and

(viii) Profit earned by the contractor to the extent it is relates to the supply of the labor and services referred to above.

Where the contractor has not maintained accounts enabling a proper evaluation of the various deductions set out above, or where the Commissioner finds that the accounts maintained by the contractor are not sufficiently clear or intelligible, the contractor or the Commissioner may, in lieu of the deductions set out above, provide a lump-sum deduction as prescribed and determine accordingly the sale price of the goods at the time of the transfer of the property.

Under the Works Contract Composition Scheme, a dealer may, at his option, choose to pay tax at the rate of 5%, in the case of construction contracts (as notified), or 8%, in the case of other contracts, on the total contract value, after deducting from that value any amount paid towards a sub-contract.

However, with respect to a contract on which a dealer has chosen to pay tax by way of composition, the amount of set-off available on inputs will be restricted to 96% of the total amount of set-off for the respective goods in the case of goods used in a construction contract and 64% in the case of goods used in any other contract.

Tax is required to be deducted at source and paid as prescribed.

4. Tax on the Right to Use Goods (Leasing and Hiring)

Previously, the tax on leasing and/or hiring charges was payable under the Maharashtra Tax on Right to Use Goods Act. Currently, all such "deemed sale" transactions are liable to tax under the MVAT Act at the same rate of tax as is prescribed in the Schedules.

The MVAT Act requires certain dealers/persons to have their accounts audited by an accountant within the prescribed period from the end of the year. The audit report is required to be furnished in a prescribed format.

G. Service Tax

Certain services are chargeable to service tax in India under Chapter V of the Finance Act, 1994, as amended by subsequent Finance Acts. The tax is levied on taxable services and the person rendering the services is responsible for collecting the service tax and paying it to the central government.

1. Taxable Services Defined

A wide range of services are "taxable services," including services provided by: a recognized stock exchange and a stockbroker in connection with the sale or purchase of securities listed on a recognized stock exchange; an insurer or reinsurer; an advertising agency; a courier agency; a consulting engineer, including computer hardware engineering services; a customs house agent; a steamer agent; a clearing and forwarding agent; a manpower recruitment agency; a travel agent or tour operator; a *mandap* keeper; a rent-a-cab scheme operator; an architect; an interior decorator; a management or business; a practicing chartered accountant or practicing cost accountant; a practicing company secretary; a real estate agent; a security agency; a credit rating agency; a market research agency; an underwriter; a scientist or technocrat; a photography studio or agency; any person, in relation to the holding of conventions or in relation to online information and database access and/or retrieval; a video production agency; a sound recording studio or agency; a broadcasting agency or organization in relation to broadcasting; [562] an actuary, intermediary or insurance intermediary or insurance agent in relation to insurance auxiliary services concerning general or life insurance business; a banking company or financial institution; a port or any person authorized by a port in relation to port services; an authorized service station; a beauty parlor; a cargo handling agency; a cable operator; a dry cleaner; an event manager; a fashion designer; a health club or fitness center; a storage or warehouse keeper; a person providing business promotion and support services, including customer care services, including the launching of products, customer education programs, seminars, help desk services, enquiry bureaus, etc., but not including computer-enabled services, namely data processing, networking, back office processing, and computer facility management, which are not subject to service tax; a commercial vocational or training institute or coaching center; a commissioning and installation agency; a franchisor in relation to a franchise; an internet café; a person providing management, maintenance and repair services; a technical testing and analysis (excluding health and diagnostic testing) or a technical inspection and certification agency; a foreign exchange broker; an airport or port authority; an aircraft operator; the organizer of a business exhibition; a goods transport agency; a person providing commercial or industrial construction services; the holder of intellectual property rights; an opinion poll agency; an outdoor caterer; a program producer; any person in relation to surveying and exploring for minerals; a *pandal* or *shamiana* contractor; a member of a recognized association or registered association, in relation to a forward contract; a person providing transport for goods other than water, through a pipeline or other conduit, in relation to site formation and clearance, excavation and earthmoving, demolition, and dredging; a person providing services in relation to surveying and mapmaking; a person providing services in relation to cleaning activity; a club or association; a person providing services in relation to packaging activity; a person providing services in relation to mailing and the compilation of mailing lists; a person providing services in relation to the construction of complex; a share transfer agent; a person providing services in relation to automated teller machine operations, or maintenance or management services; a person providing services in relation to the recovery of any sums due to a banking company or financial institution; a person providing services in relation to the sale of space or time for advertising other than the sale of space for advertising in the print media and the sale of time slots by a broadcasting agency or organization; a person receiving sponsorships other than sports events; certain aircraft operators for travel other than in economy class; a person providing services in relation to the transport of goods by rail; a person in relation to business or commerce support services; a person providing services in relation to the auction of property; a person providing services in relation to the managing of public relations; a person in relation to ship management services; a person in relation to internet telecommunication services; a person providing services in relation to transport by cruise ship; a person providing services in relation to credit, debit or charge cards; a person in relation to telecommunication services; a person providing services in relation to the mining of mineral, oil or gas; a person providing services in relation to the renting of real property for use in the course or furtherance of business or commerce; a person providing services in relation to the execution of certain works contracts; a person providing services in relation to the development and supply of content for use in telecommunication services, advertising agency services and online information and database access or retrieval services; a person providing services in relation to asset management, including portfolio management and all forms of fund management other than services provided by a banking company or a financial institution; a person in relation to certain design services; a person providing services in relation to information technology software for use in the course or furtherance of business or commerce; a person providing services in relation to the trading, processing, clearing and settlement of transactions in goods or forward contracts; a person providing services in relation to the supply of tangible goods including machinery, equipment and appliances for use; a person providing services in relation to cosmetic surgery or plastic surgery; a person providing services in relation to the transport of coastal goods, or goods through the national waterway or inland water; and a person providing services in relation to advice, consultancy or assistance in any branch of the law. [563]

---

[562] As long as the radio or television program broadcast is received in India and intended for listening or viewing, as the case may be, by the public, such service will be taxable in India even if the encryption of signals or beaming thereof via satellite may take place outside India.

[563] Service Tax, Sec. 65(105).

---

2. Invoices

Invoices for services rendered must be issued within 14 days from the date of completion of the provision of the services or receipt of payment, whichever is earlier.

3. Payment of Service Tax and Filing of Returns

Service tax is required to be paid by the 5th of the month immediately following the calendar month/quarter in which payments towards the value of taxable services are received. The service tax liability with respect to such payments received by an individual, a proprietorship or a partnership must be paid quarterly to the central government by the 5th of the month immediately following the calendar quarter. The service tax liability of other taxpayers must be paid to the central government by the 5th of the month immediately following the calendar month.

Where a taxable service transaction is entered into with any associated enterprise, any payment received towards the value of the taxable service must include any amount credited to any account, by whatever name called, in the books of account of the person liable to pay the service tax.

E-payment of service tax is mandatory for all taxpayers who paid service tax in excess of Rs.5 million in the preceding financial year or the current financial year.

Small service providers, i.e., those the aggregate value of whose taxable services provided during the preceding financial year did not exceed Rs.1 million have been exempted from service tax up to an aggregate value of taxable services of Rs.1 million in a financial year. The exemption scheme is applicable from April 1, 2005. [564]

---

[564] Notification No. 6/2005 — Service Tax, dated Mar. 1, 2005, as amended by Notification No. 8/2007 — Service Tax, dated Mar. 1, 2007.

A service tax return must be filed by all taxpayers in the prescribed form on a half-yearly basis (April 1 to September 30 and October 1 to March 31) within 25 days of the completion of the respective half year. Returns of service tax also may be filed electronically. Taxpayers may file one consolidated return for each service provided by them.

4. Special Provisions for Nonresident Taxpayers

Services provided from outside India but received in India are subject to service tax in accordance with the provisions of the Taxation of Services (Provided from outside India and received in India) Rules, 2006.

Foreign companies usually fall into the category of nonresident taxpayers. Taxable services provided by a service provider outside India to a recipient in India are chargeable to service tax. The provision of taxable services by a permanent establishment (PE) outside India to a PE in India will be regarded as services provided by one person to another and subject to service tax in India. A nonresident required to pay service tax is exempted from applying for registration provided he has no office in India. However, the person who avails himself of the services provided by the nonresident would have to register, pay service tax and furnish returns.

Taxable services provided from outside India and received in India will not be treated as output services for purposes of the availability of the credit for excise duty paid on any input or service tax paid on any input services. However, where such services are used as inputs for providing any taxable output, the service tax paid on such services may be taken as an input credit. [565] (See further at 6, below.)

---

[565] Para 4.2 of Circular F. No. B1/4/2006-TRU, dated April 19, 2006 (Departmental Clarifications on Provisions relating to Import of Services).

---

5. Rebate on the Export of Services

A rebate may be claimed on the whole of the service tax and cess paid on all taxable services exported to any country other than Nepal or Bhutan, subject to the fulfillment of the following conditions:

(i) The services must be provided to a recipient located outside India, where the services are provided in relation to a business or commerce, or to a recipient located outside India at the time of provision of the services, in other cases;

(ii) The services must be provided from India and used outside India;

(iii) Payment for the services must be received by the service provider in convertible foreign exchange. [566]

---

[566] Export of Service Rules, 2005.

---

6. Credit for Service Tax Paid on Inputs Used in Providing Taxable Services

A rebate (credit) may be claimed of the whole of the duty paid on excisable inputs or the whole of the service tax and cess paid on all taxable input services used in providing taxable services, subject to certain conditions and limitations.

No credit is available if the output service is exempt from service tax.

7. Exemption from Service Tax

Taxable services provided in relation to authorized operations in an SEZ and received by a developer or units in an SEZ, whether or not the taxable services are provided in the SEZ, are exempt from service tax, subject to certain conditions. The exemption is allowed with respect to service tax on services consumed within the SEZ; where services to the SEZ are consumed partly or wholly outside the SEZ, in which case the exemption will be by way of a refund of service tax paid on the taxable services. [567]

---

[567] Notification No. 9/2009 — Service Tax dated March 3, 2009 as amended by Notification no. 15/2009 — Service Tax dated May 20, 2009.

Specified taxable services received by an exporter of goods and used for purposes of the goods exported are exempt from service tax, subject to certain conditions. [568]

---

[568] Notification No. 18/2009 — Service Tax dated July 7, 2009.

---

8. Value of Taxable Services

The value of taxable services is determined by reference to the Service Tax (Determination of Value) Rules, 2006. Specific provisions have been laid down for determining the value of services received in kind and services provided to a related/associated enterprise. "Associated enterprise" is defined in Section 92A of the Income Tax Act, 1961 (ITA) (see VIII, below).

9. Assessment and Other Procedures

The rules provide for the self-assessment of service tax liability by the service provider and list instances in which the Assistant Commissioner or the Deputy Commissioner of Central Excise may be approached and the service tax liability assessed and paid on a provisional basis, subject to the assessment of the final liability.

Provisions have been laid down with respect to the following matters:

(i) The recovery of service tax and the imposition of interest and penalties on service tax providers in the case of specified defaults;

(ii) Refunds of service tax;

(iii) Appeals by a service provider against an order passed by the Assistant Commissioner or the Deputy Commissioner of Central Excise Tax, including an order imposing or levying interest or penalties;

(iv) The scheme of advance ruling in service tax matters. An advance ruling" is a determination of a question of law or fact on specified issues regarding the liability to pay service tax in relation to the service proposed to be provided by the applicant. An application may be made only by a person proposing to undertake a business activity in India and making an application for the same, that is:

- **A nonresident setting up a joint venture in India in collaboration with a nonresident or a resident; or**
- **A resident setting up a joint venture in India in collaboration with a nonresident; or**
- **A wholly-owned subsidiary Indian company, of which the holding company is a foreign company.**

An advance ruling is binding on the applicant and the Commissioner and the subordinate Central Excise authorities.

10. Rate of Service Tax

The rate of service tax is 10%, increased by a 3% education tax (cess).

H. Securities Transaction Tax

Securities transaction tax, as administered by the authorities under the ITA, is levied at the specified rates on the value of securities transacted on a recognized stock exchange in India, as follows:

	Taxable securities transaction	Rate	Payable by

1.	Purchase of an equity share in a company or a unit of an equity-oriented fund, where the transaction is entered into on a recognized stock exchange and the contract for the purchase of the share or unit is settled by the actual delivery or transfer of the share or unit	0.125%	Purchaser
2.	Sale of an equity share in a company or a unit of an equity-oriented fund, where the transaction is entered into on a recognized stock exchange and the contract for the sale of the share or unit is settled by the actual delivery or transfer of the share or unit	0.125%	Seller
3.	Sale of an equity share in a company or a unit of an equity oriented fund, where the transaction is entered into on a recognized stock exchange and the contract for the sale of the share or unit is settled otherwise than by the actual delivery or transfer of the share or unit	0.025%	Seller
4.	Sale of an option in securities	0.017%	Seller
5.	Sale of an option in securities, where the option is exercised	0.125%	Purchaser
6.	Sale of a future in securities	0.017%	Seller
7.	Sale of a unit of an equity-oriented fund to a mutual fund	0.25%	Seller

The securities transaction tax is collected by the stock exchange and remitted to the exchequer.

The securities, on which the tax is levied, include:

(i) Shares, bonds, debentures, etc., and other marketable securities of a like nature, in or of any incorporated company or other body corporate;

(ii) Derivatives;

(iii) Units or other instruments issued by a collective investment scheme to the investors in the scheme;

(iv) Security receipts defined in the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act;

(v) Government securities;

(vi) Other notified instruments; and

(vii) Option contracts, in the case of which the value of the transaction would include the strike price and the premium.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Detailed Analysis

VIII. Transfer Pricing

Any income arising from an international transaction is required to be computed having regard to the arm's length price. The allowance for any expense or interest arising from an international transaction must also be determined having regard to the arm's length price.

Where, in an international transaction, two or more associated enterprises enter into a mutual agreement or arrangement for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of the enterprises, the cost or expense allocated or apportioned to, or contributed by, any such enterprise must be determined having regard to the arm's length price of the benefit, service or facility.

If the application of the arm's length price has the effect of reducing income chargeable to tax or increasing loss, then the income, expense, interest or other allocation or apportionment of expenses need not be calculated at the arm's length price. [569]

---

[569] ITA, Sec. 92.

An associated enterprise in relation to another enterprise is defined to mean an enterprise:

(i) That participates, directly or indirectly, or through one or more intermediaries, in the management, control or capital of the other enterprise; or

(ii) With respect to which one or more persons that participate, directly or indirectly, or through one or more intermediaries, in its management, control or capital, are the same persons that participate, directly or indirectly, or through one or more intermediaries, in the management, control or capital of the other enterprise.

Two enterprises are deemed to be associated enterprises if, at any time during the previous year:

(i) One enterprise holds, directly or indirectly, shares carrying not less than 26% of the voting power in the other enterprise;

(ii) Any person or enterprise holds, directly or indirectly, shares carrying not less than 26% of the voting power in both enterprises;

(iii) A loan advanced by one enterprise to the other enterprise constitutes not less than 51% of the book value of the total assets of the other enterprise;

(iv) One enterprise guarantees not less than 10% of the total borrowing of the other enterprise;

(v) More than half of the board of directors or members of the governing board, or one or more executive directors or executive members of the governing board of one enterprise, are appointed by the other enterprise;

(vi) More than half of the directors or members of the governing board, or one or more of the executive directors or members of the governing board of both enterprises are appointed by the same person or persons;

(vii) The manufacture or processing of goods or articles, or the business carried on by one enterprise is wholly dependent on the use of know-how, patents, copyrights, trademarks, licenses, franchises or any other business or commercial rights of a similar nature, or any data, documentation, drawing or specification relating to any patent, invention, model design, secret formula or process, of which the other enterprise is the owner or with respect to which the other enterprise has exclusive rights;

(viii) 90% or more of the raw materials and consumables required for the manufacture or processing of goods or articles carried out by one enterprise is supplied by the other enterprise or by persons specified by the other enterprise, and the prices and other conditions relating to the supply are influenced by the other enterprise;

(ix) The goods or articles manufactured or processed by one enterprise are sold to the other enterprise or to persons specified by the other enterprise, and the prices and other conditions relating thereto are influenced by the other enterprise;

(x) Where one enterprise is controlled by an individual, the other enterprise is also controlled by that individual or a relative of that individual, or jointly by that individual and a relative of that individual;

(xi) Where one enterprise is controlled by a Hindu Undivided Family (HUF), the other enterprise is controlled by a member of that HUF, or by a relative of a member of that HUF, or jointly by that member and a relative of that member;

(xii) Where one enterprise is a firm, association of persons or body of individuals, the other enterprise holds an interest of not less than 10% in that firm, association of persons or body of individuals; or

(xiii) There exists between the two enterprises, any such relationship of mutual interest as may be prescribed.

The mere fact of participation by one enterprise in the management, control or capital of the other enterprise or the commonality of the control, management or capital of the two enterprises is not sufficient, *per se*, to make both enterprises associated enterprises unless any of the conditions specified above in (i) – (xiii) is met. [570]

---

[570] ITA, Sec. 92A.

The term "international transaction" is defined to mean any of the following types of transaction between two or more associated enterprises, where either or both enterprises are nonresidents:

(i) The purchase, sale or lease of tangible or intangible property;

(ii) The provision of services;

(iii) Any transaction of lending or borrowing money;

(iv) Any transaction having a bearing on the profits, income, losses or assets of those enterprises; and

(v) Any arrangement for the allocation or apportionment of, or contribution to, any cost or expense between the two associated enterprises.

A transaction entered into by an enterprise with a third person other than an associated enterprise is deemed to be a transaction entered into between associated enterprises if:

(i) There is a prior agreement between that person and the associated enterprise in relation to the relevant transaction; or

(ii) The substantive terms of the relevant transaction are determined between that person and the associated enterprise. [571]

---

[571] ITA, Sec. 92B.

Taxpayers are required to use any one of the following specified methods in computing the arm's length price in international transactions: [572]

---

[572] ITA, Sec. 92C.

(i) The comparable uncontrolled price method;

(ii) The resale price method;

(iii) The cost plus method;

(iv) The profit split method;

(v) The transactional net margin method; or

(vi) Any other method that may be prescribed.

The appropriate method to be adopted will depend on the nature/class of the transaction concerned, the class of the associated persons, the functions performed and other factors that may be prescribed. Where more than one price is determined by the most appropriate method, the arm's length price will be taken to be the arithmetical mean of such prices. Further, if the variation between the arm's length price so determined and the price at which the international transaction has actually been undertaken does not exceed 5% of the latter, the price at which the international transaction has actually been undertaken will be deemed to be the arm's length price. [573]

---

[573] ITA, Sec. 92C.

Rules have been prescribed for determining arm's length prices and information and documents to be maintained (see the Worksheets).

Based on information or documents in his possession, the Assessing Officer may make adjustments in computing the income of a taxpayer from international transactions using an arm's length price, if in his opinion: [574]

---

[574] ITA, Sec. 92C.

(i) The price charged in the international transactions is not an arm's length price;

(ii) Information and documents relating to the international transactions have not been maintained by the taxpayer as prescribed;

(iii) The data used in computing the arm's length price is not reliable or correct; or

(iv) The taxpayer has failed to furnish the information and documents called for by the Revenue

authorities.

If an adjustment is made to the taxpayer's income, the benefit of a tax holiday will not be available with respect to the adjusted (enhanced) income, even if the taxpayer is otherwise eligible for a tax holiday with respect to the adjusted income. [575]

---

[575] ITA, Sec. 92C.

The Assessing Officer may, with the previous approval of the Commissioner, refer the computation of the arm's length price in relation to an international transaction to a Transfer Pricing Officer. The Transfer Pricing Officer may request from the taxpayer evidence of the basis on which the taxpayer has computed the arm's length price for the international transaction.

After considering all the evidence produced by the taxpayer, the Transfer Pricing Officer will, by order in writing, determine the arm's length price in relation to the international transaction and send a copy of his order to the Assessing Officer and to the taxpayer.

In such cases, the Assessing Officer is bound to compute the total income of the taxpayer having regard to the arm's length price determined by the Transfer Pricing Officer. [576]

---

[576] ITA, Sec. 92CA.

The determination of an arm's length price under Section 92C or 92CA of the Income Tax Act, 1961 (ITA) will be subject to "safe harbor" rules, to be notified by the Central Board of Direct Taxes (CBDT). "Safe harbor" means circumstances in which the income tax authorities will accept the transfer price declared by the taxpayer. [577]

---

[577] ITA, Sec. 92CB.

Every taxpayer that has entered into an international transaction is required to maintain the prescribed information and documents, and to produce them before the Assessing Officer or the Commissioner (Appeals) in the course of any proceedings. [578]

---

[578] ITA, Sec. 92D.

The information and documents are required to be verified by an accountant and the taxpayer is required to furnish a report in the prescribed form duly signed by the accountant before the specified date. The specified dates are the same as the due dates for furnishing returns of income specified in Section 139 of the ITA. [579]

---

[579] ITA, Sec. 92E.

The term "arm's length price" means a price that is applied or proposed to be applied in transactions between persons other than associated enterprises, in uncontrolled conditions. [580]

---

[580] ITA, Sec. 92F.

An "enterprise" means a person, including a permanent establishment (PE) of a person, that is or has been or is proposed to be engaged in any activity relating to:

(i) The production, storage, supply, distribution, acquisition or control of articles or goods;

(ii) Know-how, patents, copyrights, trademarks, licenses, franchises, or any other business or commercial rights of a similar nature;

(iii) Data documentation, drawing or specification relating to any patent, invention, model design, secret formula or process;

(iv) The provision of services of any kind;

(v) The carrying out of any work in pursuance of a contract;

(vi) Investment or the provision of loans; or

(vii) The business of acquiring, holding, underwriting or dealing in shares, debentures or other securities of any body corporate. [581]

---

[581] ITA, Sec. 92F.

The term "permanent establishment" is defined to include a fixed place of business through which the business of an enterprise is wholly or partly carried on. [582]

---

[582] ITA, Sec. 92F.

The term "transaction" is defined to include an arrangement, understanding or action in concert, whether or not such understanding or action is formal or in writing, or is intended to be enforceable by legal proceeding. [583]

---

[583] ITA, Sec. 92F.

A. General

The constitution of India conferred sovereign powers to levy taxes and to enforce collection and recovery thereto on the state under Article 265 by providing that no taxes are to be levied or collected except by authority of law. The power to levy taxes is conferred on the Union of India with respect to matters falling within its domain in List 1, Schedule VII of the Constitution. The power to levy taxes conferred on the State Legislative falls within the scope of List 2 of Schedule VII. Entry (4) of List 1 under schedule VII to the Constitution of India empowers the Union of India to enter into treaties, agreements and conventions with foreign countries and to implement such treaties, agreements and conventions; Entry (10) of List 1 deals with foreign affairs; and Entry (9) of List 1 of Schedule VII covers diplomats, councils and trade representation. Thus, tax treaties, including agreements for the avoidance of double taxation, fall within the exclusive domain of the central government in view of the Constitutional Authority conferred on it.

The Income Tax Act 1961 (ITA) empowers the government of India to enter into agreements with foreign countries or specified territories outside India for the relief and avoidance of double taxation.

***Note:* "Specified territories" means areas outside India notified as such by the central government. This has been done with a view to bringing within the fold taxation relief and benefits with regard to transactions with nonsovereign jurisdictions.**

With a view to enabling the tax administration to tackle the problem of tax evasion with international ramifications, the ITA also empowers the government to enter into agreements with foreign countries for the exchange of information for the prevention of fiscal evasion or the avoidance of taxes on income, for the investigation of cases involving tax evasion or avoidance, or for the recovery of taxes in foreign countries on a reciprocal basis. [584]

---

[584] ITA, Sec. 90.

Section 9 of the ITA provides for unilateral relief in certain cases and circumstances, as specified therein. According to Section 9, if any person who is resident in India in any previous year proves that, with respect to his income accruing or arising in the previous year outside India he has paid tax in a country with which there is no double taxation agreement, he will be entitled to deduct from his Indian income tax, a sum calculated on such doubly-taxed

income at the Indian rate of tax or the rate of tax of the other country, whichever is lower.

There are specific instructions and also decided rulings and judgments that it make clear that, with respect to matters that are governed both by the ITA and a double taxation agreement, the provisions of the double taxation agreement will prevail.

Note: **The following principles have been laid down by the Andhra Pradesh High Court: [585]**

> **[585]** ***CIT v. Viskhapatnam Port Trust (Andhra Pradesh)*** **144 I.T.R. 146 [1983].**

(i) Although all income arising directly or indirectly through or from any "business connection" in India is deemed to accrue or arise in India, the charging section and the definition of "total income" are expressly made subject to the provisions of the ITA. By implication they are, therefore, subject to the terms of any double taxation agreement entered into by the Government of India with a foreign country. Consequently, the profits of a company are not liable to tax except to the extent permitted by such an agreement.

(ii) The expression "permanent establishment" used in India's double taxation agreements postulates the existence of a fixed place of business of a foreign enterprise in another country.

Note: **Although Section 9 of the ITA deems all income accruing or arising abroad directly or indirectly from any source, business connection, etc. in India to accruing or arise in India, the liability of such income to tax will be eventually determined based on any applicable double taxation agreement pursuant to Section 90 of the ITA. This is because the provisions relating to the charge of income tax and determining the scope of income tax are subject to the other provisions of the ITA, including Section 90 of the ITA. Similarly, in the context of the definition of a royalty under Section 9(1)(vi) of the ITA, it has been held by the Calcutta High Court that the definition of a royalty in a double taxation agreement prevails over the definition of a royalty contained in Explanation 2 to Section 9(1)(vi) of the ITA. [586]**

> **[586]** ***CIT v. Davy Ashmore India Ltd. (Calcutta)*** **190 I.T.R. 626 [1991].**

Note: **There is no merit in the contention that the delegate of a legislative power may not exercise the power of exemption in a fiscal statute. Section 90 of the ITA enables the central government to enter into a double taxation agreement with a foreign government. When the requisite notification has been issued thereunder, the provisions of sub-section (2) of Section 90 spring into operation and an assessee (taxpayer) who is covered by the provisions of the double taxation agreement is entitled to seek benefits under the agreement, even if the provisions of the agreement are inconsistent with the provisions of the ITA. One may not accept the contention that the India-Mauritius tax treaty [587] is *ultra vires* of the central government under Section 90 on account of its susceptibility to "treaty shopping" on behalf of residents of third countries. [588]**

> **[587] Convention Between the Government of the Republic of India and the Government of Mauritius for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital Gains, signed on Aug. 24, 1982 (the "India-Mauritius tax treaty").**
>
> **[588]** ***Vodafone International Holdings B.V. v. Union of India*** **(Bom.) 311 I.T.R. 46 [2008].**

Some double taxation agreements into which India has entered contain nondiscrimination provisions. In this context, it has been made clear that, if a foreign company is taxed at a rate higher than the rate at which domestic companies are taxed, and if the foreign company has not made the prescribed arrangement for the declaration and payment of dividends in India, the levy of tax on the foreign company is not to be regarded as a less favorable charge with respect to the foreign company. [589]

> **[589] ITA, Explanation to Sec. 90.**

B. Unilateral Double Taxation Relief

In the case of tax imposed by a country with which India has no double taxation agreement, the ITA grants unilateral relief to residents of India. The resident concerned must have paid income tax by way of withholding at source or otherwise under the law in force in the other country concerned. Unilateral relief is limited to the extent of the lower of the rate of tax chargeable on the income in India and the rate chargeable in the foreign country and applies to doubly-taxed income received or accrued in India. Accordingly, a person resident in India pays tax in India on his

foreign income only to the extent of the higher rate of tax in India on such income.

The Supreme Court has held [590] that the relief to which a taxpayer is entitled is the amount of tax paid on the foreign income that, by its inclusion in the total income taxable in India, once again bears tax under the ITA. The income that bears the double tax need not be the same income nor need it be income that falls within the identical income category.

---

[590] *K.V.A.L.M. Ramanathan Chettiar v. CIT* (S.C.) 88 I.T.R. 169 [1973].

C. Double Taxation Agreements

1. In General

For a list of India's double taxation agreements, see the Worksheets.

Comprehensive double taxation agreements normally cover income tax, including corporation tax, capital gains tax and wealth tax. Generally, the provisions of India's double taxation agreements override the provisions of Indian income tax laws and, if there is any conflict between an agreement and Indian tax laws, the provisions in the agreement will prevail, except when the Indian tax laws are more beneficial to the taxpayer.

India has also entered into double taxation agreements for the limited purpose of shipping and air transport with some countries. Under these agreements, a resident of one country is exempt from tax in the other with respect to profits from operating ships or aircraft.

By and large, India's tax treaties eliminate double taxation by way of a tax credit method. However, the amount of such credit may not exceed the proportion of tax that the income concerned bears to the entire income chargeable to tax or the tax appropriate to the income derived from sources within the other country. India's treaties, in certain circumstances, may provide for the exemption method under specific articles. Some of India's treaties provide for a tax sparing credit and contain a most favored nation (MFN) clause.

2. India-United States Tax Treaty

An agreement for the avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income was signed by India and the United States in New Delhi on September 12, 1989. [591] The agreement entered into force on December 20, 1990, and is in effect in the United States from January 1, 1991, and in India from April 1, 1991. Under this agreement, business profits of an enterprise of one country are taxable in the other country only if the enterprise maintains a permanent establishment (PE) in that other country.

---

[591] Convention Between the Government of the United States of America and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, signed on Sept. 12, 1989 (the "India-United States tax treaty").

The India-United States tax treaty also provides for the mutual exemption of aircraft and shipping profits of enterprises of the two countries. Dividends, interest, royalties and fees for certain services are taxed in the source country at concessional rates as specified in the agreement. The agreement also provides for tax credits.

It should be noted that a U.S. pension trust whose income is exempt in the United States will not be eligible to claim benefits under the India-United States tax treaty.

***Comment:* The India-United States tax treaty, which was signed after nearly 30 years of negotiations, has not only stimulated the growth of bilateral economic relations between the United States and India, but has also encouraged the flow of new technology in important areas.**

D. Adoption by the Central Government of Agreements Between Specified Associations for Double Taxation Relief

Any specified association in India may enter into an agreement with any specified association outside India for:

(i) Granting relief with respect to income that is taxable in both countries;

(ii) Granting relief with respect to income tax chargeable under Indian laws and tax chargeable under the corresponding tax law of the foreign country;

(iii) The avoidance of double taxation of income under Indian tax laws and the tax laws of the foreign country;

(iv) The exchange of information so as to prevent evasion or avoidance of tax and for helping in the investigation of such evasion or avoidance; or

(v) The recovery of income tax under Indian tax laws and the corresponding laws outside India.

The central government will notify provisions for adopting and implementing such agreements.

A. General

The Reserve Bank of India, to overcome the growing financial difficulties of a number of companies within the industrial sector of the economy, appointed a committee to look into the causes of such "industrial sickness," to assess the depth of the problem and to suggest remedial measures. In accordance with the recommendations made by the committee, The Sick Industrial Companies (Special Provisions) Act, 1985 was enacted and an autonomous tribunal set up for tackling the problems of "sick" industrial companies and for taking suitable steps for their rehabilitation/revival.

To fall within the definition of a "sick industrial company" an industrial company must meet the following criteria: [592]

---

[592] Sick Industrial Companies (Special Provisions) Act, 1985, Sec. 3(1)(o).

---

a. the company must have been registered for not less than five years;

b. the accumulated losses of the company at the end of any financial year must not be less than its entire net worth.

All scheduled industries (see below), except the industry relating to ships and powered vessels, fall within the purview of this Act. The Act contains elaborate provisions for the identification of financial troubles in industrial companies and fixes on the board of directors of the "sick" industrial company the responsibility to report such troubles to the Board for Industrial and Financial Reconstruction (BIFR) which has been set up under this Act for evolving suitable measures to rehabilitate/revive the company. The Act also provides for constitution of an appellate authority consisting of a Chairman and not more than 3 other members for deciding appeals against the orders of the BIFR.

The BIFR Act operates and is implemented through a three-tier system comprising the operating agency, the BIFR and the appellate authority.

The operating agency assists the BIFR in carrying out investigations and in giving directions for the rehabilitation and revival of a company. Generally, the operating agency is a public financial institution, which may have done the project evaluation/implementation, the follow up, and the assessment of the chances of revival. It may, in effect, have to frame a scheme within the guidelines laid down by the BIFR.

The BIFR, a quasi-judicial body, is composed of experts in various fields. The BIFR has a clear legislative mandate to entertain referrals; make due inquiries; assess whether a troubled company could be revived; prepare, frame, and sanction a scheme for its revival; implement the same; and, as a last resort, formulate an opinion for winding up of the troubled company. The BIFR's opinion regarding winding up is virtually mandatory and binding on the High Court, which would then order the winding up.

The appellate authority constituted under the Act is charged essentially with maintaining a check on the BIFR.

The scheme of the Act provides for the initiation of referral and determination by the BIFR of the degree of trouble of a company, and the inquiry, consideration and determination by the BIFR as to whether the troubled industrial company can on its own within a reasonable time make its "net worth positive" or whether the company will need a scheme of revival. If the company fails to make its net worth positive, the BIFR may determine that a scheme of revival is necessary. If the BIFR later determines that the scheme is not practicable or that the financial assistance, concessions and reliefs necessary to make the scheme successful are not forthcoming, it may issue an opinion that it would be just and equitable for the company to be wound up.

B. Scheduled Industries

Scheduled industries are those specified in the First Schedule to the Industries (Development and Regulation) Act, 1951. [593]

[593] ***Id.***, Sec. 3(1)(n).

C. Notification, Inquiries, Schemes and Potential Sickness

It is the responsibility of the board of directors to notify the BIFR if the company has become "sick." The time limit for notification is 60 days from the date of finalization of the duly audited accounts of the company for the financial year at the end of which the company has become a "sick" industrial company. Even before finalization of the accounts, if the board of directors has sufficient reason to form an opinion that the company has become a "sick" industrial company, it is responsible for so notifying the BIFR within 60 days of forming such an opinion. Financial institutions or banks which, by virtue of financial assistance to such a company, have an interest in the company may also notify the BIFR if they have sufficient reason to believe that the industrial company has become a "sick" industrial company.

In all the above cases notification is intended to enable the BIFR to determine which measures to adopt with respect to the company. [594]

[594] ***Id.***, Sec. 15.

The BIFR may make an inquiry to determine whether any industrial company has become a "sick" industrial company in the following instances:

a. on notification from the board of directors; or

b. on receipt of information or based on its own knowledge as to the financial condition of the company.

The BIFR may order an operating agency to inquire into and make a report with respect to matters specified in the report and, if the BIFR deems fit, appoint one or more persons as special directors for safeguarding the interests of the company. [595]

[595] ***Id.***, Sec. 16.

Based on the inquiry, if the BIFR is satisfied that the company has become sick, it can adopt any of the following measures:

a. If in the BIFR's view the company can make its net worth positive within a reasonable time, the BIFR may grant such time to the company. [596]

b. If the above is not possible, the BIFR can direct an operating agency to prepare a scheme with respect to the company for its reconstruction, revival or rehabilitation, or for its proper management. [597]

c. The last measure is to have the company wound up, and for this purpose the BIFR must forward its opinion to that effect to the High Court concerned which, in turn, may order the winding up of the company. [598]

[596] ***Id.***, Sec. 17(1).

[597] ***Id.***, Sec. 17(3).

[598] ***Id.***, Sec. 20.

The BIFR may order an operating agency to prepare within a period of 90 days a scheme with respect to a sick industrial company providing for any one or more of the measures specified in the Act. The BIFR, on the recommendation of the operating agency, may review the scheme and make modifications if necessary, or order a fresh scheme to be prepared. The sanction accorded by the BIFR is conclusive evidence that the requirements of the scheme have been complied with. [599]

---

[599] ***Id.*****, Sec. 18.**

The scheme may provide for financial assistance to the troubled company by way of disbursements, the issue of guarantees, and relief and concessions from the government, or a bank, financial institution or other authority. Consent must be obtained from the government, bank or financial institution for providing financial assistance to the troubled company. Where the consent of these agencies/parties is not forthcoming, the Act permits the BIFR to adopt any other measure in respect of the sick company. [600]

---

[600] ***Id.*****, Sec. 19.**

It is the responsibility of the board of directors of the company to convey to BIFR the fact that the peak net worth of the company has eroded by 50% or more. The maximum net worth during the immediately preceding five taxable years must be taken into account. The report must be submitted to the BIFR within a period of 60 days from the date of finalization of the audited accounts. The board of directors is obliged to report to the members of the company the facts and causes of the erosion. [601]

---

[601] ***Id.*****, Sec. 23.**

Note**: The Act does not specifically mention the action required to be taken by the BIFR on receipt of a report on erosion. In the absence of any specific provision or indication in this behalf, the BIFR seems to be expected to keep a watch on the company and move suo moto when the provisions of Section 16 become applicable. No other action on the part of the BIFR seems to be possible or contemplated.**

The BIFR is a quasi-judicial body and appeals against its decisions or orders can be heard only by the Appellate Tribunal, as provided for in the Act. Accordingly, the jurisdiction of civil courts has been excluded. [602]

---

[602] ***Id.*****, Sec. 26.**

The BIFR's order or decision is subject to the writ jurisdiction of the High Court, and the writ and special leave jurisdiction of the Supreme Court.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

B-101			**INDUSTRIAL POLICY**
	B-101	**Worksheet 1**	**List of Industries for Which Industrial Licensing Is Compulsory and Industries Reserved for the Public Sector.**
	B-201	**Worksheet 2**	**List of Cities with Population of 1 Million and Above According to the 2001 Census.**
B-301			**FOREIGN INVESTMENT AND EXCHANGE MANAGEMENT**
	B-301	**Worksheet 3**	**List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or Items for Which FDI Is Prohibited.**
	B-401	**Worksheet 4**	**Sector Specific Guidelines for Foreign Direct Investment.**
	B-501	**Worksheet 5**	**Guidelines for Calculation of Total Foreign Investment, i.e., Direct and Indirect Foreign Investment in Indian Companies.**
	B-601	**Worksheet 6**	**Form DR — Return to Be Filed by an Indian Company That Has Arranged Issue of GDR/ADR. (Available at http://rbidocs.rbi.org.in/rdocs/content /pdfs/10AFM010709.pdf)**
	B-701	**Worksheet 7**	**Form DR — Quarterly Return to Be Filed by an Indian Company That Has Arranged Issue of GDR/ADR. (Available at http://rbidocs.rbi.org.in/rdocs/Forms**

			/DOCs/form-qgdr.doc)
	B-801	Worksheet 8	Form FC-GPR — Reporting Under FDI Scheme. (Available at http://rbidocs.rbi.org.in/rdocs/Forms /DOCs/40495.doc)
	B-901	Worksheet 9	Form FT RBI — Application for Approval of Foreign Technology Transfer. (Available at http://www.rbi.org.in/upload/ECM/docs /FTRBI.doc)
	B-1001	Worksheet 10	Form FNC 1 — Application to the RBI for Opening a Branch/Liaison/Project Office in India. (Available at http://rbidocs.rbi.org.in/rdocs/Forms/DOCs/ form-fnc1.doc)
	B-1101	Worksheet 11	Form APR — Annual Performance Report. (Available at http://rbidocs.rbi.org.in/rdocs/Forms /DOCs/form-odi.doc)
	B-1201	Worksheet 12	Form ODI — Direct Investment in a Joint Venture (JV)/Wholly Owned Subsidiary Overseas (WOS) Approval/Reporting of Outward Remittances. (Available at http://rbidocs.rbi.org.in/rdocs/Forms /DOCs/form-odi.doc)
	B-1301	Worksheet 13	Form FC/IL SIA — Composite Application to the Government for Foreign Investment and Foreign Technology Agreement Not Qualifying for Automatic Approval and for Grant of Industrial License. (Available at http://siadipp.nic.in/policy/policy/form2.doc)
	B-1401	Worksheet 14	Schedule I to the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004.
	B-1501	Worksheet 15	Guidelines for the Consideration of Foreign Direct Investment (FDI) Proposals by the Foreign Investment Promotion Board (FIPB).
B-1601			BUSINESS ORGANIZATION
	B-1601	Worksheet 16	Exemptions and Privileges for Private Company.
	B-1701	Worksheet 17	Stamp Duty and Fees Payable for Registration of Companies.
	B-1801	Worksheet 18	Memorandum of Association of a Company Limited by Shares.
	B-1901	Worksheet 19	Regulations for Management of a Company Limited by Shares.
	B-2001	Worksheet 20	Rates of Depreciation (Schedule XIV, Companies Act, 1956).
	B-2101	Worksheet 21	List of Accounting Standards.
	B-2201	Worksheet 22	Statement on Matters to Be Included in the Auditor's Report.
	B-2301	Worksheet 23	Schedule XIII — Conditions to Be Fulfilled for Appointment of a Managing or Full Time Director or a Manager Without the Approval of the Central Government.
B-2401			TAXATION
	B-2401	Worksheet 24	Rules for Valuing Perquisites Provided by the Employer for the Purpose of Calculating Income Under the Head "Salaries".
	B-2501	Worksheet 25	Table of Indices for Computation of Long-Term Capital Gains.
	B-2601	Worksheet 26	Depreciation Table.
	B-2701	Worksheet 27	Depreciation Table — Assets of an Undertaking Engaged in Generation or Generation and Distribution of Power.
	B-2801	Worksheet 28	The Eleventh Schedule, Income Tax Act, 1961, List of Articles or Things.
	B-2901	Worksheet 29	The Eighth Schedule, Income Tax Act, 1961, List of Industrially Backward States and Union Territories.
	B-3001	Worksheet 30	The Thirteenth Schedule, Income Tax Act, 1961, List of Articles or Things.
	B-3101	Worksheet 31	The Fourteenth Schedule, Income Tax Act, 1961, List of Articles or Things or Operations.
	B-3201	Worksheet 32	Form ITR-6 — Income Tax Return for Companies. (Available at http://incometaxindia.gov.in/archive /ITR2007-08/I.T.R-6.pdf)

B-3301	Worksheet 33	Form 34C — Application by a Nonresident for Obtaining an Advance Ruling Under Section 245Q(1) of the Income Tax Act, 1961. (Available at http://law.incometaxindia.gov.in/DITTaxmann/IncomeTaxRules/pdf/itr62Form34C.pdf)
B-3401	Worksheet 34	Rules for Determining Arm's Length Price, Information and Documents to Be Furnished Under Transfer Pricing Regulations Pursuant to Sections 92 to 92F of ITA.
B-3501	Worksheet 35	1989 India-United States Income Tax Treaty.
B-3601	Worksheet 36	List of Comprehensive Double Taxation Agreements and Related Protocols Signed by India as of August 1, 2010.

Note: **RBI Master Circular No. 8/2010-11 on External Commercial Borrowings and Trade Credits can be viewed on the RBI website at: http://www.rbi.org.in/scripts/BS_ViewMasterCirculars.aspx?Id=5786&Mode=0**

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 1 Lists of Industries for Which Industrial Licensing Is Compulsory and Industries Reserved for the Public Sector

List of Industries for which Industrial licensing is compulsory (Schedule II of Notification no. 10(43)/91-L.P.)

1. Distillation and brewing of alcoholic drinks.

2. Cigars and tobacco cigarettes, manufactured tobacco substitutes.

3. Electronic Aerospace and defense equipment: all types.

4. Industrial explosives, including detonating fuses, safety fuses, gun powder, nitrocellulose and matches.

5. Hazardous chemicals.

6. Drugs and pharmaceuticals (according to modified Drug Policy issued in September, 1994, as modified in 1999).

List of Industries Reserved for the Public Sector (Schedule I of Notification no. 10(43)/91-L.P.)

1. Atomic Energy.

2. The substances specified in the schedule to the notification of the Government of India in the Department of Atomic Energy number S.O.212(E), dated March 15, 1995.

3. Railway Transport.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 2 List of Cities with Population of 1 Million and Above According to the 2001 Census

Name of City

1. **Greater Mumbai**
2. **Kolkata**
3. **Delhi**
4. **Chennai**
5. **Bangalore**
6. **Hyderabad**
7. **Ahmadabad**
8. **Pune**
9. **Surat**
10. **Kanpur**
11. **Jaipur**
12. **Lucknow**

13. **Nagpur**
14. **Patna**
15. **Indore**
16. **Vadodara**
17. **Bhopal**
18. **Coimbatore**
19. **Ludhiana**
20. **Kochi**
21. **Visakhapatnam**
22. **Agra**
23. **Varanasi**
24. **Madurai**
25. **Meerut**
26. **Nashik**
27. **Jabalpur**
28. **Jamshedpur**
29. **Asansol**
30. **Dhanbad**
31. **Faridabad**
32. **Allahabad**
33. **Amritsar**
34. **Vijayawada**
35. **Rajkot**

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 3 List of Activities or Items for Which Automatic Route of Reserve Bank for Investment from Persons Resident Outside India Is Not Available/List of Activities or Items for Which FDI Is Prohibited

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

1. where provisions of Press Note 1 (2005 Series) issued by the Government of India are attracted. (Cases where the foreign investor has an existing venture or tie-up in India through an investment/technical collaboration/trademark agreement in the same/allied field as the company whose shares are being issued, subject to exceptions).

This restriction does not apply to the transfer of shares:

a) to multinational financial institutions; or

b) where in the existing joint-venture, investment by either of the parties is less than 3%; or

c) where the existing joint venture/collaboration is defunct or sick; or

d) where the transfer is of shares of an Indian company engaged in Information Technology sector or in the mining sector, if the existing joint venture or technology transfer/trademark agreement of the person to whom the shares are to be transferred are also in the Information Technology sector or in the mining sector for same area/mineral.

2. where more than 24% foreign equity is proposed to be inducted for manufacture of items reserved for the Small Scale sector.

B. Sectors prohibited for FDI

1. Retail Trading (except single brand product retailing)

2. Atomic Energy

3. Lottery Business

4. Gambling and Betting

5. Business of chit fund

6. Nidhi Company

7. Trading in Transferable Development Rights (TDRs)

8. Activities/sector not opened to private sector investment

9. Agriculture (excluding Floriculture, Horticulture, Development of seeds, Animal Husbandary, Pisciculture and cultivation of vegetables, mushrooms etc. under controlled conditions and services related to agro and allied sectors) and Plantations (Other than Tea Plantations)

10. Real estate business, or construction of farm houses

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 4 Sector Specific Guidelines for Foreign Direct Investment

Sr. No.	Sector/Activity	FDI Cap/Equity	Entry Route	Other Conditions
I	AGRICULTURE			
1.	Floriculture, horticulture, development of seeds, animal husbandry, pisciculture, aquaculture, cultivation of vegetables and mushrooms under controlled conditions and services related to agro and allied sectors. *Note:* Besides the above, FDI is not allowed in any other agricultural sector/activity.	100%	Automatic	
2.	Tea Sector, including tea plantation *Note:* Besides the above, FDI is not allowed in any other plantation sector/activity.	100%	FIPB	Subject to: i) divestment of 26% equity in favour of Indian partner/Indian public within five years; and ii) prior approval of State Government concerned in case of any change in future land use.
II	INDUSTRY			
II A	MINING			
3.	Mining covering exploration and mining of diamonds and precious stones; gold, silver and minerals.	100%	Automatic	Subject to Mines & Minerals (Development & Regulation) Act, 1957 (www.mines.nic.in) Press Note 18 (1998) and Press Note 1 (2005) are not applicable for setting up 100% owned subsidiaries in so far as the mining sector is concerned, subject to a declaration from the applicant that he has no existing joint venture for the same area and/or the particular mineral.
4.	Coal and Lignite mining for captive consumption by power projects, and iron and steel, cement production and other eligible activities permitted under the Coal Mines (Nationalisation) Act, 1973.	100%	Automatic	Subject to provisions of Coal Mines (Nationalisation) Act, 1973. (www.coal.nic.in)
5.	Mining and mineral separation of titanium bearing minerals and ores, its value addition	100%	FIPB	Subject to sectoral Regulations and the Mines and Minerals (Development & Regulation)

	and integrated activities. ***Note:*** **FDI will not be allowed in mining of "prescribed substances" listed in Government of India notification No. S.O. 61(E) dated 18.1.2006 issued by the Department of Atomic Energy.**			**Act, 1957 and the following conditions —** **i) value addition facilities are set up within India along with transfer of technology;** **ii) disposal of tailings during the mineral separation shall be carried out in accordance with Regulations framed by the Atomic Energy Regulatory Board such as Atomic Energy (Radiation Protection) Rules, 2004 and the Atomic Energy (Safe Disposal of Radioactive Wastes) Rules, 1987.**
	MANUFACTURING			
6.	**Alcohol: Distillation and brewing.**	**100%**	**Automatic**	**Subject to license by appropriate authority.**
7.	**Cigars and Cigarettes: manufacture.**	**100%**	**FIPB**	**Subject to industrial license under the Industries (Development & Regulation) Act, 1951.**
8.	**Coffee and Rubber processing and warehousing.**	**100%**	**Automatic**	**—**
9.	**Defence production**	**26%**	**FIPB**	**Subject to licensing under Industries (Development & Regulation) Act, 1951 and guidelines on FDI in production of arms & ammunition.**
10.	**Hazardous chemicals, viz., hydrocyanic acid and its derivatives; phosgene and its derivatives; and isocyanates and diisocyantes of hydrocarbon.**	**100%**	**Automatic**	**Subject to the industrial license under the Industries (Development & Regulation) Act, 1951 and other sectoral Regulations.**
11.	**Industrial explosives: manufacture**	**100%**	**Automatic**	**Subject to industrial license under the Industries (Development & Regulation) Act, 1951 and Regulations under Explosives Act, 1898.**
12.	**Drugs and Pharmaceuticals including those involving use of recombinant DNA technology.**	**100%**	**Automatic**	**—**
	POWER			
13.	**Power including generation (except Atomic energy); transmission, distribution and power trading.**	**100%**	**Automatic**	**Subject to provisions of the Electricity Act, 2003 (www.powermin.nic.in)**
	SERVICES			
	CIVIL AVIATION SECTOR			
14.	**Airports**			
a.	**Greenfield projects.**	**100%**	**Automatic**	**Subject to sectoral Regulations notified by Ministry of Civil Aviation (www.civilaviation.nic.in)**
b.	**Existing projects.**	**100%**	**FIPB beyond 74%**	**Subject to sectoral Regulations notified by Ministry of Civil Aviation. (www.civilaviation.nic.in)**
15.	**Air Transport Services including Domestic Scheduled Passenger Airlines; Non-Scheduled Airlines; Chartered Airlines; Cargo Airlines; Helicopter and Seaplane Services**			

a.	Scheduled Air Transport Services/Domestic Scheduled Passenger Airline.	FDI: 49% NRIs: 100%	Automatic	Subject to no direct or indirect participation by foreign airlines and Sectoral Regulations. (www.civilaviation.nic.in)
b.	Non-Scheduled Air Transport Service/Non-Scheduled airlines, Chartered airlines, and Cargo airlines.	FDI: 74% NRIs: 100%	Automatic	Subject to no direct or indirect participation by foreign airlines in Non-Scheduled and Chartered airlines. Foreign airlines are allowed to participate in the equity of companies operating Cargo airlines. Also subject to sectoral Regulations. (www.civilaviation.nic.in)
c.	Helicopter Services/Seaplane services requiring DGCA approval.	100%	Automatic	Foreign airlines are allowed to participate in the equity of companies operating Helicopter and seaplane airlines. Also subject to sectoral Regulations. (www.civilaviation.nic.in)
16.	Other services under Civil Aviation Sector			
a.	Ground Handling Services.	FDI: 74% NRIs: 100%	Automatic	Subject to sectoral Regulations and security clearance.
b.	Maintenance and Repair organizations; flying training institutes; and technical training institutions.	100%	Automatic	—
17.	Asset Reconstruction Companies.	49% (only FDI)	FIPB	Where any individual investment exceeds 10% of the equity, provisions of Section 3(3)(f) of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 should be complied with. (www.finmin.nic.in)
18.	Banking: Private sector.	74% (FDI+FII) Within this limit, FII investment not to exceed 49%	Automatic	Subject to guidelines for setting up branches/subsidiaries of foreign banks issued by RBI. (www.rbi.org.in)
19.	Broadcasting			
a.	FM Radio.	FDI+FII investment up to 20%	FIPB	Subject to guidelines notified by Ministry of Information & Broadcasting. (www.mib.nic.in)
b.	Cable network.	49% (FDI+FII)	FIPB	Subject to Cable Television Network Rules (1994), notified by Ministry of Information & Broadcasting. (www.mib.nic.in)
c.	Direct-To-Home	49% (FDI+FII). Within this limit, FDI component not to exceed 20%	FIPB	Subject to guidelines issued by Ministry of Information & Broadcasting. (www.mib.nic.in)
d.	Setting up hardware facilities such as up-linking, HUB, etc.	49% (FDI+FII)	FIPB	Subject to Up-linking Policy notified by Ministry of Information & Broadcasting. (www.mib.nic.in)
e.	Up-linking a News and Current Affairs TV Channel	26% (FDI+FII)	FIPB	Subject to guidelines issued by Ministry of Information & Broadcasting. (www.mib.nic.in)

f.	**Up-linking a Non-news and Current Affairs TV Channel.**	**100%**	**FIPB**	**Subject to the guidelines issued by Ministry of Information & Broadcasting. (www.mib.nic.in)**
20.	**Commodity Exchanges**	**49% (FDI+FII)** **FDI: 26%** **FII: 23%**	**FIPB**	**FII purchases shall be restricted to secondary market only.** **Subject to regulations specified by concerned Regulators.**
21.	**Construction Development projects including: housing, commercial premises, resorts, educational institutions, recreational facilities, city and regional level infrastructure, townships.** ***Note:* FDI is not allowed in Real Estate Business.**	**100%**	**Automatic**	**Subject to conditions notified vide Press Note 2 (2005 Series) including:** **i) Minimum capitalization of US$ 10 million for wholly owned subsidiaries and US$ 5 million for joint venture. The funds would have to be brought within six months of commencement of business of the Company.** **ii) Minimum area to be developed under each project: 10 hectares in case of development of serviced housing plots; and built-up area of 50,000 sq. mts. in case of construction development project; and any of the above in case of a combination project.** ***Note 1:* For investment by NRIs, the conditions mentioned in Press Note 2 (2005) are not applicable.** ***Note 2:* For investment in SEZs, Hotels & Hospitals, conditions mentioned in Press Note 2 (2005) are not applicable.**
22.	**Courier services for carrying packages, parcels and other items which do not come within the ambit of the Indian Post Office Act, 1898.**	**100%**	**FIPB**	**Subject to existing laws and exclusion of activity relating to distribution of letters, which is exclusively reserved for the State. (www.indiapost.gov.in)**
23.	**Infrastructure companies in securities markets namely, Stock Exchanges, Depositories and Clearing Corporations.**	**49% (FDI+FII)** **FDI: 26%** **FII: 23%**	**FIPB**	**FII purchases shall be restricted to secondary market.** **Subject to regulations specified by concerned Regulators.**
24.	**Credit Information Companies (CIC).**	**49% (FDI+FII) Within this limit, FII investment not to exceed 24%**	**FIPB**	**Foreign Investment in CIC will be subject to Credit Information Companies (Regulation) Act, 2005. Subject to regulations specified by concerned Regulators.**
25.	**Industrial Parks both setting up and in established Industrial Parks.**	**100%**	**Automatic**	**Conditions in Press Note 2 (2005 Series) applicable for construction development projects would not apply provided the Industrial Parks meet with the under mentioned conditions:** **i) it would comprise of a minimum of 10 units and no single unit shall occupy more than 50% of the allocable area**

				and; **ii) the minimum percentage of the area to be allocated for industrial activity shall not be less than 66% of the total allocable area.**
26.	**Insurance.**	**26%**	**Automatic**	**Subject to licensing by the Insurance Regulatory & Development Authority. (www.irda.nic.in)**
27.	**Investing companies in infrastructure/services sector (excerpt telecom sector).**	**100%**	**FIPB**	**Where there is a prescribed cap for foreign investment, only the direct investment will be considered for the prescribed cap and foreign investment in an investing company will not be set off against this cap provided the foreign direct investment in such investing company does not exceed 49% and the management of the investing company is with the Indian owners.**
28.	**Non-Banking Finance Companies**			
a. **b.** **c.** **d.** **e.** **f.** **g.** **h.** **i.** **j.** **k.** **l.** **m.** **n.** **o.** **p.** **q.** **r.**	**Merchant banking.** **Underwriting.** **Portfolio Management Services.** **Investment Advisory Services.** **Financial Consultancy.** **Stock Broking.** **Asset Management.** **Venture Capital.** **Custodial Services.** **Factoring.** **Credit Rating Agencies.** **Leasing and Finance.** **Housing Finance.** **Forex Broking.** **Credit card Business.** **Money changing business.** **Micro credit.** **Rural credit.**	**100%**	**Automatic**	**Subject to:** **i) Minimum capitalization norms for fund based NBFCs — US$ 0.5 million to be brought upfront for FDI up to 51%; US$ 5 million to be brought upfront for FDI above 51% and up to 75%; and US$ 50 million out of which US$ 7.5 million to be brought upfront and the balance in 24 month, for FDI beyond 75% and up to 100%.** **ii) Minimum capitalization norms for non-fund based NBFC activities; US$ 0.5 million.** **iii) Foreign investors can set up 100% operating subsidiaries without the condition to disinvest a minimum of 25% of its equity to Indian entities subject to bringing in US$ 50 million without any restriction on number of operating subsidiaries without bringing additional capital.** **iv) Joint venture operating NBFCs that have 75% or less than 75% foreign investment will also be allowed to set up subsidiaries for undertaking other NBFC activities subject to the subsidiaries also complying with the applicable minimum capital inflow.** **v) Compliance with the guidelines of the Reserve Bank.**

29.	**Petroleum & Natural Gas sector**			
a.	**Refining.**	**49% in case of PSUs.** **100% in case of Private companies**	**FIPB (in case of PSUs)** **Automatic (in case of private companies)**	**Subject to Sectoral policy and no divestment or dilution of domestic equity in the existing PSUs. (www.petroleum.nic.in)**
b.	**Other than Refining and including market study and formulation; investment/financing; setting up infrastructure for marketing in Petroleum and Natural Gas sector.**	**100%**	**Automatic**	**Subject to sectoral Regulations issued by Ministry of Petroleum & Natural Gas. (www.petroleum.nic.in)**
30.	**Print Media**			
a.	**Publishing of newspaper and periodicals dealing with news and current affairs.**	**26%**	**FIPB**	**Subject to guidelines notified by Ministry of Information & Broadcasting. (www.mib.nic.in)**
b.	**Publishing of scientific magazines/specialty journals/periodicals.**	**100%**	**FIPB**	**Subject to guidelines issued by Ministry of Information & Broadcasting. (www.mib.nic.in)**
31.	**Telecommunications**			
a.	**Basic and cellular, Unified Access Services, National/International Long Distance, V-Sat, Public Mobile Radio Trunked Services (PMRTS), Global Mobile Personal Communications Services (GMPCS) and other value added telecom services.**	**74% (Including FDI, FII, NRI, FCCBs, ADRs, GDRs, convertible preference shares, and proportionate foreign equity in Indian promoters/Investing Company)**	**Automatic up to 49%.** **FIPB beyond 49%.**	**Subject to guidelines notified in the Press Note 3 (2007 Series) dated April 19, 2007.**
b.	**ISP with gateways, radio-paging, end-to-end bandwidth.**	**74%**	**Automatic up to 49%.** **FIPB beyond 49%.**	**Subject to licensing and security requirements notified by the Department of Telecommunications. (www.dotindia.com)**
c.	**(a) ISP without gateway;** **(b) infrastructure provider providing dark fibre, right of way, duct space, tower (Category I);** **(c) electronic mail and voice mail.**	**100%**	**Automatic up to 49%** **FIPB beyond 49%.**	**Subject to the condition that such companies shall divest 26% of their equity in favour of Indian public in 5 years, if these companies are listed in other parts of the world. Also subject to licensing and security requirements, where required. (www.dotindia.com)**
d.	**Manufacture of telecom Equipments.**	**100%**	**Automatic**	**Subject to sectoral requirements. (www.dotindia.com)**
32.	**Trading**			
a.	**Wholesale/cash and carry trading.**	**100%**	**Automatic**	
b.	**Trading for exports.**	**100%**	**Automatic**	
c.	**Trading of items sourced from small scale sector.**	**100%**	**FIPB**	
d.	**Test marketing of such items for which a company has approval for manufacture.**	**100%**	**FIPB**	**Subject to the condition that the test marketing approval will be for a period of two years and investment in setting up manufacturing facilities commences simultaneously with test marketing.**

e.	Single brand product retailing.	51%	FIPB	Subject to guidelines for FDI in trading issued by Department of Industrial Policy & Promotion vide Press Note 3 (2006 Series) dated February 10, 2006.
33.	Satellites: Establishment and operation.	74%	FIPB	Subject to sectoral guidelines issued by Department of Space/ISRO. (www.isro.org)
34.	Special Economic Zones and Free Trade Warehousing Zones covering setting up of these Zones and setting up units in the Zones.	100%	Automatic	Subject to Special Economic Zones Act, 2005 and the Foreign Trade Policy. (www.sezindia.nic.in)
35.	Drugs and Pharmaceuticals including those involving recombitant DNA technology.	100%	Automatic	—

Note: All the above sector/activities are governed by the respective Press Notes/Releases issued by the Government of India.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 5 Guidelines for Calculation of Total Foreign Investment, i.e., Direct and Indirect Foreign Investment in Indian Companies

1.1 Calculation of Total Foreign Investment i.e. Direct and Indirect Foreign Investment in Indian Companies

1.1.1 Investment in Indian companies can be made both by non-resident as well as resident Indian entities. Any non-resident investment in an Indian company is direct foreign investment. Investment by resident Indian entities could again comprise of both resident and non-resident investment. Thus, such an Indian company would have indirect foreign investment if the Indian investing company has foreign investment in it. The indirect investment can also be a cascading investment i.e. through multi-layered structure.

1.1.2 For the purpose of computation of indirect Foreign investment, Foreign Investment in Indian company shall include all types of foreign investments i.e. FDI; investment by FIIs (holding as on March 31); NRIs; ADRs; GDRs; Foreign Currency Convertible Bonds (FCCB); fully, compulsorily and mandatorily convertible preference shares and fully, compulsorily and mandatorily convertible Debentures regardless of whether the said investments have been made under Schedule 1, 2, 3 and 6 of FEMA (Transfer or Issue of Security by Persons Resident Outside India) Regulations.

1.1.3 Guidelines for calculation of total foreign investment i.e. direct and indirect foreign investment in an Indian company.

(i) Counting the Direct Foreign Investment: All investment directly by a non-resident entity into the Indian company would be counted towards foreign investment.

(ii) Counting of indirect foreign Investment:

(a) The foreign investment through the investing Indian company would not be considered for calculation of the indirect foreign investment in case of Indian companies which are 'owned and controlled' by resident Indian citizens and/or Indian Companies which are owned and controlled by resident Indian citizens.

(b) For cases where condition (a) above is not satisfied or if the investing company is owned or controlled by 'non resident entities', the entire investment by the investing company into the subject Indian Company would be considered as indirect foreign investment, Provided that, as an exception, the indirect foreign investment in only the 100% owned subsidiaries of operating-cum-investing/investing companies, will be limited to the foreign investment in the operating-cum-investing/ investing company. This exception is made since the downstream investment of a 100% owned subsidiary of the holding company is akin to investment made by the holding company and the downstream investment should be a mirror image of the holding company. This exception, however, is strictly for those cases where the entire capital of the downstream subsidy is owned by the holding company.

Illustration

To illustrate, if the indirect foreign investment is being calculated for Company X which has investment through an investing Company Y having foreign investment, the following would be the method of calculation:

(A) Where Company Y has foreign investment less than 50%- Company X would not be taken as having any indirect foreign investment through Company Y.

(B) Where Company Y has foreign investment of say 75% and:

(I) invests 26% in Company X, the entire 26% investment by Company Y would be treated as indirect foreign investment in Company X;

(II) Invests 80% in Company X, the indirect foreign investment in Company X would be taken as 80%;

(III) Where Company X is a wholly owned subsidiary of Company Y (i.e. Company Y owns 100% shares of Company X), then only 75% would be treated as indirect foreign equity and the balance 25% would be treated as resident held equity. The indirect foreign equity in Company X would be computed in the ratio of 75: 25 in the total investment of Company Y in Company X.

(iii) The total foreign investment would be the sum total of direct and indirect foreign investment.

(iv) The above methodology of calculation would apply at every stage of investment in Indian Companies and thus to each and every Indian Company.

(v) Additional conditions:

(a) The full details about the foreign investment including ownership details etc. in Indian company(s) and information about the control of the company(s) would be furnished by the Company(s) to the Government of India at the time of seeking approval.

(b) In any sector/activity, where Government approval is required for foreign investment and in cases where there are any *inter-se* agreements between/amongst share-holders which have an effect on the appointment of the Board of Directors or on the exercise of voting rights or of creating voting rights disproportionate to shareholding or any incidental matter thereof, such agreements will have to be informed to the approving authority. The approving authority will consider such *inter-se* agreements for determining ownership and control when considering the case for granting approval for foreign investment.

(c) In all sectors attracting sectoral caps, the balance equity i.e. beyond the sectoral foreign investment cap, would specifically be beneficially owned by/held with/in the hands of resident Indian citizens and Indian companies, owned and controlled by resident Indian citizens.

(d) In the I&B and Defence sectors where the sectoral cap is less than 49%, the company would need to be 'owned and controlled' by resident Indian citizens and Indian companies, which are owned and controlled by resident Indian citizens.

(A) For this purpose, the equity held by the largest Indian shareholder would have to be at least 51% of the total equity, excluding the equity held by Public Sector Banks and Public Financial Institutions, as defined in Section 4A of the Companies Act, 1956. The term 'largest Indian shareholder', used in this clause, will include any or a combination of the following:

(I) In the case of an individual shareholder,

(aa) The individual shareholder,

(bb) A relative of the shareholder within the meaning of Section 6 of the Companies Act, 1956.

(cc) A company/ group of companies in which the individual shareholder/HUF to which he belongs has management and controlling interest.

(II) In the case of an Indian company,

(aa) The Indian company

(bb) A group of Indian companies under the same management and ownership control.

(B) For the purpose of this Clause, "Indian company" shall be a company which must have a resident Indian or a relative as defined under Section 6 of the Companies Act, 1956/ HUF, either singly or in combination holding at least 51% of the shares.

(C) Provided that, in case of a combination of all or any of the entities mentioned in Sub-Clauses (i) and (ii) of clause 1.1.3(v)(d)(1) above, each of the parties shall have entered into a legally binding agreement to act as a single unit in managing the matters of the applicant company.

(e) If a declaration is made by persons as per section 187C of the Indian Companies Act about a beneficial interest being held by a non resident entity, then even though the investment may be made by a resident Indian citizen, the same shall be counted as foreign investment.

1.1.4 The above mentioned policy and the methodology would be applicable for determining the total foreign investment in all sectors, excepting in sectors where it is governed specifically under any statutes or rules there under. The above methodology of determining direct and indirect foreign investment therefore does not apply to the Insurance Sector which will continue to be governed by the relevant Regulation.

1.1.5 Any foreign investment already made in accordance with the guidelines in existence prior to February 13, 2009 (date of issue of Press Note 2 of 2009) would not require any modification to conform to these guidelines. All other investments, past and future, would come under the ambit of these new guidelines.

Policy for downstream investment by investing companies

1.2.1 The Policy for downstream investment by Indian companies seeks to lay down and clarify about compliance with the Foreign investment norms on entry route, conditionalities and sectoral caps. The 'guiding principle' is that downstream investment by companies 'owned' or 'controlled' by non resident entities would require to follow the

same norms as a direct foreign investment i.e. only as much can be done by way of indirect foreign investment through downstream investment in Para 1.1 as can be done through direct foreign investment and what can be done directly can be done indirectly under same norms.

1.2.2 The Guidelines for calculation of total foreign investment, both direct and indirect in an Indian company, at every stage of investment, including downstream investment, have been detailed in Para 1.1 which enables determination of total foreign investment in any/all Indian Companies.

1.2.3 For the purpose of this chapter,

(i) 'Operating Company' is an Indian company which is undertaking operations in various economic activities and sectors.

(ii) 'Downstream investment' means indirect foreign investment by one Indian company into another Indian company by way of subscription or acquisition in terms of Para 1.1. Para 1.1.3 provides the guidelines for calculation of indirect foreign investment with conditions specified in para 1.1.3 (v)

(iii) 'Foreign Investment' would have the same meaning as in Para 1.1

1.2.4 Guidelines for downstream investment by Investing Indian Companies 'owned or controlled by non resident entities' as per Para 1.1:

(i) The Policy on downstream investment comprises policy for (a) only operating companies (b) operating-cum-investing companies (c) only investing companies as below:

(ii) Only operating companies: Foreign investment in such companies would have to comply with the relevant sectoral conditions on entry route, conditionalities and caps with regard to the sectors in which such companies are operating.

(iii) Operating-cum-investing companies: Foreign investment into such companies would have to comply with the relevant sectoral conditions on entry route, conditionalities and caps with regard to the sectors in which such companies are operating. Further, the subject Indian companies into which downstream investments are made by such companies would have to comply with the relevant sectoral conditions on entry route, conditionalities and caps in regard of the sector in which the subject Indian companies are operating.

(iv) Investing companies: Foreign Investment in Investing Companies will require the prior Government/FIPB approval, regardless of the amount or extent of foreign investment. The Indian companies into which downstream investments are made by such investing companies would have to comply with the relevant sectoral conditions on entry route, conditionalities and caps in regard of the sector in which the subject Indian companies are operating.

1.2.5 For infusion of foreign investment into such companies which do not have any operations and also do not have any downstream investments, Government/FIPB approval would be required, regardless of the amount or extent of foreign investment. Further, as and when such company commences business(s) or makes downstream investment it will have to comply with the relevant sectoral conditions on entry route, conditionalities and caps.

1.2.6. For Operating-cum- investing companies and investing companies (Para 1.2.4) and for companies as per para 1.2.5 above, downstream investments can be made subject to the following conditions:

(i) Such company is to notify SIA, DIPP and FIPB of its downstream investment within 30 days of such investment even if capital instruments have not been allotted along with the modality of investment in new/existing ventures (with/without expansion programme);

(ii) downstream investment by way of induction of foreign equity in an existing Indian Company to be duly supported by a resolution of the Board of Directors supporting the said induction as also a shareholders Agreement if any;

(iii) issue/transfer/pricing/valuation of shares shall be in accordance with applicable SEBI/RBI guidelines;

(iv) For the purpose of downstream investment, the operating cum investing companies and the investing companies would have to bring in requisite funds from abroad and not leverage funds from domestic market for such investments. This would, however, not preclude downstream operating companies to raise debt in the domestic market.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 6 Form DR — Return to Be Filed by an Indian Company That Has Arranged Issue of GDR/ADR

Instructions: The Form should be completed and submitted to the Reserve Bank of India, Foreign Investment Division, Central Office, Mumbai.

1. **Name of the Company**
2. **Address of Registered Office**

3. **Address for Correspondence**
4. **Existing Business (please give the NIC Code of the activity in which the company is predominantly engaged)**
5. **Details of the purpose for which GDRs/ADRs have been raised. If funds are deployed for overseas investment, details thereof**
6. **Name and address of the Depository abroad**
7. **Name and address of the Lead Manager/Investment/ Merchant Banker**
8. **Name and address of the Sub-Managers to the issue**
9. **Name and address of the Indian Custodians**
10. **Details of FIPB approval (please quote the relevant NIC Code if the GDRs/ADRs are being issued under the Automatic Route)**
11. **Whether any overall sectoral cap for foreign investment is applicable. If yes, please give details**
12. **Details of the Equity Capital** — **Before Issue** — **After Issue**
    - **(a) Authorised Capital**
    - **(b) Issued and Paid-up Capital**
    - **(i) Held by persons Resident in India**
    - **(ii) Held by foreign investors other than FIIs/NRIs/PIOs/ OCBs (a list of foreign investors holding more than 10 percent of the paid-up capital and number of shares held by each of them should be furnished)**
    - **(iii) Held by NRIs/PIOs/OCBs**
    - **(iv) Held by FIIs**
    - **Total Equity held by non-residents**
    - **(c) Percentage of equity held by non-residents to total paid-up capital**
13. **Whether issue was on private placement basis. If yes, please give details of the investors and GDRs/ADRs issued to each of them**
14. **Number of GDRs/ADRs issued**
15. **Ratio of GDRs/ADRs to underlying shares**
16. **Issue Related Expenses**
    - **(a) Fee paid/payable to Merchant Bankers/Lead Manager**
    - **(i) Amount (in US$)**
    - **(ii) Amount as percentage to the total issue**
    - **(b) Other expenses**
17. **Whether funds are kept abroad. If yes, name and address of the bank**
18. **Details of the listing arrangement Name of Stock Exchange Date of commencement of trading**
19. **The date on which GDRs/ADRs issue was launched**
20. **Amount raised (in US $)**
21. **Amount repatriated (in US $)**

Certified that all the conditions laid down by Government of India and Reserve Bank of India have been complied with.

Sd/- **Sd/-**

Chartered Accountant **Authorised Signatory of the Company**

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 7 Form DR — Quarterly Return to Be Filed by an Indian Company That Has Arranged Issue of GDR/ADR

Quarterly Return

(to be submitted to the Reserve Bank of India, Foreign Investment Division, Central Office, Mumbai)

1. Name of the Company

2. Address

3. GDR/ADR issue launched on

4. Total No. of GDRs/ADRs issued

5. Total amount raised

6. Total interest earned till end of quarter

7. Issue expenses and commission etc.

8. Amount repatriated

9. Balance kept abroad — Details

(i) Banks Deposits

(ii) Treasury Bills

(iii) Others (please specify)

10. No. of GDRs/ADRs still outstanding

11. Company's share price at the end of the quarter

12. GDRs/ADRs price quoted on overseas stock exchange as at the end of the quarter

Certified that the funds raised through GDRs/ADRs have not been invested in stock market or real estate.

Sd/- **Sd/-**
Chartered Accountant **Authorised Signatory of the Company**

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 8 Form FC-GPR — Reporting Under FDI Scheme

Form FC-GPR

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 9 Form FT RBI — Application for Approval of Foreign Technology Transfer

Form FT RBI

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 10 Form FNC 1 — Application to the RBI for Opening a Branch/Liaison/Project Office in India

General Instructions to Applicants:

The application form only should be completed and submitted to the Chief General Manager, Exchange Control Department (Foreign Investment Division), Reserve Bank of India, Central Office, Mumbai-400001.

B. Documentation:

i) English version of the certificate of incorporation/registration or Memorandum & Articles of Association attested by Indian Embassy/Notary Public in the country of registration.

ii) Latest Audited Balance Sheet of the applicant company/firm.

iii) In case of Project Office documentary evidence that the Project is funded by bilateral or multilateral International Financing Agencies OR the project has been cleared by the concerned regulatory authority OR the Indian company has been granted term loan for the concerned Project by a Financial Institution or a Bank in India.

----

1. i) Full name and address of the applicant company/firm [State whether the applicant is a proprietary concern or partnership firm or limited company or public sector undertaking or any other organisation

(Please specify).

ii) Date and Place of incorporation / registration.

2. Details of capital

i) Paid-up capital divided into shares of each

ii) Free Reserves as per last audited Balance Sheet

3. Brief description of the activities of the applicant.

4. FOR LIAISON / BRANCH OFFICE

i) Value of goods imported from and / or exported to India by the applicant during each of the last three years:

a) Imports from India

b) Exports to India

ii) Particulars of existing arrangements if any, for representing the company in India.

iii) Particulars of the proposed Branch/ Liaison Office

a) Details of the activities/services proposed to be undertaken/ rendered by the office.

b) Place where the office will be located.

5. FOR PROJECT OFFICE

If the office is to be opened on a temporary basis in connection with any specific project or contract to be executed in India by the applicant:

i) Brief description of the project/ contract, including terms of payment / duration, etc.

ii) Place where the office will be located iii) Whether the project office is funded entirely by inward remittances or by any other source specified at B (iii)

6. Any other information which the applicant company wishes to furnish in support of this application.

We hereby declare that:

i) The particulars given above are true and correct to the best of our knowledge and belief;

ii) Our activities in India would be confined to the fields indicated in column 4(iii)(a) or 5(i) above;

iii) If we shift the office to another place, we shall intimate the Reserve Bank of India; and

iv) We will abide by the terms and conditions that may be stipulated by Reserve Bank of India if approval is given.

Place:	**(Signature of Authorised Official of the Applicant Company)**
	Name:
Date:	**Designation:**

Worksheet 11 Form APR — Annual Performance Report

ANNUAL PERFORMANCE REPORT (APR)

(To be submitted certified by Chartered Accountant through the designated AD Category-I bank every year within 3 months of the closing of annual accounts of the JV/WOS as long as the JV/WOS is in existence)

I. Date of APR:

II. Unique Identification Number:

(Please indicate 13 digit Unique Identification number issued by RBI)

III. Changes in capital structure since last reporting

		Amount (new)	% share (new)
	Indian		
	Foreign		

IV. Operational details of the JV/WOS for the last two years

(Amount in 000's FCY)

		Previous Year	Current Year
(i)	Net Profit/(Loss)		
(ii)	Dividend		
(iii)	Net worth		

V. Repatriation from the JV/WOS

Foreign exchange earnings from Joint Ventures (JV) and Wholly Owned Subsidiaries (WOS)

		During the last year ended	Since commencement of business
(i)	Profit		
(ii)	Dividend		
(iii)	Retained Earnings*		
(iv)	Investments into India		
(v)	Others** (Please specify)		

***(Represent part of the profits of the JV/WOS which is retained and reinvested in the JV/WOS).**

****(Royalties, technical know-how fees, consultancy fees, etc.)**

VI. Investment in step down subsidiaries since last reporting

Country
Name of JV/WOS
Amount of Investment
Place:
Date: **(Signature of authorized official)**
Stamp/Seal
Name:
Designation:

(Signature of the Statutory Auditor of the Company)
Name of the firm, Stamp and Registration number

Signature of the Authorised Official of the bank:
Name:
Designation:

Foreign Income Portfolios
Business Operations Abroad (Countries)

Worksheet 12 Form ODI — Direct Investment in a Joint Venture (JV)/Wholly Owned Subsidiary Overseas (WOS) Approval/Reporting of Outward Remittances

FORM ODI
PART I

For office use only

Date of Receipt _____

Inward No. _____

Section A: Details of Indian Party

(I) Investment under (i) Automatic Route (ii) Approval Route

(In case there is more than one Indian party, information may be given on separate sheets for each of the parties)

(II) Name of Indian Party _____

(III) Address of Indian Party _____

City _____ State _____ Pin _____

(IV) Contact Person _____ Designation _____

Tel No. _____ Fax _____

e-mail _____

(V) Status of Indian Party: (Please tick appropriate category)

(1) Public Ltd. Company	**_____**	**(2) Private Limited Company**	**_____**
(3) Public Sector Undertaking	**_____**	**(4) Registered Partnership**	**_____**
(5) Proprietorship	**_____**	**(6) Unregistered Partnership**	**_____**
(7) Trust	**_____**	**(8) Society**	**_____**
(9) Others	**_____**		

(VI) Activity code of Indian Party * _____

*** NIC code at 3-digit level**

[If the Indian Party is engaged in Financial sector or falls under the category of Proprietorship, Unregistered Partnership or Financial sector, the details are to be furnished in Item VII below].

(VII) Financial particulars of the Indian Party for the last 3 years

(Amt. in Rs. 000s)

Particulars	Year 1 31-3-	Year 2 31-3	Year 3 31-3
Foreign exchange earnings (excluding equity exports to JV/WOS)			
Net profit			
Paid-up Capital			
Net worth of (a) Indian Party (b) Group Company@			

@ In terms of Explanation to Regulation 6 (3) of Notification No. FEMA 120/ RB-2004 dated July 7, 2004

(VIII) Particulars of existing Joint Ventures (JV) and Wholly Owned Subsidiaries (WOS) already in operation or under implementation, of the Indian party and its group concerns:

Sr. No.	Name of Indian Party	Unique Identification Number allotted by Reserve Bank

1.		
2.		
3.		

(IX) Whether the proposed investment is (Tick the appropriate box)

(a) New Project (Please furnish the details in Section B)

(b) Existing Project*

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 13 Form FC/IL SIA — Composite Application to the Government for Foreign Investment and Foreign Technology Agreement Not Qualifying for Automatic Approval and for Grant of Industrial License

Form FC/IL SIA

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 14 Schedule I to the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004

Automatic Route for Issue of Foreign Currency Convertible Bonds (FCCBs)

(i) The FCCBs to be issued will have to conform to the Foreign Direct Investment Policy (including Sectoral Cap and Sectors where FDI is permissible) of the Government of India as announced from time to time and the Reserve Bank's Regulations/directions issued from time to time.

(ii) The issue of FCCBs shall be subject to a ceiling of USD 500 million in any one financial year.

(iii) Public issue of FCCBs shall be only through reputed lead managers in the international capital market. In case of private placement, the placement shall be with banks, or with multilateral and bilateral financial institutions, or foreign collaborators, or foreign equity holder having a minimum holding of 5% of the paid up equity capital of the issuing company. Private placement with unrecognized sources is prohibited.

(iv) The maturity of the FCCB shall not be less than 5 years. The call and put option, if any, shall not be exercisable prior to 5 years.

(v) Issue of FCCBs with attached warrants is not permitted.

(vi) The "all in cost" will be on par with those prescribed for External Commercial Borrowing (ECB) schemes specified in the Schedule to Notification No. FEMA 3/2000-RB, dated 3rd May, 2000. The "all in cost" shall include coupon rate, redemption premium, default payments, commitment fees, and fronting fees, if any, but shall not include the issue related expenses such as legal fees, lead managers fees, out of pocket expenses.

(vii) The FCCB proceeds shall not be used for investment in Stock Market, and may be used for such purposes for which ECB proceeds are permitted to be utilized under the ECB schemes.

(viii) FCCBs are allowed for corporate investments in industrial sector, especially infrastructure sector. Funds raised through the mechanism may be parked abroad unless actually required.

(ix) FCCBs for meeting rupee expenditure under automatic route to be hedged unless there is a natural hedge in the form of uncovered foreign exchange receivables, which will be ensured by Authorised Dealers.

(x) Financial intermediaries (viz. a bank, DFI, or NBFC) shall not be allowed access to FCCBs, except those Banks and financial intermediaries that have participated in the Textile or Steel Sector restructuring package of the Government/RBI subject to the limit of their investment in the package.

(xi) Banks, FIs, NBFCs shall not provide guarantee/letter of comfort etc. for the FCCB issue.

(xii) The issue related expenses shall not exceed 4% of issue size and in case of private placement, shall not exceed 2% of the issue size.

(xiii) The issuing entity shall, within 30 days from the date of completion of the issue, furnish a report to the concerned Regional Office of the Reserve Bank of India through a designated branch of an Authorized Dealer giving

the details and documents as under:

(a) The total amount of the FCCBs issued,

(b) Names of the investors resident outside India and number of FCCBs issued to each of them.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 15 Guidelines for the Consideration of Foreign Direct Investment (FDI) Proposals by the Foreign Investment Promotion Board (FIPB)

1.1 GUIDELINES FOR THE CONSIDERATION OF FOREIGN DIRECT INVESTMENT (FDI) PROPOSALS BY THE FOREIGN INVESTMENT PROMOTION BOARD (FIPB)

1.1.1 The following guidelines are laid down to enable the FIPB to consider the proposals for FDI and formulate its recommendations.

1.1.2 All applications should be put up before the FIPB by its Secretariat within 15 days and it should be ensured that comments of the administrative ministries are placed before the Board either prior to/or in the meeting of the Board.

1.1.3 Proposals should be considered by the Board keeping in view the time frame of thirty (30) days for communicating Government decision.

1.1.4 In cases in which either the proposal is not cleared or further information is required in order to obviate delays presentation by applicant in the meeting of the FIPB should be resorted to.

1.1.5 While considering cases and making recommendations, FIPB should keep in mind the sectoral requirements and the sectoral policies vis-à-vis the proposal(s).

1.1.6 FIPB would consider each proposal in its totality.

1.1.7 The Board should examine the following while considering proposals submitted to it for consideration.

(i) Whether the items of activity involve industrial licence or not and if so the considerations for grant of industrial licence must be gone into.

(ii) Whether the proposal involves any export projection and if so the items of export and the projected destinations.

(iii) Whether the proposal has any strategic or defence related considerations.

1.1.8 While considering proposals the following may be prioritised.

(i) Items falling in infrastructure sector.

(ii) Items which have an export potential.

(iii) Items which have large scale employment potential and especially for rural people.

(iv) Items which have a direct or backward linkage with agro business/farm sector.

(v) Items which have greater social relevance such as hospitals, human resource development, life saving drugs and equipment.

(vi) Proposals which result in induction of technology or infusion of capital.

1.1.9 The following should be especially considered during the scrutiny and consideration of proposals.

(i) The extent of foreign equity proposed to be held (keeping in view sectoral caps if any

(ii) Extent of equity from the point of view whether the proposed project would amount to a holding company/wholly owned subsidiary/a company with dominant foreign investment (i.e. 76% or more) joint venture.

(iii) Whether the proposed foreign equity is for setting up a new project (joint venture or otherwise) or whether it is for enlargement of foreign/NRI equity or whether it is for fresh induction of foreign equity/NRI equity in an existing Indian company.

(iv) In the case of fresh induction offerings/NRI equity and/or in cases of enlargement of foreign/NRI equity, in existing Indian companies whether there is a resolution of the Board of Directors supporting the said induction/enlargement of foreign/NRI equity and whether there is a shareholders agreement or not.

(v) In the case of induction of fresh equity in the existing Indian companies and/or enlargement of foreign equity in existing Indian companies, the reason why the proposal has been made and the modality for induction/enhancement (i.e. whether by increase of paid up capital/authorized capital, transfer of shares (hostile or otherwise) whether by rights issue, or by what modality.

(vi) Issue/transfer/pricing of shares will be as per SEBI/RBI guidelines.

(vii) Whether the activity is an industrial or a service activity or a combination of both.

(viii) Whether the items of activity involves any restriction by way of reservation for the Micro & Small

Enterprises sector.

(ix) Whether there are any sectoral restrictions on the activity.

(x) Whether the proposal involves import of items which are either hazardous, banned or detrimental to environment (e.g. import of plastic scrap or recycled plastics).

1.1.10 No condition specific to the letter of approval issued to a foreign investor would be changed or additional condition imposed subsequent to the issue of a letter of approval. This would not prohibit changes in general policies and, regulations applicable to the industrial sector.

1.2 APPROVAL LEVELS FOR CASES UNDER GOVERNMENT ROUTE

1.2.1 The following approval levels shall operate for proposals involving FDI under the Government route i.e. requiring prior Government approval:

(i) The Minister of Finance who is in-charge of FIPB would consider the recommendations of FIPB on proposals with total foreign equity inflow of and below Rs.1200 crore.

(ii) The recommendations of FIPB on proposals with total foreign equity inflow of more than Rs.1200 crore would be placed for consideration of CCEA. The FIPB Secretariat in DEA will process the recommendations of FIPB to obtain the approval of Minister of Finance and CCEA.

(iii) The CCEA would also consider the proposals which may be referred to it by the FIPB/ the Minister of Finance (in-charge of FIPB).

1.3 CASES WHICH DO NOT REQUIRE FRESH APPROVAL

1.3.1 Companies may not require fresh prior approval of the Government i.e. Minister in-charge of FIPB/CCEA for bringing in additional foreign investment into the same entity, in the following cases:

(i) Cases of entities whose activities had earlier required prior approval of FIPB/CCFI/CCEA and who had, accordingly, earlier obtained prior approval of FIPB/CCFI/CCEA for their initial foreign investment but subsequently such activities/sectors have been placed under automatic route;

(ii) Cases of entities whose activities had sectoral caps earlier and who had, accordingly, earlier obtained prior approval of FIPB/CCFI/CCEA for their initial foreign investment but subsequently such caps were removed/increased and the activities placed under the automatic route; provided that such additional investment along with the initial/original investment does not exceed the sectoral caps; and

(iii) The cases of additional foreign investment into the same entity where prior approval of FIPB/CCFI/CCEA had been obtained earlier for the initial/original foreign investment due to requirements of Press Note 18/1998 or Press Note 1 of 2005 and prior approval of the Government under the FDI policy is not required for any other reason/purpose.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 16 Exemptions and Privileges for Private Company[1]

Section[2]	Nature of exemptions/privileges
70	A statement in lieu of a prospectus need not be delivered to the Registrar before allotting shares.[3]
77	Financial assistance can be given for the purchase of or subscription for a company's own shares or shares in its holding company.
8	Further shares can be issued without passing a special resolution or obtaining the central government's approval and without necessarily offering the same to existing shareholders.[3]
85 to 90	Provisions as to kinds of share capital (Sec. 85), further issue of shares with disproportionate rights (Sec. 88), and termination of disproportionate excessive rights (Sec. 89).
111A	Appeal against refusal to register a transfer or transmission of shares.
149	Business can be commenced immediately on incorporation without obtaining a certificate of commencement from the Registrar.[3]
165	Holding statutory meeting and forwarding copy of the statutory report to members or to Registrar of Companies.
170 to 186	Length of notice for calling general meeting, contents and manner of service of notices, explanatory statements, quorum for meeting, chairman of meeting, restrictions of voting rights etc.
192A	Passing of resolution by Postal Ballot.

198	Any amount of managerial remuneration can be paid and is not restricted to any particular proportion of net profits.
204	A private company can appoint a firm or body corporate to an office or position of profit under the company.
255	A proportion of directors need not retire every year.
257	Giving of 14 days notice by a new candidate for office of directorship is not necessary in case of private company.
259	The central government's sanction is not required to effect an increase in the number of directors beyond 12 or the number fixed by the articles of association.
263	In passing a resolution for the election of directors, all directors can be appointed by a single resolution.
264	Consent to act as director need not be filed with Registrar.
266	Restriction on appointment or advertisement of director before obtaining his or her consent.
268	The central government's sanction is not required to modify any provision relating to the appointment of managing, full-time or nonrotational directors.
269	The central government's approval is not required for the appointment of a managing or full-time director or manager.
273	Directors of a private company need not possess any share qualifications, in terms of section 270.
274(1)(g)	Default in repayment of deposit or payment of interest will not disqualify a director of a private company.
275 to 278	Restrictive provisions regarding the total number of directorships which any person may hold do not apply to directorships held in a private company, that is not a subsidiary of a public company.
Section	Nature of exemptions/privileges
292A	Provisions with regard to formation of audit committee are not applicable to private companies.
293	Certain restrictions on the powers of a Board of Directors do not apply.
295	The prohibition against loans to directors does not apply.
300	The prohibition against participation in board meetings by an interested director does not apply to a private company that is neither a subsidiary nor a holding company of a public company.
303	The dates of birth of directors need not be entered in the register of directors.
309	There is no restriction on the remuneration payable to directors.
310	A change in the remuneration of directors does not require government's approval.
311	An increase in the remuneration that is not "sitting fees" (i.e. fees for attending meetings of the Board of Directors) beyond the limit specified on the appointment or reappointment of directors does not require central government approval.
316 & 317	There is no restriction on the appointment of a managing director.
372A	No restrictions on giving loans or guarantees to other companies or making investments in the shares of other companies.
409	The central government cannot exercise its power to prevent a change in Board of Directors that is likely to affect the company prejudicially.
416	A person can enter into a contract on behalf of a company as undisclosed principal and need not give notice to the other directors.

[1] Not being a subsidiary of a public company.

[2] Companies Act, 1956, as amended.

[3] Exemption/privilege under this section is also available to a private company which is a subsidiary of a public company.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 17 Stamp Duty and Fees Payable for Registration of Companies

Filing fees to be deposited with Registrar of Companies	Stamp duty payable in Maharastra State on

Nominal Capital Rupees	Memorandum of Association Rupees	Articles of Association and Forms Rupees	Memorandum of Association Rupees	Articles of Association Rupees
50,000	4,000	100	200	1,000
100,000	4,000	200	200	1,000
200,000	7,000	200	200	1,000
500,000	16,000	300	200	1,000
1 million	26,000	300	200	2,000
1.5 million	36,000	300	200	3,000
2.5 million	56,000	500	200	5,000
5 million	106,000	500	200	10,000
7.5 million	131,000	500	200	15,000
10 million	156,000	500	200	20,000
12.5 million	168,500	500	200	25,000
15 million	181,000	500	200	30,000
17.5 million	193,500	500	200	35,000
20 million	206,000	500	200	40,000
25 million	231,000	500	200	50,000
30 million	256,000	500	200	60,000
40 million	306,000	500	200	80,000
50 million	356,000	500	200	100,000
75 million	481,000	500	200	150,000
100 million	606,000	500	200	200,000
200 million	1,106,000	500	200	400,000
300 million	1,606,000	500	200	600,000
400 million	2,106,000	500	200	800,000
500 million	2,606,000	500	200	1,000,000
750 million	3,856,000	500	200	1,500,000
1000 million	5,106,000	500	200	2,000,000

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 18 Memorandum of Association of a Company Limited by Shares

(Schedule I — Table B *)

* **Companies Act, 1956, as amended.**

1st — The name of the company is "The Eastern Steam Packet Company Limited."

2nd — The registered office of the company will be situated in the State of Maharashtra.

3rd — (a) The main objects to be pursued by the company on its incorporation are "the acquisition, construction, building, setting up and provision of establishments for repairing ships or boats, for the training of personnel required for the running of ships or boats and the doing of all such other things as are conducive to the attainment of the foregoing main objects."

(b) The objects incidental or ancillary to the attainment of the above main objects are "the acquisition, construction, building, setting up and provision of establishments for repairing ships or boats, for the training of personnel required for the running of ships or boats and the doing of all such other things as are conductive to the attainment of the foregoing main objects."

(c) The other objects for which the company is established are "carrying on the business of carriers by land and air and the running of hotels for tourists."

4th — The liability of the members is limited.

5th — The share capital of the company is five hundred thousand rupees, divided into fifty thousand shares of hundred rupees each. We, the several persons whose names and addresses are subscribed, are desirous of being formed into a company in pursuance of this memorandum of association, and we respectively agree to take the number of shares in the capital of the company set opposite our respective names.

Names, addresses, descriptions, occupations of subscriber		Number of shares taken by each subscriber	
1.	A.B.of	Merchant	200
2.	C.B.of	Merchant	25
3.	E.F.of	Merchant	30
4.	G.H.of	Merchant	40
5.	I.J.of	Merchant	15
6.	K.L.of	Merchant	5
7.	M.N.of	Merchant	10
		Total shares taken	325

Dated the ___ day of _____ 20___ Witness to the above X.Y. of _____

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 19 Regulations for Management of a Company Limited by Shares

(Schedule I — Table A) *

* ***See*** **sections 2(2), 14, 28(1), 29 and 223, Companies Act, 1956, as amended.**

Interpretation

1.(1) In these regulations —

(a) "the Act" means the Companies Act, 1956,

(b) "the seal" means the common seal of the company.

(2) Unless the context otherwise requires, words or expressions contained in these regulations shall bear the same meaning as in the Act or any statutory modification thereof in force at the date at which these regulations become binding on the company.

Share capital and variation of rights

2. Subject to the provisions of section 80, any preference shares may, with the sanction of an ordinary resolution, be issued on the terms they are, or at the option of the company are liable, to be redeemed on such terms and in such manner as the company before the issue of the shares may, by special resolution, determine.

3.(1) If at any time the share capital is divided into different classes of shares, the rights attached to any class (unless otherwise provided by the terms of issue of shares of that class) may, subject to the provisions of sections 106 and 107 and whether or not the company is being wound up, be varied with the consent in writing of the holders of three-fourths of the issued shares of that class or with the sanction of a special resolution passed at the separate meeting of the holders of the shares of that class.

(2) To every such separate meeting, the provisions of these regulations relating to general meetings shall *mutatis mutandis* apply, but so that the necessary quorum shall be two persons at least holding or representing by proxy one-third of the issued shares of the class in question.

4. The rights conferred upon the holders of the shares of any class issued with preferred or other rights shall not, unless otherwise expressly provided by the terms of issue of the shares of that class, be deemed to be varied by the creation or issue of further shares ranking *pari passu* therewith.

5.(1) The company may exercise the powers of paying commissions conferred by section 76, provided that the rate percent or the amount of the commission paid or agreed to be paid shall be disclosed in the manner required by that section.

(2) The rate of the commission shall not exceed the rate of five percent of the price at which the shares in respect whereof the same is paid are issued or an amount equal to five percent of such price, as the case may be.

(3) The commission may be satisfied by the payment of cash or the allotment of fully or partly paid shares or partly in the one way and partly in the other.

(4) The company may also, on any issue of shares, pay such brokerage as may be lawful.

6. Except as required by law, no person shall be recognised by the company as holding any share upon any trust and the company shall not be bound by or be compelled in any way to recognize (even when having notice thereof) any equitable, contingent, future or partial interest in any share or any interest in any fractional part of a share or (except only as by these regulations or by law otherwise provided) any other rights in respect of any share except an absolute

right to the entirety thereof in the registered holder.

7.(1) Every person whose name is entered as a member in the register of members shall be entitled to receive within three months after allotment or within two months after the application for the registration of transfer (or within such other period as the conditions of issue shall provide) —

(a) one certificate for all his shares without payment; or

(b) several certificates, each for one or more of his shares, upon payment of one rupee for every certificate after the first.

(2) Every certificate shall be under the seal and shall specify the shares to which it relates and the amount paid up thereon.

(3) In respect of any share or shares held jointly by several persons, the company shall not be bound to issue more than one certificate and delivery of a certificate for a share to one of several joint holders shall be sufficient delivery to all such holders.

8. If a share certificate is defaced, lost or destroyed, it may be renewed on payment of such fee, if any, not exceeding two rupees and on such terms, if any, as to evidence and indemnity and the payment of out-of-pocket expenses incurred by the company in investigating evidence, as the directors think fit.

Lien

9.(1) The company shall have a first and paramount lien —

(a) on every share (not being a fully-paid share), for all moneys (whether presently payable or not) called or payable at a fixed time, in respect of that share; and

(b) on all shares (not being fully-paid shares) standing registered in the name of a single person, for all moneys presently payable by him or his estate to the company:

Provided that the Board of Directors may at any time declare any share to be wholly or in part exempt from the provisions of this clause.

(2) The company's lien, if any, on a share shall extend to all dividends payable thereon.

10. The company may sell, in such manner as the Board thinks fit, any shares on which the company has a lien:

Provided that no sale shall be made —

(a) unless a sum in respect of which the lien exists is presently payable, or

(b) until the expiration of fourteen days after a notice in writing stating and demanding payment of such part of the amount in respect of which the lien exists as is presently payable, has been given to the registered holder for the time being of the share or the person entitled thereto by reason of his death or insolvency.

11.(1) To give effect to any such sale, the Board may authorise some person to transfer the shares sold to the purchaser thereof.

(2) The purchaser shall be registered as the holder of the shares comprised in any such transfer.

(3) The purchaser shall not be bound to see to the application of the purchase money, nor shall his title to the shares be affected by any irregularity or invalidity in the proceedings in reference to the sale.

12.(1) The proceeds of the sale shall be received by the company and applied in payment of such part of the amount in respect of which the lien exists as is presently payable.

(2) The residue, if any, shall, subject to a like lien for sums not presently payable as existed upon the shares before the sale, be paid to the person entitled to the shares at the date of the sale.

Call on shares

13.(1) The Board may, from time to time, make calls upon the members in respect to any moneys unpaid on their shares (whether on account of the nominal value of the shares or by way of premium) and not by the conditions of allotment thereof made payable at fixed times:

Provided that no call shall exceed one-fourth of the nominal value of the share or be payable at less than one month from the date fixed for the payment of the last preceding call.

(2) Each member shall, subject to receiving at least fourteen days' notice specifying the time or times and place of payment, pay to the company, at the time or times and place so specified, the amount called on his shares.

(3) A call may be revoked or postponed at the discretion of the Board.

14. A call shall be deemed to have been made at the time when the resolution of the Board authorizing the call was passed and may be required to be paid by installments

15. The joint holders of a share shall be jointly and severally liable to pay all calls in respect thereof.

16.(1) If a sum called in respect of a share is not paid before or on the day appointed for payment thereof, the person

from whom the sum is due shall pay interest thereof from the day appointed for payment thereof to the time of actual payment at five percent per annum or at such lower rate, if any, as the Board may determine.

(2) The Board shall be at liberty to waive payment of any such interest wholly or in part.

17.(1) Any sum which by the terms of issue of a share becomes payable on allotment or at any fixed date, whether on account of the nominal value of the share or by way of premium shall, for the purposes of these regulations, be deemed to be a call duly made and payable on the date on which by the terms of issue such sum becomes payable.

(2) In case of non-payment of such sum, all the relevant provisions of these regulations as to payment of interest and expenses, forfeiture or otherwise shall apply as if such sum had become payable by virtue of a call duly made and notified.

18. The Board —

(a) may, if it thinks fit, receive from any member willing to advance the same, all or any part of the moneys uncalled and unpaid upon any shares held by him; and

(b) upon all or any of the moneys so advanced, may (until the same would, but for such advance, become presently payable) pay interest at such rate not exceeding, unless the company in general meeting shall otherwise direct, six percent per annum, as may be agreed upon between the Board and the member paying the sum in advance.

Transfer of shares

19.(1) The instrument of transfer of any share in the company shall be executed by or on behalf of both the transferor and transferee.

(2) The transferor shall be deemed to remain a holder of the share until the name of the transferee is entered in the register of members in respect thereof.

20. Subject to the provisions of section 108, the shares in the company shall be transferred in form No. 7B.

21. The Board may, subject to the right of appeal conferred by Section 111, decline to register —

(a) the transfer of a share, not being a fully-paid share, to a person of whom they do not approve; or (b) any transfer of shares on which the company has a lien.

22. The Board may also decline to recognise any instrument of transfer unless:

(a) a fee of two rupees is paid to the company in respect thereof;

(b) the instrument of transfer is accompanied by the certificate of the share to which it relates, and such other evidence as the Board may reasonably require to show the right of the transferor to make the transfer; and

(c) the instrument of transfer is in respect of only one class of shares.

23. Subject to the provisions of section 154, the registration of transfers may be suspended at such times and for such periods as the Board may from time to time determine:

Provided that such registration shall not be suspended for more than thirty days at any one time or for more than forty-five days in the aggregate in any year.

24. The company shall be entitled to charge a fee not exceeding two rupees on the registration of every probate, letters of administration, certificate of death or marriage, power of attorney or other instrument.

Transmission of shares

25.(1) On the death of a member, the survivor or survivors where the member was a joint holder and his legal representatives where he was a sole holder, shall be the only person recognized by the company as having any title to his interest in the shares.

(2) Nothing in clause (1) shall release the estate of a deceased joint holder from any liability in respect of any share which had been jointly held by him with other persons.

26.(1) Any person becoming entitled to a share in consequence of the death or insolvency of a member may, upon such evidence being produced as may from time to time properly be required by the Board and subject as hereinafter provided, elect, either —

(a) to be registered himself as holder of the share; or

(b) to make such transfer of the share as the deceased or insolvent member could have made.

(2) The Board shall, in either case, have the same right to decline or suspend registration as it would have had if the deceased or insolvent member had transferred the share before his death or insolvency.

27.(1) If the person so becoming entitled shall elect to be registered as holder of the share himself, he shall deliver or send to the company a notice in writing signed by him stating that he so elects.

(2) If the person aforesaid shall elect to transfer the share, he shall testify his election by executing a transfer of the share.

(3) All the limitations, restrictions and provisions of these regulations relating to the right to transfer and the registration of transfers of shares shall be applicable to any such notice or transfer as aforesaid as if the death or insolvency of the member had not occurred and the notice or transfer were a transfer signed by that member.

28. A person becoming entitled to a share by reason of the death or insolvency of the holder shall be entitled to the same dividends and other advantages to which he would be entitled if he were the registered holder of the share, except that he shall not, before being registered as a member in respect of the share, be entitled in respect of it to exercise any right conferred by membership in relation to meetings of the company:

Provided that the Board may, at any time, give notice requiring any such person to elect either to be registered himself or to transfer the share and if the notice is not complied with within ninety days, the Board may thereafter withhold payment of all dividends, bonuses or other moneys payable in respect of the share, until the requirements of the notice have been complied with.

Forfeiture of shares

29. If a member fails to pay any call or installment of a call, on the day appointed for payment thereof, the Board may, at any time thereafter during such time as any part of the call or installment remains unpaid, serve a notice on him requiring payment of so much of the call or installment as is unpaid, together with any interest which may have accrued.

30. The notice aforesaid shall —

(a) name a further day (not being earlier than the expiry of fourteen days from the date of service of the notice) on or before which the payment required by the notice is to be made; and

(b) state that, in the event of non-payment on or before the day so named, the shares in respect of which the call was made will be liable to be forfeited.

31. If the requirements of any such notice as aforesaid are not complied with, any share in respect of which the notice has been given may, at any time thereafter, before the payment required by the notice has been made, be forfeited by a resolution of the Board to that effect.

32.(1) A forfeited share may be sold or otherwise disposed of on such terms and in such manner as the Board thinks fit.

(2) At any time before a sale or disposal as aforesaid, the Board may cancel the forfeiture on such terms as it thinks fit.

33.(1) A person whose shares have been forfeited shall cease to be a member in respect of the forfeited shares, but shall, notwithstanding the forfeiture, remain liable to pay to the company all moneys which, at the date of forfeiture, were presently payable by him to the company in respect of the shares.

(2) The liability of such person shall cease if and when the company shall have received payment in full of all such moneys in respect of the shares.

34.(1) A duly verified declaration in writing that the declarant is a director, the manager or the secretary, of the company and that a share in the company has been duly forfeited on a date stated in the declaration, shall be conclusive evidence of the facts therein stated as against all persons claiming to be entitled to the share.

(2) The company may receive the consideration, if any, given for the share on any sale or disposal thereof and may execute a transfer of the share in favour of the person to whom the share is sold or disposed of.

(3) The transferee shall thereupon be registered as the holder of the share.

(4) The transferee shall not be bound to see to the application of the purchase money, if any, nor shall his title to the share be affected by any irregularity or invalidity in the proceedings in reference to the forfeiture, sale or disposal of the share.

35. The provisions of these regulations as to forfeiture shall apply in the case of non-payment of any sum which, by the terms of issue of a share, becomes payable at a fixed time, whether on account of the nominal value of the share or by way of premium, as if the same had been payable by virtue of a call duly made and notified.

Conversion of shares into stock

36. The company may, by ordinary resolution, —

(a) convert any paid-up shares into stock; and

(b) reconvert any stock into paid-up shares of any denomination.

37. The holders of stock may transfer the same or any part thereof in the same manner as, and subject to the same regulations under which, the shares from which the stock arose might before the conversion have been transferred, or as near thereto as circumstances admit:

Provided that the Board may, from time to time, fix the minimum amount of stock transferable, so however that such minimum shall not exceed the nominal amount of the shares from which the stock arose.

38. The holders of stock shall, according to the amount of stock held by them, have the same rights, privileges and

advantages as regards dividends, voting at meetings of the company, and other matters, as if they held the shares from which the stock arose; but no such privilege or advantage (except participation in the dividends and profits of the company and in the assets on winding up) shall be conferred by an amount of stock which would not, if existing in shares, have conferred that privilege or advantage.

39. Such of the regulations of the company (other than those relating to share warrants), as are applicable to paid-up shares shall apply to stock and the words "share" and "shareholder" in those regulations shall include "stock" and "stockholder" respectively.

Share warrants

40. The company may issue share warrants subject to, and in accordance with, the provisions of sections 114 and 115; and accordingly the Board may in its discretion, with respect to any share which is fully paid up, on application in writing signed by the person registered as holder of the share and authenticated by such evidence (if any) as the Board may, from time to time, require as to the identity of the person signing the application, and on receiving the certificate (if any) of the share, and the amount of the stamp duty on the warrant and such fee as the Board may from time to time require, issue a share warrant.

41.(1) The bearer of a share warrant may at any time deposit the warrant at the office of the company, and so long as the warrant remains so deposited, the depositor shall have the same right of signing a requisition for calling a meeting of the company, and of attending, and voting and exercising the other privileges of a member at any meeting held after the expiry of two clear days from the time of deposit, as if his name were inserted in the register of members as the holder of the shares included in the deposited warrant.

(2) Not more than one person shall be recognised as depositor of the share warrant.

(3) The company shall, on two days' written notice, return the deposited share warrant to the depositor.

42.(1) Subject as herein otherwise expressly provided, no person shall, as bearer of a share warrant, sign a requisition for calling a meeting of the company, or attend, or vote or exercise any other privilege of a member at a meeting of the company, or be entitled to receive any notices from the company.

(2) The bearer of a share warrant shall be entitled in all other respects to the same privileges and advantages as if he were named in the register of members as the holder of the shares included in the warrant, and he shall be a member of the company.

43. The Board may, from time to time, make rules as to the terms on which (if it shall think fit) a new share warrant or coupon may be issued by way of renewal in case of defacement, loss or destruction.

Alteration of capital

44. The company, may, from time to time, by ordinary resolution increase the share capital by such sum, to be divided into shares of such amount, as may be specified in the resolution.

45. The company may, by ordinary resolution, —

(a) consolidate and divide all or any of its share capital into shares of larger amount that its existing shares;

(b) sub-divide its existing shares or any of them into shares of smaller amount than is fixed by the memorandum, subject, nevertheless, to the provisions of clause (d) of sub-section (1) of section 94;

(c) cancel any shares which, at the date of the passing of the resolution, have not been taken or agreed to be taken by any person.

46. The company may, by special resolution, reduce in any manner and with, and subject to, any incident authorized and consent required by law.

(a) its share capital;

(b) any capital redemption reserve account; or

(c) any share premium account.

General meetings

47. All general meetings other than annual general meetings shall be called extraordinary general meetings.

48.(1) The Board may, whenever it thinks fit, call an extraordinary general meeting.

(2) It at any time there are not within India directors capable or acting who are sufficient in number to form a quorum, any director or any two members of the company may call an extraordinary general meeting in the same manner, as nearly as possible, as that in which such a meeting may be called by the Board.

Proceedings at general meetings

49.(1) No business shall be transacted at any general meeting unless a quorum or members is present at the time when the meeting proceeds to business.

(2) Save as herein otherwise provided, five members present in person (in the case of a public company — two members present in person, in the case of a private company) shall be a quorum.

50. The chairman, if any, of the Board shall preside as chairman at every general meeting of the company.

51. If there is no such chairman, or if he is not present within fifteen minutes after the time appointed for holding the meeting, or is unwilling to act as chairman of the meeting, the directors present shall elect one of their number to be chairman of the meeting.

52. If at any meeting no director is wiling to act as chairman or if no director is present within fifteen minutes after the time appointed for holding the meeting, the members present shall choose one of their number to be chairman of the meeting.

53.(1) The chairman may, with the consent of any meeting at which a quorum is present, and shall, if so directed by the meeting, adjourn the meeting from time to time and from place to place.

(2) No business shall be transacted at any adjourned meeting other than the business left unfinished at the meeting from which the adjournment took place.

(3) When a meeting is adjourned for thirty days or more, notice of the adjourned meeting shall be given as in the case of an original meeting.

(4) Save as aforesaid, it shall not be necessary to give any notice of an adjournment or of the business to be transacted at an adjourned meeting.

54. In the case of an equality of votes, whether on a show of hands or on a poll, the chairman of the meeting at which the show of hands takes place, or at which the poll is demanded, shall be entitled to a second or casting vote.

55. Any business other than that upon which a poll has been demanded may be proceeding with, pending the taking of the poll.

Vote of members

56. Subject to any rights or restrictions for the time being attached to any class or classes of shares —

(a) on a show of hands, every member present in person shall have one vote; and

(b) on a poll, the voting rights of members shall be as laid down in section 87.

57. In the case of joint holders, the vote of the senior [first named shareholder] who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other joint holders.

For this purpose, seniority shall be determined by the order in which the names stand in the register of members.

58. A member of unsound mind, or in respect of whom an order has been made by any Court having jurisdiction in lunacy, may vote, whether on a show of hands or on a poll, by his committee or other legal guardian, and any such committee or guardian may, on a poll, vote by proxy.

59. No member shall be entitled to vote at any general meeting unless all calls or other sums presently payable by him in respect of shares in the company have been paid.

60.(1) No objection shall be raised to the qualification of any voter except at the meeting or adjourned meeting at which the vote objected to is given or tendered, and every vote not disallowed at such meeting shall be valid for all purposes.

(2) Any such objection made in due time shall be referred to the chairman of the meeting, whose decision shall be final and conclusive.

61. The instrument appointing a proxy and the power of attorney or other authority, if any, under which it is signed or a notarially certified copy of that power or authority, shall be deposited at the registered office of the company not less than 48 hours before the time for holding the meeting or adjourned meeting at which the person named in the instrument proposes to vote, or, in the case of a poll, not less than 24 hours before the time appointed for the taking of the poll; and in default the instrument of proxy shall not be treated as valid.

62. An instrument appointing a proxy shall be in either of the forms in Schedule IX to the Act or a form as near thereto as circumstances admit.

63. A vote given in accordance with the terms of an instrument of proxy shall be valid, notwithstanding the previous death or insanity of the principal or the revocation of the proxy or of the authority under which the proxy was executed, or the transfer of the shares in respect to which the proxy is give: Provided that no intimation in writing of such death, insanity, revocation or transfer shall have been received by the company at its office before the commencement of the meeting or adjourned meeting at which the proxy is used.

Board of directors

64. The number of the directors and the names of the first directors shall be determined in writing by the subscribers of the memorandum or a majority of them.

65.(1) The remuneration of the directors shall, in so far as it consists of a monthly payment, be deemed to accrue from day to day.

(2) In addition to the remuneration payable to them in pursuance of the Act, the directors may be paid all traveling,

hotel and other expenses properly incurred by them—

(a) in attending and returning from meetings of the Board of Directors or any committee thereof or general meetings of the company; or

(b) in connection with the business of the company.

66. The qualification of a director shall be the holding of at least one share of the company.

67. The Board may pay all expenses incurred in getting up and registering the company.

68. The company may exercise the powers conferred by section 50 with regard to having an official seal for use abroad, and such powers shall be vested in the Board.

69. The company may exercise the powers conferred on it by sections 157 and 158 with regard to the keeping of a foreign register, and the Board may (subject to the provisions of those sections) make and vary such regulations as it may think fit respecting the keeping of any such register.

70. All cheques, promissory notes, drafts, hundis (i.e., Indian bills of exchange), bills of exchange and other negotiable instruments, and all receipts for moneys paid to the company, shall be signed, drawn, accepted, endorsed or otherwise executed, as the case may be, or where there is no managing agent or secretaries and treasurers, by such person and in such manner as the Board shall from time to time by resolution determine.

71. Every director present at any meeting of the Board or of a committee thereof shall sign his name in a book to be kept for that purpose.

72.(1) The Board shall have power at any time, and from time to time, to appoint a person as an additional director, provided the number of the directors and additional directors together shall not at any time exceed the maximum strength fixed for the Board by the articles.

(2) Such person shall hold office only up to the date of the next annual general meeting of the company but shall be eligible for appointment by the company as a director at that meeting subject to the provisions of the Act.

Proceedings of Board

73.(1) The Board of directors may meet for the despatch of business, adjourn and otherwise regulate its meetings, as it thinks fit.

(2) A director may, and the manager or secretary on the requisition of the Board shall, at any time, summon a meeting of the Board.

74.(1) Save as otherwise expressly provided in the Act, questions arising at any meeting of the Board shall be decided by a majority of votes.

(2) In case of an equality of votes, the chairman of the Board, if any, shall have a second or casting vote.

75. The continuing directors may act notwithstanding any vacancy in the Board; but, if and so long as their number is reduced below the quorum fixed by the Act for a meeting of the Board; the continuing directors or director may act for the purpose of increasing the number of directors to that fixed for the quorum, or of summoning a general meeting of the company, but for no other purpose.

76.(1) The Board may elect a chairman of its meetings and determine the period for which he is to hold office.

(2) If no such chairman is elected, or if at any meeting the chairman is not present within five minutes after the time appointed for holding the meeting, the directors present may choose one of their number to be chairman of the meeting.

77.(1) The Board may, subject to the provisions of the Act, delegate any of its powers to committees consisting of such member or members of its body as it thinks fit.

(2) Any committee so formed shall, in the exercise of the powers so delegated, conform to any regulations that may be imposed on it by the Board.

78.(1) A committee may elect a chairman of its meetings.

(2) If no such chairman is elected, or if at any meeting the chairman is not present within five minutes after the time appointed for holding the meeting, the members present may choose one of their number to be chairman of the meeting.

79.(1) A committee may meet and adjourn as it thinks proper.

(2) Questions arising at any meeting of a committee shall be determined by a majority of votes of the members present, and in case of an equality of votes, the chairman shall have a second or casting vote.

80. All acts done by any meeting of the Board of a committee thereof or by any person acting as a director shall, notwithstanding that it may be afterwards discovered that there was some defect in the appointment of any one or more of such directors or of any person acting as aforesaid, or that they or any of them were disqualified, be as valid as if every such director or such person had been duly appointed and was qualified to be a director.

81. Save as otherwise expressly provided in the Act, a resolution in writing, signed by all the members of the Board or of a committee thereof, for the time being entitled to receive notice of a meeting of the Board or committee, shall be as valid and effectual as if it had been passed at a meeting of the Board or committee, duly convened and held.

Manager or secretary

82. Subject to the provisions of the Act,—

(1) A manager or secretary may be appointed by the Board of such term, at such remuneration and upon such conditions as it may think fit; and any manager or secretary so appointed may be removed by the Board;

(2) A director may be appointed as manager or secretary.

83. A provision of the Act of these regulations requiring or authorizing a thing to be done by or to a director and the manager or secretary shall not be satisfied by its being done by or to the same person acting both as director and as, or in place of, the manager or secretary.

The Seal

84.(1) The Board shall provide for the safe custody of the seal.

(2) The seal of the company shall not be affixed to any instrument except by the authority of a resolution of the Board or of a committee of the Board authorized by it in that behalf, and except in the presence of at least two directors and of the secretary or such other person as the Board may appoint for the purpose; and those two directors and the secretary or other person as aforesaid shall sign every instrument to which the seal of the company is so affixed in their presence.

Dividends and reserve

85. The company in general meeting may declare dividends, but no dividend shall exceed the amount recommended by the Board.

86. The Board may from time to time pay to the members such interim dividends as appear to it to be justified by the profits of the company.

87.(1) The Board may, before recommending any dividend, set aside out of the profits of the company such sums as it thinks proper as a reserve or reserves which shall at the discretion of the Board, be applicable for any purpose to which the profits of the company may be properly applied, including provision for meeting contingencies or for equalising dividends; and pending such application, may, at the like discretion, either be employed in the business of the company or be invested in such investments (other than shares of the company) as the Board may, from time to time think fit.

(2) The Board may also carry forward any profits which it may think prudent not to divide, without setting them aside as a reserve.

88.(1) Subject to the rights of persons, if any, entitled to shares with special rights as to dividends, all dividends shall be declared and paid according to the amounts paid or credited as paid on the shares in respect whereof the dividend is paid, but if and so long as nothing is paid upon any of the shares in the company, dividends may be declared and paid according to the amounts of the shares.

(2) No amount paid or credited as paid on a share in advance of calls shall be treated for the purposes of this regulation as paid on the share.

(3) All dividends shall be apportioned and paid proportionately to the amounts paid or credited as paid on the shares during any portion or portions of the period in respect of which the dividend is paid; but if any share is issued on terms providing that it shall rank for dividend as from a particular date such share shall rank for dividend accordingly.

89. The Board may deduct from any dividend payable to any member all sums of money, if any, presently payable by him to the company on account of calls or otherwise in relation to the shares of the company.

90. (Omitted by Notification No. GSR 631, dated April 23, 1966).

91.(1) Any dividend, interest or other moneys payable in cash in respect of shares may be paid by cheque or warrant sent through the post directed to the registered address of the holder or, in the case of joint holders, to the registered address of that one of the joint holders who is first named on the register of the members, or to such person and to such address as the holder or joint holders may in writing direct.

(2) Every such cheque or warrant shall be made payable to the order of the person to whom it is sent.

92. Any one of two or more joint holders of a share may give effectual receipts for any dividends, bonuses or other moneys payable in respect of such share.

93. Notice of any dividend that may have been declared shall be given to the persons entitled to share therein in the manner mentioned in the Act.

94. No dividend shall bear interest against the company.

Accounts

95.(1) The Board shall from time to time determine whether and to what extent and at what time and places and

under what conditions or regulations, the accounts and books of the company, or any of them, shall be open to the inspection of members not being directors.

(2) No member (not being a director) shall have any right of inspecting any account or book or document of the company except as conferred by law or authorized by the Board or by the company in general meeting.

Capitalization of profits

96.(1) The company in general meeting may, upon the recommendation of the Board, resolve —

(a) that it is desirable to capitalize any part of the amount for the time being standing to the credit of any of the company's reserve accounts or to the credit of the profit and loss account, or otherwise available for distribution; and

(b) that such sum be accordingly set free for distribution in the manner specified in clause (2) amongst the members who would have been entitled thereto, if distributed by way of dividend and in the same proportions.

(2) The sum aforesaid shall not be paid in cash but shall be applied, subject to the provisions contained in clause (3), either in or towards —

(i) paying up any amounts for the time being unpaid on any shares held by such members respectively;

(ii) paying up in full, unissued shares of the company to be alloted and distributed, credited as fully paid up, to and amongst such members in the proportions aforesaid; or

(iii) partly in the way specified in sub-clause (i) and partly in that specified in sub-clause (ii).

(3) A share premium account and a capital redemption reserve account may, for the purposes of this regulation, only be applied in the paying up of unissued shares to be issued to members of the company as fully paid bonus shares.

(4) The Board shall give effect to the resolution passed by the company in pursuance of this regulation.

97.(1) Whenever such a resolution as aforesaid shall have been passed, the Board shall —

(a) make all appropriations and applications of the undivided profits resolved to be capitalized thereby, and all allotments and issues of fully paid shares if any; and

(b) generally do all acts and things required to give effect thereto.

(2) The Board shall have full power —

(a) to make such provision, by the issue of fractional certificates or by payment in cash or otherwise as it thinks fit, for the case of shares or debentures becoming distributable in fractions; and also

(b) to authorise any person to enter, on behalf of all the members entitled thereto, into an agreement with the company providing for the allotment of them respectively, credited as fully paid up, of any further shares to which they may be entitled upon such capitalization, or (as the case may require) for the payment up by the company on their behalf, by the application thereto of their respective proportions of the profits resolved to be capitalized, of the amounts or any part of the amounts remaining unpaid on their existing shares.

(3) Any agreement made under such authority shall be effective and binding on all such members.

Winding up

98.(1) If the company shall be wound up, the liquidator may, with the sanction of a special resolution of the company and any other sanction required by the Act, divide amongst the members, in specie or kind, the whole or any part of the assets of the company, whether they shall consist of the same kind or not.

(2) For the purpose aforesaid, the liquidator may set such value as he deems fair upon any property to be divided as aforesaid and may determine how such division shall be carried out as between the members or different classes of members.

(3) The liquidator may, with the like sanction, vest the whole or any part of such assets in trustees upon such trusts for the benefit of the contributories as the liquidator, with the like sanction, shall think fit, but so that no member shall be compelled to accept any shares or other securities whereon there is any liability.

Indemnity

99. Every officer or agent for the time being of the company shall be indemnified out of the assets of the company against any liability incurred by him in defending any proceedings, whether civil or criminal, in which judgment is given in his favour or in which he is acquitted or in connection with any application under section 633 in which relief is granted to him by the court.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 20 Rates of Depreciation (Schedule XIV, Companies Act, 1956)

	Nature of assets	Single Shift		Double Shift		Triple Shift	
		W.D.V. *	S.L.M. **	W.D.V.	S.L.M.	W.D.V.	S.L.M.
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
I.	(a) Buildings (other than factory buildings (NESD)) ***	5%	1.63%	—	—	—	—
	(b) Factory buildings	10%	3.34%	—	—	—	—
	(c) Purely temporary structures, such as wooden structures	100%	100%	—	—	—	—
II.	Plant and Machinery						
	(i) General rate applicable to						
	(a) Plant and machinery (not being a ship) other than continuous process plant for which no special rate has been prescribed under (b) below	13.91%	4.75%	20.87%	7.42%	27.82%	10.34%
	(b) Continuous process plant, for which no special rate has been prescribed under (ii) below, (NESD)	15.33%	5.28%	—	—	—	—
(ii.)	Special rates						
A.1.	Cinematograph films — machinery used in the production and exhibition of cinematograph films (NESD)						
(a)	Recording equipment, reproducing equipment, developing machines, printing machines, editing machines, synchronizers and studio lights except bulbs	20%	7.07%	—	—	—	—
(b)	Projecting equipment of film exhibiting concerns	20%	7.07%	—	—	—	—
2.	Cycles (NESD)	20%	7.07%	—	—	—	—
3.	Electrical machinery, X-ray and electrotherapeutic apparatus and electrotherapeutic apparatus and accessories thereto, medical diagnostic equipments, namely cat-scan, ultrasound machines, ECG monitors etc. (NESD)	20%	7.07%	—	—	—	—
4.	Juice boiling pans (karhais) (NESD)	20%	7.07%	—	—	—	—
5.	Motor cars, motor cycles, scooters and other mopeds (NESD)	25.89%	9.5%	—	—	—	—
6.	Electrically operated vehicles including battery powered or fuel cell powered vehicles (NESD)	20%	7.07%	—	—	—	—
7.	Sugarcane crushers (indigenous kolhus and belans) (NESD)	20%	7.07%	—	—	—	—
8.	Glass manufacturing concerns except direct fire glass melting furnaces — recuperative and regenerative glass melting furnaces	20%	7.07%	30%	11.31%	40%	16.21%
9.	Machinery used in the manufacturing of electronic goods and components	15.62%	5.38%	23.42%	8.46%	31.23%	11.87%
B1.	Aeroplanes, aero engines, simulators, visual system and quick engine change equipment (NESD)	16.2%	5.6%	—	—	—	—
2.	Concrete pipes manufacture — moulds (NESD)	30%	11.31%	—	—	—	—
3.	Drum container manufacture — dies (NESD)	30%	11.31%	—	—	—	—
4.	Earth moving machinery employed in heavy construction works, such as dams, tunnels, canals, etc. (NESD)	30%	11.31%	—	—	—	—
5.	Glass manufacturing concerns except direct fire glass melting furnaces — moulds (NESD)	30%	11.31%	—	—	—	—
6.	Moulds in iron foundries (NESD)	30%	11.31%	—	—	—	—
7.	Mineral oil concerns — field operations (above ground) — portable boilers, drilling tools, well head tanks, rigs, etc. (NESD)	30%	11.31%	—	—	—	—
8.	Mines and quarries — portable underground machinery and earth moving machinery used in open cast mining (NESD)	30%	11.31%	—	—	—	—

9.	Motor buses and motor lorries other than those used in a business of running them on hire (NESD)	30%	11.31%	—	—	—	—
9A.	Motor tractors, harvesting combines (NESD)	30%	11.31%	—	—	—	—
10.	Patterns, dies and templates (NESD)	30%	11.31%	—	—	—	—
11.	Ropeway structures — ropeways, ropes and trestle sheaves and connected parts (NESD)	30%	11.31%	—	—	—	—
12.	Shoe and other leather goods factories — wooden lasts used in the manufacture of shoes	30%	11.31%	—	—	—	—
C1.	Omitted						
2.	Motor buses, motor lorries and motor taxis used in a business of running them on hire (NESD)	40%	16.21%	—	—	—	—
3.	Rubber and plastic goods factories — moulds (NESD)	40%	16.21%	—	—	—	—
4.	Data processing machines including computers (NESD)	40%	16.21%	—	—	—	—
5.	Gas cylinders including valves and regulators (NESD)	40%	16.21%	—	—	—	—
D1.	Artificial silk manufacturing machinery wooden parts	100%	100%	—	—	—	—
2.	Cinematograph films — bulbs of studio lights	100%	100%	—	—	—	—
3.	Flour mills – Rollers	100%	100%	—	—	—	—
4.	Glass manufacturing concerns — direct fire glass melting furnaces	100%	100%	—	—	—	—
4A.	Float glass melting furnaces (NESD)	27%	10%	—	—	—	—
5.	Iron and Steel industries — rolling mill rolls	100%	100%	—	—	—	—
6.	Match factories — wooden match frames	100%	100%	—	—	—	—
7.	Mineral oil concerns —						
(a)	Plant used in field operations (below ground) — distribution — returnable packages	100%	100%	—	—	—	—
(b)	Plant used in field operations (distribution), curbside pumps including underground tanks and fittings	100%	100%	—	—	—	—
8.	Mines and quarries						
(a)	Tubs, winding ropes, haulage ropes and sand stowing pipes	100%	100%	—	—	—	—
(b)	Safety lamps	100%	100%	—	—	—	—
9.	Salt works — salt pans, reservoirs and condensers, etc. made of earthly, sandy or clay material or any other similar material	100%	100%	—	—	—	—
10.	Sugar works — rollers	100%	100%	—	—	—	—
III.	Furniture and Fittings—						
1.	General rates (NESD)	18.1%	6.33%	—	—	—	—
2.	Rate for furniture and fittings used in hotels, restaurants and boarding houses, schools, colleges and other educational institutions, libraries, welfare centers, meeting halls, cinema houses, theatres and circuses and for furniture and fittings let out on hire for use on the occasion of marriages and similar functions (NESD)	25.88%	9.5%	—	—	—	—
IV.	Ships						
1.	Ocean going ships —						
i)	Fishing vessels with wooden hulls (NESD)	27.05%	10%	—	—	—	—
ii)	Dredgers, tugs, barges, survey launches and other similar ships used mainly for dredging purposes (NESD)	19.8%	7%	—	—	—	—
iii)	Other ships (NESD)	14.6%	5%	—	—	—	—
2.	Vessels ordinarily operating on inland waters —						
i)	Speed boats (NESD)	20%	7.07%	—	—	—	—
	Other vessels (NESD)	10%	3.34%	—	—	—	—

NOTES

1. "buildings" includes roads, bridges, culverts, wells and tube-wells.

2. "factory buildings" does not include offices, godowns, officers and employees' quarters, roads, bridges, culverts, wells and tube-wells.

3. "speed boat" means a motor boat driven by a high speed internal combustion engine capable of propelling the boat at a speed exceeding 24 Kilometers per hour in still water and so designed that when running at a speed it will plane, i.e., its bow will rise from the water.

4. Where, during any financial year, any addition has been made to any asset, or where any asset has been sold, discarded, demolished or destroyed, the depreciation on such assets shall be calculated on a pro rata basis from the date of such addition or, as the case may be, up to the date on which such asset has been sold, discarded, demolished or destroyed.

5. The following information should also be disclosed in the accounts:

(i) depreciation methods used; and

(ii) depreciation rates or the useful lives of the assets, if they are different from the principal rates specified in the Schedule.

6. The calculations of the extra depreciation for double shift working and for triple shift working shall be made separately in the proportion which the number of days for which the concern worked double shift or triple shift, as the case may be, bears to the normal number of working days during the year. For this purpose, the normal number of working days during the year shall be deemed to be —

(a) in the case of a seasonal factory or concern, the number of days on which the factory or concern actually worked during the year or 180 days, whichever is greater;

(b) in any other case, the number of days on which the factory or concern actually worked during the year or 240 days, whichever is greater.

The extra shift depreciation shall not be charged in respect of any item of machinery or plant which has been specifically, excepted by inscription of the letters "NESD" (meaning "No Extra Shift Depreciation") against it in sub-items above and also in respect of the following items of machinery and plant to which the general rate of depreciation of 13.91% applies —

(1) Accounting machines.

(2) Air-conditioning machinery including room air-conditioners.

(3) Building contractor's machinery.

(4) Calculating machines.

(5) Electrical machinery - switchgear and instruments, transformers and other stationary plant and wiring and fitting of electric light and fan installations.

(6) Hydraulic works, pipelines and sluices

(7) Locomotives, rolling stocks, tramways and railways used by concerns, excluding railway concerns.

(8) Mineral oil concerns - field operations:

(a) [Omitted]

(b) Prime movers.

(c) [Omitted]

(d) Storage tanks (above ground).

(e) Pipelines (above ground).

(f) Jetties and dry docks.

(9) Mineral oil concerns - field operations (distribution) - kerbside pumps, including underground tanks and fittings.

(10) Mineral oil concerns - refineries:

(a) [Omitted]

(b) Prime movers.

(c) [Omitted]

(d) LPG Plant

(11) Mines and quarries:

(a) Surface and underground machinery (other than electrical machinery and portable underground machinery).

(b) Head-gears.

(c) Rails.

(d) [Omitted]

(e) Shafts and inclines.

(f) Tramways on the surface.

(12) Neo-post franking machines.

(13) Office machinery

(14) Overhead cables and wires.

(15) Railway sidings.

(16) Refrigeration plant containers, etc. (other than racks).

(17) Ropeway structures:

(a) Trestle and station steel work.

(b) Driving and tension gearing.

(18) Salt works - reservoirs, condensers, salt pans, delivery channels and piers if constructed of masonry, concrete, cement, asphalt or similar materials; barges and floating plant; piers, quays and jetties; and pipelines for conveying brine if constructed of masonry, concrete, cement, asphalt or similar materials.

(19) Surgical instruments.

(20) Tramways electric and tramways run by internal combustion engines - permanent way: cars - car trucks, car bodies, electrical equipment and motors; tram cars including engines and gears.

(21) Typewriters.

(22) Weighing machines.

(23) Wireless apparatus and gear, wireless appliances and accessories.

7. "Continuous process plant" means a plant that is required and designed to operate 24 hours a day.

8. Notwithstanding anything mentioned in this Schedule, depreciation on assets, whose actual cost does not exceed five thousand rupees, shall be provided depreciation at the rate of 100%. Provided that where the aggregate actual cost of individual items of plant and machinery costing Rs. 5,000 or less constitutes more than 10% of the total actual cost of plant and machinery, rates of depreciation applicable to such items shall be the rates as specified in Item II of the Schedule.

---

* **Written Down Value**

** **Straight line method**

*** **See endnote 6.**

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 21 List of Accounting Standards

Accounting Standard (AS)	Title of the AS	Mandatory for periods commencing on or after	Levels of Enterprises to whom applicable, Remarks [See Note 1]	Refer Note No.
AS 1	Disclosure of Accounting Policies	1-4-1991 for companies, 1-4-1993 for others	I, II and III	
AS 2	Valuation of Inventories	1-Apr-99	I, II and III	
AS 3	Cash flow Statements	1-Apr-01	I	1

AS 4	Contingencies and Events Occurring After the Balance Sheet Date	1-Apr-95	I, II and III	2
AS 5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	1-Apr-96	I, II and III	3
AS 6	Depreciation Accounting	1-Apr-95	I, II and III	4
AS 7	Construction Contracts	For all contracts entered into during accounting periods on or after 1-4-2003	I, II and III	5a
AS 8	Accounting for Research and Development	1-4-1991 for companies, 1-4-1993 for others	I, II and III	4
AS 9	Revenue Recognition	1-4-1991 for companies 1-4-1993 for others	I, II and III	
AS 10	Accounting for Fixed Assets	1-4-1991 for companies, 1-4-1993 for others	I, II and III	6, 4
AS 11	The Effects of Changes in Foreign Exchange Rates	1-Apr-04	I, II and III	5b
AS 12	Accounting for Government Grants	1-Apr-94	I, II and III	
AS 13	Accounting for Investments	1-Apr-95	I, II and III	7
AS 14	Accounting for Amalgamations	1-Apr-95	I, II and III	8
AS 15	Employees Benefits (Revised 2005)	1-Apr-06	I, II and III	9
AS 16	Borrowing Costs	1-Apr-00	I, II and III	6
AS 17	Segment Reporting	1-Apr-01	I	2
AS 18	Related Party Disclosures	1-Apr-01	I	1, 10
AS 19	Leases	For all assets leased for accounting periods commencing on or after 1-4-2001	I, II and III	1, 11a
AS 20	Earnings Per Share	1-Apr-01	I, II and III	1, 11b, 19
AS 21	Consolidated Financial Statements	1-Apr-01	I	12
AS 22	Accounting for Taxes on Income	1-Apr-01	I, II and III	13
AS 23	Accounting for investments in associates in Consolidated Financial Statements	1-Apr-02	I	14
AS 24	Discontinuing Operations	1-Apr-04	I	1
		1-Apr-05	II, III	
AS 25	Interim Financial Reporting	1-Apr-02	I	11c, 15
AS 26	Intangible Assets	1-Apr-03	I	4, 16
		1-Apr-04	II, III	
AS 27	Financial Reporting of Interests in Joint Ventures	1-Apr-02	I	14, 17
AS 28	Impairment of Assets	1-Apr-04	I	1,18
		1-Apr-06	II	
		1-Apr-08	III	

AS 29	Provisions, Contingent Liabilities and Contingent Assets	1-Apr-04	I, II and III	1, 11d, 2

Note 1:

In view of the applicability of the accounting standards and exemptions/relaxations for SMEs, the necessary modifications have been made in AS 3, AS 17, AS 18, AS 19, AS 20, AS 24 and AS 28, coming into effect in respect of accounting periods commencing on or after 1-4-2004. Relaxations for AS 29 are incorporated in the AS itself.

Note 2:

From the date of coming into operation of AS 29, the following stand withdrawn:

AS 4 — Contingencies and Events Occurring after the Balance Sheet Date — paras 1(a), 2.3.1, 4(4.1 to 4.4), 5(5.1 to 5.6), 6, 7 (7.1 to 7.3), 9.1 (relevant portion), 9.2, 10, 11, 12 and 16) stand withdrawn. However, till the issuance of the proposed Accounting Standard on financial instruments, paragraphs which deal with contingencies would remain operational to the extent they cover impairment of assets not covered by other Accounting Standards. For example, provision for bad and doubtful debts.

Note 3:

Limited revision to AS 5 by adding para 33 effective for accounting periods commencing on or after 1-4-2001.

Note 4:

From the date of coming into operation of AS 26, the following stand withdrawn:

AS 8 — Accounting for Research and Development

AS 6 — Depreciation Accounting only with respect to amortisation of intangible assets

AS 10 — Accounting for Fixed Assets — paras 16.3 to 16.7, 37 and 38

Note 5:

a. The revised AS 7 (2002) is applicable in respect of all contracts entered into during the accounting periods commencing on or after 1-4-2003; however, for contracts entered into prior to this date, AS 7 (1983) would continue to be applicable.

b. The revised AS 11 (2003) would supersede AS 11 (1994); however, accounting for transactions in foreign currencies entered into before the date the revised AS 11 (2003) comes into effect, i.e. 1-4-2004, AS 11 (1994) would continue to be applicable.

Note 6:

From the date of coming into operation of AS 16, the following stand withdrawn:

AS 10 — Accounting for Fixed Assets — paragraphs 9.2, 29 (except the first sentence)

Note 7:

Limited revision to AS 13 in para 2 effective for accounting periods commencing on or after 1-4-2002.

Note 8:

Limited revision to AS 14 in paras 23 and 42 effective for accounting periods commencing on or after 1.4.2004.

Note 9:

Exemptions and Relaxations for AS 15 (Revised)

CRITERIA	LEVEL II SMES	LEVEL III SMES
No. of Employees	Average No. of employees of 50 or more	Average employees of less than 50
Recognition and measurement of short term accumulated compensating absences contained in Paras 11 to 16	Not applicable	Not applicable
Amounts due for payment under Defined Contribution Plans or Termination Benefits, after 12 months from the end of the year	Applicable (See Note i)	Applicable (See Note i)
Recognition and measurement under Defined Benefit Plans contained in Paras 50 to 116 and disclosures under Paras 117 to 118	Applicable (See Note ii)	Applicable (See Note iii)
Disclosures contained in Paras 119 to 123 under Defined Benefit Plans	Applicable (See Note iv)	Not applicable

Recognition and measurement of other long term benefits contained in Paras 129 to 131	**Applicable**	**Applicable**

i. Need not be accounted for on discounted basis (Paras 46 and 139)

ii. Determination of liability should be based on PUCM (discount rate provisions shall apply)

iii. For recognition and measurement of liabilities under DBP, PUCM need not be applied. Some other rational methods can be applied.

iv. Actuarial assumptions should be disclosed

Note 10:

Limited revision to AS 18 in para 26 and insertion of para 27 effective for accounting periods commencing on or after 1-4-2003, but earlier application is encouraged.

Note 11:

a. AS 19 — paras 22(c), (e) and (f); 25(a), (b) and (e); 37(a), (f) and (g); and 46(b), (d) and (e) with respect to disclosures, of AS 19 are not applicable to Level II and Level III enterprises.

b. AS 20 is applicable to Level II and Level III enterprises, if they disclose earnings per share. AS 20 is applicable to all companies, (irrespective of category of Level) as Part IV of Schedule VI to the Companies Act, 1956, requiring disclosure of earnings per share (Also refer ASI 12). However, all the enterprises including companies, who fall either in Level II or Level III, are not required to disclose diluted earnings per share and information required by para 48 of AS 20.

c. At present, in India, as no enterprise is required to present interim financial report within the meaning of AS 25, compliance with the disclosure and presentation requirements and measurement principles of AS 25 are applicable to certain Level I enterprises, for their interim financial results. At present, in any case, AS 25 is not mandatorily applicable to Level II and Level III enterprises.

d. AS 29 — para 67 is not applicable to Level II enterprises and para 66 and para 67 are not applicable to Level III enterprises.

Note 12:

AS 21 is mandatory if an enterprise presents consolidated financial statements. In other words, the accounting standard does not mandate an enterprise to present consolidated financial statements but, if the enterprise presents consolidated financial statements for complying with the requirements of any statute or otherwise, it should prepare and present consolidated financial statements in accordance with AS 21.

Note 13:

AS 22 comes into effect in respect of accounting periods commencing on or after 1-4-2001. It is mandatory in nature for:

a. All the accounting periods commencing on or after 1-4-2001, in respect of the following:

i. Enterprises whose equity or debt securities are listed on a recognised stock exchange in India and enterprises that are in the process of issuing equity or debt securities that will be listed on a recognised stock exchange in India as evidenced by the board of directors' resolution in this regard.

ii. All the enterprises of a group, if the parent presents consolidated financial statements and the Accounting Standard is mandatory in nature in respect of any of the enterprises of that group in terms of (i) above.

b. All the accounting periods commencing on or after 1-4-2002, in respect of companies not covered by (a) above.

c. All the accounting periods commencing on or after 1-4-2003 (deferred to 1-4-2006) in respect of all other enterprises. (Refer July 2004 ICAI Journal)

Note 14:

AS 23, AS 27 would come into effect in respect of accounting periods commencing on or after 1-4-2002. AS 23, AS 27 is mandatory if an enterprise presents consolidated financial statements. In other words, if an enterprise presents consolidated financial statements, it should account for investments in associates in the consolidated financial statements in accordance with AS 23, AS 27 from the date of its coming into effect; i.e., 1-4-2002.

Note 15:

Limited revision to AS 25 in para 16 effective for accounting periods commencing on or after 1.4.2004. Para 29(c) and certain paragraphs of Appendix 3 have also been revised to omit the word "effective".

Note 16:

Limited revision to AS 26 in para 6 effective for accounting periods commencing on or after 1-4-2003.

Note 17:

Limited revision to AS 27 in para 6 and deletion of para 9 effective for accounting periods commencing on or after

1-4-2004.

Note 18:

i. Applicable only for accounting periods commencing on or after April 1, 2008.

ii. Option to measure value in use on a reasonable estimate basis under para 121(g).

Note 19:

Limited revision to AS 20 in para 48 (and consequential in para 51) effective for accounting periods commencing on or after 1-4-2004.

Other Notes:

I. Applicability of Accounting Standards

a. Enterprises are classified into three categories, viz., Level I, Level II and Level III.

b. Level I enterprises are to comply fully with all the accounting standards;

c. Level II and Level III enterprises are considered as Small and Medium Sized Enterprises (SMEs). Level II and Level III enterprises are fully exempted from certain accounting standards, which primarily deal with disclosure requirements, given relaxations from certain disclosure requirements in respect of other accounting standards, which deal with recognition, measurement and disclosure requirements.

II. Criteria for classification of enterprises

a. Level I Enterprises

Enterprises which fall in any one or more of the following categories, at any time during the accounting period:

i. Whose equity or debt securities are listed, whether in India or outside India.

ii. Which are in the process of listing their equity or debt securities as evidenced by the board of directors' resolution.

iii. Banks including co-operative banks.

iv. Financial Institutions.

v. Carrying on insurance business.

vi. All commercial, industrial and business reporting enterprises, whose turnover for the immediately preceding accounting period on the basis of audited financial statements exceeds Rs. 50 crore. Turnover does not include 'other income'.

vii. All commercial, industrial and business reporting enterprises having borrowings, including public deposits, in excess of Rs. 10 crore at any time during the accounting period.

viii. Holding and subsidiary enterprises of any one of the above at any time during the accounting period.

b. Level II Enterprises

Enterprises which are not Level I but fall in one or more of the following categories:

i. All commercial, industrial and business reporting enterprises, whose turnover for the immediately preceding accounting period on the basis of audited financial statements exceeds Rs. 40 lakhs but does not exceed Rs. 50 crore. Turnover does not include 'other income'.

ii. All commercial, industrial and business reporting enterprises having borrowings, including public deposits, in excess of Rs. 1 crore but not in excess of Rs. 10 crore at any time during the accounting period.

iii. Holding and subsidiary enterprises of any one of the above at any time during the accounting period.

c. Level III Enterprises

Enterprises which are not covered under Level I and Level II.

III. Accounting Standards as applicable to different levels

Level-I	Level-II	Level-IIILevel-ILevel-IILevel-III
AS 1	AS 1	AS 1AS 17——
AS 2	AS 2	AS 2AS 18——
AS 3	—	—AS 19AS 19AS 19
AS 4	AS 4	AS 4(Partly)(Partly)
AS 5	AS 5	AS 5AS 20AS 20AS 20
AS 6	AS 6	AS 6(Partly)(Partly)
AS 7	AS 7	AS 7AS 21——
AS 8	AS 8	AS 8AS 22AS 22
AS 9	AS 9	AS 9AS 23——
AS 10	AS 10	AS 10AS 24——
AS 11	AS 11	AS 11AS 25——

AS 12	**AS 12**	**AS 12AS 26AS 26AS 26**
AS 13	**AS 13**	**AS 13AS 27——**
AS 14	**AS 14**	**AS 14AS 28AS 28AS 28**
AS 15	**AS 15**	**AS 15AS 29AS 29AS 29**
AS 16	**AS 16**	**AS 16(Partly)(Partly)**

IV. Note 2:

It may be noted that where a requirement of an accounting standard is different from the applicable law, requirements as per the law would prevail.

Accounting Standard (AS)	*Title of the AS*	*Exemptions for SMCs*	*Refer Note No.*
AS 1	**Disclosure of Accounting Policies**	**None**	
AS 2	**Valuation of Inventories**	**None**	
AS 3	**Cash flow Statements**	**Optional**	**1**
AS 4	**Contingencies and Events Occurring After the Balance Sheet Date**	**None**	**2**
AS 5	**Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies**	**None**	
AS 6	**Depreciation Accounting**	**None**	
AS 7	**Construction Contracts**	**None**	
AS 9	**Revenue Recognition**	**None**	
AS 10	**Accounting for Fixed Assets**	**None**	
AS 11	**The Effects of Changes in Foreign Exchange Rates**	**None**	**10**
AS 12	**Accounting for Government Grants**	**None**	
AS 13	**Accounting for Investments**	**None**	
AS 14	**Accounting for Amalgamations**	**None**	
AS 15	**Accounting for Retirement Benefits in the Financial Statements of Employers Employees Benefits (Revised 2005)**	**Partial**	**3**
AS 16	**Borrowing Costs**	**None**	
AS 17	**Segment Reporting**	**Optional**	**1**
AS 18	**Related Party Disclosures**	**None**	
AS 19	**Leases**	**Partial**	**4, 11**
AS 20	**Earnings Per Share**	**Partial**	**5**
AS 21	**Consolidated Financial Statements**	**None**	**6**
AS 22	**Accounting for Taxes on Income**	**None**	
AS 23	**Accounting for investments in associates in Consolidated Financial Statements**	**None**	**7**
AS 24	**Discontinuing Operations**	**None**	
AS 25	**Interim Financial Reporting**	**None**	
AS 26	**Intangible Assets**	**None**	
AS 27	**Financial Reporting of Interests in Joint Ventures**	**None**	**7**
AS 28	**Impairment of Assets**	**Partial**	**8**
AS 29	**Provisions, Contingent Liabilities and Contingent Assets**	**Partial**	**2, 9**

NOTES

Note 1:

It is not mandatory for SMCs. However, SMCs are encouraged to apply this standard.

Note 2:

As per the Notified AS, all portions of the Standard that deal with contingencies are applicable only to the extent not covered by other Accounting Standards prescribed by the Central Government.

Note 3: ***SMCs are given specific exemptions from the following specified paras of AS 15***

a. Paragraphs 11 to 16 of the standard to the extent they deal with recognition and measurement of short-term accumulating compensated absences which are non-vesting (i.e., short-term accumulating compensated absences in respect of which employees are not entitled to cash payment for unused entitlement on leaving);

b. Paragraphs 46 and 139 of the Standard which deal with discounting of amounts that fall due more than 12 months after the balance sheet date;

c. Recognition and measurement principles laid down in paragraphs 50 to 116 and presentation and disclosure requirements laid down in paragraphs 117 to 123 of the Standard in respect of accounting for defined benefit plans. However, such companies should actuarially determine and provide for the accrued liability in respect of defined benefit plans by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard. Such companies should disclose actuarial assumptions as per paragraph 120(l) of the Standard; and

d. Recognition and measurement principles laid down in paragraphs 129 to 131 of the Standard in respect of accounting for other long term employee benefits. However, such companies should actuarially determine and provide for the accrued liability in respect of other long-term employee benefits by using the Projected Unit Credit Method and the discount rate used should be determined by reference to market yields at the balance sheet date on government bonds as per paragraph 78 of the Standard.

Note 4:

SMCs are exempted from certain disclosure requirements of paragraphs 22(c), (e) and (f); 25(a), (b) and (e); 37(a) and (f); 46(b) and (d) of this standard.

Note 5:

SMCs are not required to disclose diluted EPS both including and excluding extraordinary items.

Note 6:

AS 21 is mandatory if an enterprise presents consolidated financial statements. In other words, the accounting standard does not mandate an enterprise to present consolidated financial statements but, if the enterprise presents consolidated financial statements for complying with the requirements of any statute or otherwise, it should prepare and present consolidated financial statements in accordance with AS 21.

Note 7:

AS 23, AS 27 is mandatory if an enterprise presents consolidated financial statements. In other words, if an enterprise presents consolidated financial statements, it should account for investments in associates in the consolidated financial statements in accordance with AS 23, AS 27.

Note 8:

SMCs are allowed to measure the 'value in use' on the basis of reasonable estimate thereof instead of computing the value in use by present value technique. Consequently, if an SMC chooses to measure the 'value in use' by not using the present value technique, the relevant provisions of AS 28, such as discount rate etc., would not be applicable to such an SMC. Further, such an SMC need not disclose the information required by paragraph 121(g) of the Standard.

Note 9:

AS 29, paragraphs 66 and 67 relating to disclosures are not applicable to SMCs.

Note 10:

In respect of accounting for transactions in foreign currencies entered into by the reporting enterprise itself or through its branches before the effective date of the notification prescribed in this Standard under section 211 of Companies Act, 1956, the applicability of this Standard would be determined on the basis of Accounting Standard (AS) 11 revised by ICAI in 2003

Note 11:

In respect of assets leased prior to the effective date of notification presenting this Standard under section 211 of the Companies Act, 1956, the applicability of this Standard would be determined on the basis of the Accounting Standard (AS) 19, issued by ICAI in 2001.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 22 Statement on Matters to Be Included in the Auditor's Report

COMPANIES (AUDITOR'S REPORT) ORDER, 2003

[GSR 480(E), DATED 12-6-2003]

In exercise of the powers conferred by sub-section (4A) of section 227 of the Companies Act, 1956 (1 of 1956), read with the Notification of the Government of India in the Department of Company Affairs, number G.S.R. 443(E), dated 18th October, 1972, as amended from time to time and in supersession of order number G.S.R. 909(E), dated 7th September, 1988, published in the Gazette of India, part II, section 3, sub-section* (i), *except as respects things done or omitted to be done before the supersession, and after consultation with the Institute of Chartered Accountants of India [constituted under the Chartered Accountants Act, 1949 (38 of 1949)], in regard to class of companies to which this order applies and other ancillary matters, the Central Government hereby makes the following order, namely:—

Short title, application and commencement.

1. (1) This order may be called the Companies (Auditor's Report) Order, 2003.

(2) It shall apply to every company including a foreign company as defined in section 591 of the Act, except the following :—

(i) a banking company as defined in clause (c) of section 5 of the Banking Regulation Act, 1949 (10 of 1949);

(ii) an insurance company as defined in clause (21) of section 2 of the Act;

(iii) a company licensed to operate under section 25 of the Act; and

(iv) a private limited company with a paid-up capital and reserves not more than rupees fifty lakh (five million) and which does not have loan outstanding exceeding rupees twenty-five lakh (two and a half million) from any bank or financial institution and does not have a turnover exceeding rupees five crore (fifty million) at any point of time during the financial year.

(3) It shall come into force on the 1st day of July, 2003.

Definitions.

2. In this Order, unless the context otherwise requires,—

(a) "Act" means the Companies Act, 1956 (1 of 1956);

(b) "chit fund company", "nidhi company" or "mutual benefit company" means a company engaged in the business of managing, conducting or supervising as a foreman or agent of any transaction or arrangement by which it enters into an agreement with a number of subscribers that every one of them shall subscribe to a certain sum of instalments for a definite period and that each subscriber, in his turn, as determined by lot or by auction or by tender or in such other manner as may be provided for in the agreement, shall be entitled to a prize amount, and includes companies whose principal business is accepting fixed deposits from, and lending money to, members;

Auditor's report to contain matters specified in paragraphs 4 and 5.

3. Every report made by the auditor under section 227 of Act, on the accounts of every company examined by him to which this Order applies for every financial year ending on any day on or after the commencement of this Order, shall contain the matters specified in paragraphs 4 and 5.

Matters to be included in the auditor's report.

4. The auditor's report on the account of a company to which this Order applies shall include a statement on the following matters, namely:—

(i) (a) whether the company is maintaining proper records showing full particulars, including quantitative details and situation of fixed assets;

(b) whether these fixed assets have been physically verified by the management at reasonable intervals; whether any material discrepancies were noticed on such verification and if so, whether the same have been properly dealt with in the books of account;

(c) if a substantial part of fixed assets have been disposed of during the year, whether it has affected the going concern;

(ii) (a) whether physical verification of inventory has been conducted at reasonable intervals by the management;

(b) are the procedures of physical verification of inventory followed by the management reasonable and adequate in relation to the size of the company and the nature of its business. If not, the inadequacies in such procedures should be reported;

(c) whether the company is maintaining proper records of inventory and whether any material discrepancies were noticed on physical verification and if so, whether the same have been properly dealt with in the books of account;

(iii) (a) has the company granted any loans, secured or unsecured to companies, firms or other parties covered in the register maintained under section 301 of the Act. If so, give the number of parties and amount involved in the transactions; and

(b) whether the rate of interest and other terms and conditions of loans given by the company, secured or unsecured, are prima facie prejudicial to the interest of the company; and

(c) whether receipt of the principal amount and interest are also regular; and

(d) if overdue amount is more than rupees one lakh, whether reasonable steps have been taken by the company for recovery of the principal and interest; and

(e) has the company taken any loans, secured or unsecured from companies, firms or other parties covered in the register maintained under section 301 of the Act. If so, give the number of parties and the amount involved in the transactions; and

(f) whether the rate of interest and other terms and conditions of loans taken by the company, secured or unsecured, are prima facie prejudicial to the interest of the company; and

(g) whether payment of the principal amount and interest are also regular;

(iv) is there an adequate internal control system commensurate with the size of the company and the nature of its business, for the purchase of inventory and fixed assets and for the sale of goods and service. Whether there is a continuing failure to correct major weaknesses in internal control system;

(v) [(a) whether the particulars of contracts or arrangements referred to in section 301 of the Act have been entered in the register required to be maintained under that section; and

(b) whether transactions made in pursuance of such contracts or arrangements have been made at prices which are reasonable having regard to the prevailing market prices at the relevant time;

(vi) in case the company has accepted deposits from the public, whether the directives issued by the Reserve Bank of India and the provisions of sections 58A, 58AA or any other relevant provisions of the Act and the rules framed thereunder, where applicable, have been complied with. If not, the nature of contraventions should be stated; If an order has been passed by Company Law Board or National Company Law Tribunal or Reserve Bank of India or any Court or any other Tribunal whether the same has been complied with or not?

(vii) in the case of listed companies and/or other companies having a paid-up capital and reserves exceeding Rs. 50 lakhs (five million) as at the commencement of the financial year concerned, or having an average annual turnover exceeding five crore (fifty million) rupees for a period of three consecutive financial years immediately preceding the financial year concerned, whether the company has an internal audit system commensurate with its size and nature of its business;

(viii) where maintenance of cost records has been prescribed by the Central Government under clause (d) of sub-section (1) of section 209 of the Act, whether such accounts and records have been made and maintained;

(ix) (a) is the company regular in depositing undisputed statutory dues including Provident Fund, Investor Education and Protection Fund, Employees' State Insurance, Income-tax, Sales Tax, Wealth-tax, Service tax, Custom Duty, Excise Duty, cess and any other statutory dues with the appropriate authorities and if not, the extent of the arrears of outstanding statutory dues as at the last day of the financial year concerned for a period of more than six months from the date they became payable, shall be indicated by the auditor;

(b) in case dues of Income-tax/Sales tax /Wealth-tax/Service tax/Custom duty/Excise duty/cess have not been deposited on account of any dispute, then the amounts involved and the forum where dispute is pending shall be mentioned.

(A mere representation to the Department shall not constitute the dispute);

(x) whether in case of a company which has been registered for a period not less than five years, its accumulated losses at the end of the financial year are not less than fifty per cent of its net worth and whether it has incurred cash losses in such financial year and in the immediately preceding financial year;

(xi) whether the company has defaulted in repayment of dues to a financial institution or bank or debenture-holders? If yes, the period and amount of default to be reported;

(xii) whether adequate documents and records are maintained in cases where the company has granted loans and advances on the basis of security by way of pledge of shares, debentures and other securities; if not, the deficiencies to be pointed out;

(xiii) whether the provisions of any special statute applicable to chit fund have been duly complied with? In respect of nidhi/mutual benefit fund/societies:

(a) whether the net-owned funds to deposit liability ratio is more than 1:20 as on the date of balance sheet;

(b) whether the company has complied with the prudential norms on income recognition and provisioning against sub-standard/doubtful/loss assets;

(c) whether the company has adequate procedures for appraisal of credit proposals/requests, assessment of credit needs and repayment capacity of the borrowers;

(d) whether the repayment schedule of various loans granted by the nidhi is based on the repayment capacity of the borrower;

(xiv) if the company is dealing or trading in shares, securities, debentures and other investments, whether proper records have been maintained of the transactions and contracts and whether timely entries have been made therein; also whether the shares, securities, debentures and other investments have been held by the company, in its own name except to the extent of the exemption, if any, granted under section 49 of the Act;

(xv) whether the company has given any guarantee for loans taken by others from bank or financial institutions, the terms and conditions whereof are prejudicial to the interest of the company;

(xvi) whether term loans were applied for the purpose for which the loans were obtained;

(xvii) whether the funds raised on short-term basis have been used for long-term investment if yes, the nature and amount is to be indicated;

(xviii) whether the company has made any preferential allotment of shares to parties and companies covered in the Register maintained under section 301 of the Act and if so whether the price at which shares have been issued is prejudicial to the interest of the company;

(xix) whether security or charge has been created in respect of debentures issued;

(xx) whether the management has disclosed on the end use of money raised by public issues and the same has been verified;

(xxi) whether any fraud on or by the company has been noticed or reported during the year; if yes, the nature and the amount involved is to be indicated.

Reasons to be stated for unfavourable or qualified answers.

5. Where, in the auditor's report, the answer to any of the questions referred to in paragraph 4 is unfavourable or qualified, the auditor's report shall also state the reasons for such unfavourable or qualified answer, as the case may be. Where the auditor is unable to express any opinion in answer to a particular question, his report shall indicate such fact together with the reasons why it is not possible for him to give an answer to such question.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 23 Schedule XIII — Conditions to Be Fulfilled for Appointment of a Managing or Full Time Director or a Manager Without the Approval of the Central Government

PART I
APPOINTMENTS

No person shall be eligible for appointment as a managing or whole-time director or a manager (hereinafter referred to as managerial person) of a company unless he satisfies the following conditions, namely:

(a) he had not been sentenced to imprisonment for any period, or to a fine exceeding one thousand rupees, for the conviction of an offence under any of the following Acts, namely:

i) the Indian Stamp Act, 1899 (2 of 1899),

ii) the Central Excise and Salt Act, 1944 (1 of 1944),

iii) the Industries (Development and Regulation) Act, 1951 (65 of 1951),

iv) the Prevention of Food Adulteration Act, 1954 (37 of 1954),

v) the Essential Commodities Act, 1955 (10 of 1955),

vi) the Companies Act, 1956 (1 of 1956),

vii) the Securities Contracts (Regulation) Act, 1956 (42 of 1956),

viii) the Wealth-tax Act, 1957 (27 of 1957),

ix) the Income-tax Act, 1961 (43 of 1961),

x) the Customs Act, 1962 (52 of 1962),

xi) the Monopolies and Restrictive Trade Practices Act, 1969 (54 of 1969),

xii) The Foreign Exchange Regulation Act, 1973 (46 of 1973),

xiii) The Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986),

xiv) the Securities and Exchange Board of India Act, 1992 (15 of 1992),

xv) the Foreign Trade (Development and Regulation) Act, 1992 (22 of 1992),

(b) he had not been detained for any period under the Conservation of Foreign Exchange and Prevention of Smuggling Activities Act, 1974 (52 of 1974):

Provided that where the Central Government has given its approval to the appointment of a person convicted or detained under sub-paragraph (a) or sub-paragraph (b), as the case may be, no further approval of the Central Government shall be necessary for the subsequent appointment of that person if he had not been so convicted or detained subsequent to such approval;

(c) he has completed the age of 25 years and has not attained the age of 70 years:

Provided that where -

(i) he has not completed the age of 25 years, but has attained the age of majority; or

(ii) he has attained the age of 70 years;

and where his appointment is approved by a special resolution passed by the company in general meeting, no further approval of the Central Government shall be necessary for such appointment;

(d) where he is a managerial person in more than one company he draws remuneration from one or more companies subject to the ceiling provided in Section III of Part II;

(e) he is resident in India.

EXPLANATION I: For the purpose of this Schedule, resident in India includes a person who has been staying in India for a continuous period of not less than twelve months immediately preceding the date of his appointment as a managerial person and who has come to stay in India —

i) for taking up employment in India, or

ii) for carrying on a business or vocation in India.

EXPLANATION II: This condition shall not apply to the companies in Special Economic Zones as notified by the

Department of Commerce from time to time.

Provided that a person, being a nonresident in India shall enter India only after obtaining a proper Employment visa from the concerned Indian mission abroad. For this purpose, such person shall be required to furnish, along with the visa application form, profile of the company, the principal employer and terms and conditions of such person's appointment.

PART II
REMUNERATION

Section I — Remuneration payable by companies having profits.

Subject to the provisions of section 198 and section 309, a company having profits in a financial year may pay any remuneration, by way of salary, dearness allowance, perquisites, commission and other allowances, which shall not exceed five percent of its net profits for one such managerial person, and if there is more than one such managerial person, ten per cent for all of them together.

Section II — Remuneration payable by companies having no profits or inadequate profits.

1. Notwithstanding anything contained in this Part, where in any financial year during the currency of tenure of the managerial person, a company has no profits or its profits are inadequate, it may pay remuneration to a managerial person, by way of salary, dearness allowance, perquisites and any other allowances:

(A) not exceeding the ceiling limit of Rs.2,400,000 per annum or Rs.200,000 per month calculated on the following scale:-

Where the effective capital of company is		Monthly remuneration payable shall not exceed (Rupees)
i.	less than Rupees 1 crore	75,000
ii.	Rupees 1 crore or more but less than Rupees 5 crores	100,000
iii.	Rupees 5 crores or more but less than Rupees 25 crores	125,000
iv.	Rupees 25 crores or more but less than Rupees 50 crores	150,000
v.	Rupees 50 crores or more but less than Rupees 100 crores	175,000
vi.	Rupees 100 crores or more	200,000

Provided that the ceiling limits specified under this sub-paragraph shall apply, if –

(i) payment of remuneration is approved by a resolution passed by the Remuneration Committee;

(ii) the company has not made any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of thirty days in the preceding financial year before the date of appointment of such managerial person.

(B) not exceeding the ceiling limit of Rs.4,800,000 per annum or Rs.400,000 per month calculated on the following scale:-

Where the effective capital of company is		Monthly remuneration payable shall not exceed (Rupees)
i.	less than Rupees 1 crore	150,000
ii.	Rupees 1 crore or more but less than Rupees 5 crores	200,000
iii.	Rupees 5 crores or more but less than Rupees 25 crores	250,000
iv.	Rupees 25 crores or more but less than Rupees 50 crores	300,000
v.	Rupees 50 crores or more but less than Rupees 100 crores	350,000
vi.	Rupees 100 crores or more	400,000

Provided that the ceiling limits specified under this sub-paragraph shall apply, if –

(i) payment of remuneration is approved by a resolution passed by the Remuneration Committee;

(ii) the company has not made any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of thirty days in the preceding financial year before the date of appointment of such managerial person;

(iii) a special resolution has been passed at the general meeting of the company for payment of remuneration for a period not exceeding three years;

(iv) a statement along with a notice calling the general meeting referred to in clause (iii) is given to the

shareholders containing the following information, namely; -

I. General Information :

(1) Nature of industry

(2) Date or expected date of commencement of commercial production

(3) In case of new companies, expected date of commencement of activities as per project approved by financial institutions appearing in the prospectus.

(4) Financial performance based on given indicators

(5) Export performance and net foreign exchange collaborations

(6) Foreign investments or collaborators, if any.

II. Information about the appointee:

(1) Background details

(2) Past remuneration

(3) Recognition or awards

(4) Job profile and his suitability

(5) Remuneration proposed

(6) Comparative remuneration profile with respect to industry, size of the company, profile of the position and person (in case of expatriates the relevant details would be w.r.t. the country of his origin)

(7) Pecuniary relationship directly or indirectly with the company, or relationship with the managerial personnel, if any.

III. Other information:

(1) Reasons of loss or inadequate profits

(2) Steps taken or proposed to be taken for improvement

(3) Expected increase in productivity and profits in measurable terms.

IV. Disclosures:

(1) The shareholders of the company shall be informed of the remuneration package of the managerial person.

(2) The following disclosures shall be mentioned in the Board of director's report under the heading "Corporate Governance", if any, attached to the annual report:-

(i) All elements of remuneration package such as salary, benefits, bonuses, stock options, pension etc. of all the directors;

(ii) Details of fixed component and performance linked incentives along with the performance criteria;

(iii) Service contracts, notice period, severance fees;

(iv) Stock option details, if any, and whether the same has been issued at a discount as well as the period over which accrued and over which exercisable.

(C) exceeding the ceiling limit of Rs.4,800,000 per annum or Rs.400,000 per month calculated on the following scale:-

Where the effective capital of company is		Monthly remuneration payable shall not exceed (Rupees)
i.	less than Rupees 1 crore	150,000
ii.	Rupees 1 crore or more but less than Rupees 5 crores	200,000
iii.	Rupees 5 crores or more but less than Rupees 25 crores	250,000
iv.	Rupees 25 crores or more but less than Rupees 50 crores	300,000
v.	Rupees 50 crores or more but less than Rupees 100 crores	350,000
vi.	Rupees 100 crores or more	400,000

Provided that the ceiling limits specified under this sub-paragraph shall apply, if –

(i) payment of remuneration is approved by a resolution passed by the Remuneration Committee;

(ii) the company has not made any default in repayment of any of its debts (including public deposits) or debentures or interest payable thereon for a continuous period of thirty days in the preceding financial year before the date of appointment of such managerial person;

(iii) a special resolution has been passed at the general meeting of the company for payment of remuneration for a period not exceeding three years;

(iv) a statement along with a notice calling the general meeting referred to in clause (iii) is given to the shareholders containing the same information as given herein before at:

I. General Information:

II. Information about the appointee:

III. Other information:

IV. Disclosures:

Provided further that the conditions specified in sub-paragraph (C) shall apply in the case the effective capital of the company is negative;

Provided also that the prior approval of the Central Government is obtained for payment of remuneration on the above scale.

(D) not exceeding Rs, 24,000,000 per annum or Rs, 2,000,000 per month in respect of companies in Special Economic Zones as notified by the Department of Commerce from time to time.

Provided that these companies have not raised any money by public issue of shares or debentures in India;

Provided further that such companies have not made any default in India in repayment of any debts (including public deposits) or debentures or interest payable thereon for a continuous period of 30 days in any financial year.

2. A managerial person shall also be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in paragraph 1 of this section:

(a) contribution to provident fund, super-annuation fund or annuity fund to the extent these either singly or put together are not taxable under the Income-tax Act, 1961,

(b) gratuity payable at a rate not exceeding half a month's salary for each completed year of service, and

(c) encashment of leave at the end of the tenure.

3. In addition to the perquisites specified in paragraph 2 of this section, an expatriate managerial person (including a non-resident Indian) shall be eligible to the following perquisites which shall not be included in the computation of the ceiling on remuneration specified in paragraph 1 of this section:

(a) *Children's education allowance:* In case of children studying in or outside India, an allowance limited to a maximum of Rs.5,000 per month per child or actual expenses incurred, whichever is less. Such allowance is admissible upto a maximum of two children.

(b) *Holiday passage for children studying outside India/ family staying abroad:* Return holiday passage once in a year by economy class or once in two years by first class to children and to the members of the family from the place of their study or stay abroad to India if they are not residing in India with the managerial person.

(c) *Leave travel concession:* Return passage for self and family in accordance with the rules specified by the company where it is proposed that the leave be spent in home country instead of anywhere in India.

Explanation I

For the purposes of section II of this Part, "effective capital" means the aggregate of the paid-up share capital (excluding share application money or advances against shares); amount, if any, for the time being standing to the credit of share premium account; reserves and surplus (excluding revaluation reserve); long-term loans and deposits repayable after one year (excluding working capital loans, over-drafts, interest due on loans unless funded, bank guarantee, etc., and other short-term arrangements) as reduced by the aggregate of any investments (except in the case of investment by an investment company whose principal business is acquisition of shares, stock debentures or other securities), accumulated losses and preliminary expenses not written off.

Explanation II

(a) Where the appointment of the managerial person is made in the year in which company has been incorporated, the effective capital shall be calculated as on the date of such appointment;

(b) In any other case, the effective capital shall be calculated as on the last date of the financial year preceding the financial year in which the appointment of the managerial person is made.

Explanation III

For the purposes of section II of this Part, family means the spouse, dependent children and dependent parents of the managerial person.

Explanation IV

For the purposes of this section, "Remuneration Committee" means that a committee which consists of at least three non-executive independent directors including nominee director or nominee directors, if any.

Explanation V

For the purposes of this clause, the Remuneration Committee while approving the remuneration under this section, shall,-

(a) take into account, financial position of the company, trend in the industry, appointee's qualification, experience, past performance, past remuneration etc.

(b) be in a position to bring about objectivity in determining the remuneration package while striking a balance

between the interest of the company and the shareholders.

Explanation VI

For the purposes of Paragraph 1, " negative effective capital" means the effective capital which is calculated:-

(a) in accordance with the provisions contained in Explanation I of this Part;

(b) less than zero".

Section III — Remuneration payable to a managerial person in two companies

Subject to the provisions of section I and II, a managerial person shall draw remuneration from one or both companies, provided that the total remuneration drawn from the companies does not exceed the higher maximum limit admissible from any one of the companies of which he is a managerial person.

PART III — Provisions applicable to Parts I and II of this Schedule

1. The appointment and remuneration referred to in Parts I and II of this Schedule shall be subject to approval by a resolution of the shareholders in general meeting.

2. The auditor or the secretary of the company or where the company has not appointed a secretary, a secretary in whole-time practice shall certify that the requirements of this Schedule have been complied with and such certificate shall be incorporated in the return filed with the Registrar under sub-section (2) of section 269.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 24 Rules for Valuing Perquisites Provided by the Employer for the Purpose of Calculating Income Under the Head "Salaries"

For the purpose of computing the income chargeable under the head "Salaries", the value of perquisites provided by the employer directly or indirectly to the assessee (hereinafter referred to as employee) or to any member of his household by reason of his employment shall be determined in accordance with the following sub-rules, namely:—

(1) The value of residential accommodation provided by the employer during the previous year shall be determined on the basis provided in the Table below:

Table

Sl. No.	Circumstances	Where accommodation is unfurnished	Where accommodation is furnished
(1)	(2)	(3)	(4)
(1)	Where the accommodation is provided by the Central Government or any State Government to the employees either holding office or post in connection with the affairs of the Union or of such State or serving with any body or undertaking under the control of such Government on deputation.	Licence fee determined by the Central Government or any State Government in respect of accommodation in accordance with the rules framed by such Government as reduced by the rent actually paid by the employee.	The value of perquisite as determined under column (3) and increased by 10% per annum of the cost of furniture (including television sets, radio sets, refrigerators, other household appliances, air-conditioning plant or equipment) or if such furniture is hired from a third party, the actual hire charges payable for the same as reduced by any charges paid or payable for the same by the employee during the previous year.
(2)	Where the accommodation is provided by any other employer and— (a) where the accommodation is owned by the employer, or	(i) 15% of salary in cities having population exceeding 25 lakhs as per 2001 census;	The value of perquisite as determined under column (3) and increased by 10% per annum of the cost of furniture (including television sets, radio sets, refrigerators, other household appliances, air-conditioning plant or equipment or other similar appliances or gadgets) or if such furniture is hired from a

			third party, by the actual hire charges payable for the same as reduced by any charges paid or payable for the same by the employee during the previous year.
		(ii) 10% of salary in cities having population exceeding 10 lakhs but not exceeding 25 lakhs as per 2001 census; (iii) 7.5% of salary in other areas, in respect of the period during which the said accommodation was occupied by the employee during the previous year as reduced by the rent, if any, actually paid by the employee.	
	(b) where the accommodation is taken on lease or rent by the employer.	Actual amount of lease rental paid or payable by the employer or 15% of salary whichever is lower as reduced by the rent, if any, actually paid by the employee.	The value of perquisite as determined under column (3) and increased by 10% per annum of the cost of furniture (including television sets, radio sets, refrigerators, other household appliances, air-conditioning plant or equipment or other similar appliances or gadgets) or if such furniture is hired from a third party, by the actual hire charges payable for the same as reduced by any charges paid or payable for the same by the employee during the previous year.
	(3) Where the accommodation is provided by the employer specified in serial number (1) or (2) above in a hotel (except where the employee is provided such accommodation for a period not exceeding in aggregate 15 days on his transfer from one place to another)	Not applicable.	24% of salary paid or payable for the previous year or the actual charges paid or payable to such hotel, which is lower, for the period during which such accommodation is provided as reduced by the rent, if any, actually paid or payable by the employee]:

Provided that nothing contained in this sub-rule shall apply to any accommodation provided to an employee working at a mining site or an on-shore oil exploration site or a project execution site, or a dam site or a power generation site or an off-shore site which,—

(i) being of a temporary nature and having plinth area not exceeding 800 square feet, is located not less than eight kilometers away from the local limits of any municipality or a cantonment board; or

(ii) is located in a remote area:

Provided further that where on account of his transfer from one place to another, the employee is provided with accommodation at the new place of posting while retaining the accommodation at the other place, the value of perquisite shall be determined with reference to only one such accommodation which has the lower value with reference to the Table above for a period not exceeding 90 days and thereafter the value of perquisite shall be charged for both such accommodations in accordance with the Table.

(2) (A) The value of perquisite provided by way of use of motor car to an employee by an employer, who is not liable to pay fringe benefit tax under Chapter XII-H of the Act, shall be determined in accordance with the following Table, namely:—

TABLE II
VALUE OF PERQUISITE PER CALENDAR MONTH

Sl. No.	Circumstances	Where cubic capacity of	Where cubic capacity of engine

		engine does not exceed 1.6 litres	exceeds 1.6 litres
(1)	(2)	(3)	(4)
(1)	Where the motor car is owned or hired by the employer and—	No value: Provided that the documents specified in clause (B) of this sub-rule are maintained by the employer. Actual amount of expenditure incurred by the employer on the running and maintenance of motor car during the relevant previous year including remuneration, if any, paid by the employer to the chauffeur as increased by the amount representing normal wear and tear of the motor car and as reduced by any amount charged from the employee for such use.	No value: Provided that the documents specified in clause (B) of this sub-rule are maintained by the employer. Actual amount of expenditure incurred by the employer on the running and maintenance of motor car during the relevant previous year including remuneration, if any, paid by the employer to the chauffeur as increased by the amount representing normal wear and tear of the motor car and as reduced by any amount charged from the employee for such use.
(a)	is used wholly and exclusively in the performance of his official duties;		
(b)	is used exclusively for the private or personal purposes of the employee or any member of his household and the running and maintenance expenses are met or reimbursed by the employer;		
(c)	is used partly in the performance of duties and partly for private or personal purposes of his own or any member of his household and		
	(i) the expenses on maintenance and running are met or reimbursed by the employer,	Rs. 1,200 (plus Rs. 600, if chauffeur is also provided to run the motor car)	Rs. 1,600 (plus Rs. 600, if chauffeur is also provided to run the motor car)
	(ii) the expenses on running and maintenance for such private or personal use are fully met by the assessee.	Rs. 400 (plus Rs. 600, if chauffeur is also provided by the employer to run the motor car)	Rs. 600 (plus Rs. 600, if chauffeur is also provided to run the motor car)
(2)	Where the employee owns a motor car but the actual running and maintenance charges (including remuneration of the chauffeur, if any) are met or reimbursed to him by the employer and		
	(i) such reimbursement is for the use of the vehicle wholly and exclusively for official purposes,	No value: Provided that the documents specified in clause (B) of this sub-rule are maintained by the employer.	No value: Provided that the documents specified in clause (B) of this sub-rule are maintained by the employer.
	(ii) such reimbursement is for the use of the vehicle partly for official purposes and partly for personal or private purposes of the employee or any member of his household.	Subject to the provisions of clause (B) of this sub-rule, the actual payment of expenditure incurred by the employer as reduced by the amount's specified in Sl. No. (1)(c)(i) above	Subject to the provisions of clause (B) of this sub-rule, the actual payment of expenditure incurred by the employer as reduced by the amount's specified in Sl. No. (1)(c)(i) above

(3)	Where the employee owns any other automotive conveyance but the actual running and maintenance charges are met or reimbursed to him by the employer and (i) such reimbursement is for the use of the vehicle wholly and exclusively for official purposes, (ii) such reimbursement is for the use of the vehicle partly for official purposes and partly for personal or private purposes of the employee.	No value: Provided that the documents specified in clause (B) of this sub-rule are maintained by the employer. Subject to the provisions of clause (B) of this sub-rule, the actual payment of expenditure incurred by the employer as reduced by the amount's specified in Sl. No. (1)(c)(i) above	Not applicable

Provided that where one or more motor-cars are owned or hired by the employer and the employee or any member of his household are allowed the use of such motor-car or all or any of such motor-cars (otherwise than wholly and exclusively in the performance of his duties), the value of perquisite shall be the amount calculated in respect of one car in accordance with Sl. No. (1)(c)(i) of Table II as if the employee had been provided one motor-car for use partly in the performance of his duties and partly for his private or personal purposes and the amount calculated in respect of the other car or cars in accordance with Sl. No. (1)(b) of Table II as if he had been provided with such car or cars exclusively for his private or personal purposes.

(B) Where the employer or the employee claims that the motor-car is used wholly and exclusively in the performance of official duty or that the actual expenses on the running and maintenance of the motor-car owned by the employee for official purposes is more than the amounts deductible in Sl. No. 2(ii) or 3(iii) of Table II, he may claim a higher amount attributable to such official use and the value of perquisite in such a case shall be the actual amount of charges met or reimbursed by the employer as reduced by such higher amount attributable to official use of the vehicle provided that the following conditions are fulfilled:—

(a) the employer has maintained complete details of journey undertaken for official purpose which may include date of journey, destination, mileage, and the amount of expenditure incurred thereon;

(b) the employer gives a certificate to the effect that the expenditure was incurred wholly and exclusively for the performance of official duties.

***Explanation*.—For the purposes of this sub-rule, the normal wear and tear of a motor-car shall be taken at 10% per annum of the actual cost of the motor-car or cars.]**

(3) The value of benefit to the employee or any member of his household resulting from the provision by the employer of services of a sweeper, a gardener, a watchman or a personal attendant, shall be the actual cost to the employer. The actual cost in such a case shall be the total amount of salary paid or payable by the employer or any other person on his behalf for such services as reduced by any amount paid by the employee for such services.

(4) The value of the benefit to the employee resulting from the supply of gas, electric energy or water for his household consumption shall be determined as the sum equal to the amount paid on that account by the employer to the agency supplying the gas, electric energy or water. Where such supply is made from resources owned by the employer, without purchasing them from any other outside agency, the value of perquisite would be the manufacturing cost per unit incurred by the employer. Where the employee is paying any amount in respect of such services, the amount so paid shall be deducted from the value so arrived at.

(5) The value of benefit to the employee resulting from the provision of free or concessional educational facilities for any member of his household shall be determined as the sum equal to the amount of expenditure incurred by the employer in that behalf or where the educational institution is itself maintained and owned by the employer or where free educational facilities for such member of employees' household are allowed in any other educational institution by reason of his being in employment of that employer, the value of the perquisite to the employee shall be determined with reference to the cost of such education in a similar institution in or near the locality. Where any amount is paid or recovered from the employee on that account, the value of benefit shall be reduced by the amount so paid or recovered:

Provided that where the educational institution itself is maintained and owned by the employer and free educational facilities are provided to the children of the employee or where such free educational facilities are provided in any institution by reason of his being in employment of that employer, nothing contained in this sub-rule shall apply if the cost of such education or the value of such benefit per child does not exceed Rs. 1,000 p.m.

(6) The value of any benefit or amenity resulting from the provision by an employer, who is not liable to pay fringe benefit tax under Chapter XII-H of the Income-tax Act and is engaged in the carriage of passengers or goods to any employee or to any member of his household for personal or private journey free of cost or at concessional fare, in any conveyance owned, leased or made available by any other arrangement by such employer for the purpose of transport of passengers or goods shall be taken to be the value at which such benefit or amenity is offered by such

employer to the public as reduced by the amount, if any, paid by or recovered from the employee for such benefit or amenity:

Provided that nothing contained in this sub-rule shall apply to the employees of an airline or the railways.

(7) In terms of provisions contained in sub-clause (vi) of sub-section (2) of section 17, the following other fringe benefits or amenities are hereby prescribed and the value thereof shall be determined in the manner provided hereunder:

(i) The value of the benefit to the assessee resulting from the provision of interest-free or [concessional loan for any purpose made available to the employee or any member of his household during the relevant previous year by the employer or any person on his behalf shall be determined as the sum equal to the interest computed at the rate charged per annum by the State Bank of India, constituted under the State Bank of India Act, 1955 (23 of 1955), as on the 1st day of the relevant previous year in respect of loans for the same purpose advanced by it] on the maximum outstanding monthly balance as reduced by the interest, if any, actually paid by him or any such member of his household.

However, no value would be charged if such loans are made available for medical treatment in respect of diseases specified in rule 3A of these Rules or where the amount of loans are petty not exceeding in the aggregate Rs. 20,000:

Provided that where the benefit relates to the loans made available for medical treatment referred to above, the exemption so provided shall not apply to so much of the loan as has been reimbursed to the employee under any medical insurance scheme.

(ii) The value of travelling, touring, accommodation and any other expenses paid for or borne or reimbursed by the employer, who is not liable to pay fringe benefit tax under Chapter XII-H of the Act, for any holiday availed of by the employee or any member of his household, other than concession or assistance referred to in rule 2B of these rules, shall be determined as the sum equal to the amount of the expenditure incurred by such employer in that behalf. Where such facility is maintained by the employer, and is not available uniformly to all employees, the value of benefit shall be taken to be the value at which such facilities are offered by other agencies to the public. Where the employee is on official tour and the expenses are incurred in respect of any member of his household accompanying him, the amount of expenditure so incurred shall also be a fringe benefit or amenity. However, where any official tour is extended as a vacation, the value of such fringe benefit shall be limited to the expenses incurred in relation to such extended period of stay or vacation. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity.

(iii) The value of free food and non-alcoholic beverages provided by the employer, who is not liable to pay fringe benefit tax under Chapter XII-H of the Act, to an employee shall be the amount of expenditure incurred by such employer. The amount so determined shall be reduced by the amount, if any, paid or recovered from the employee for such benefit or amenity:

Provided that nothing contained in this sub-rule shall apply to free food and non-alcoholic beverages provided by such employer during working hours at office or business premises or through paid vouchers which are not transferable and usable only at eating joints, to the extent the value thereof in either case does not exceed Rs. 50 per meal or to tea or snacks provided during working hours or to free food and non-alcoholic beverages during working hours provided in a remote area or an off-shore installation.

(iv) The value of any gift, or voucher, or token in lieu of which such gift may be received by the employee or by member of his household on ceremonial occasions or otherwise from the employer, who is not liable to pay fringe benefit tax under Chapter XII-H of the Act, shall be determined as the sum equal to the amount of such gift. However, where the value of such gift, voucher or token, as the case may be, is below Rs. 5,000 in the aggregate during the previous year, the value of perquisite shall be taken as `nil'.

(v) The amount of expenses including membership fees and annual fees incurred by the employee or any member of his household, which is charged to a credit card (including any add-on-card), provided by the employer, who is not liable to pay fringe benefit tax under Chapter XII-H of the Act, or otherwise, paid for or reimbursed by such employer shall be taken to be the value of perquisite chargeable to tax. However, there shall be no value of such benefit where the expenses are incurred wholly and exclusively for official purposes and the following conditions are fulfilled—

(a) complete details in respect of such expenditure are maintained by the employer which may, inter alia, include the date of expenditure and the nature of expenditure;

(b) the employer gives a certificate for such expenditure to the effect that the same was incurred wholly and exclusively for the performance of official duties.

The amount so determined shall be reduced by the amount, if any paid or recovered from the employee for such benefit or amenity.

(vi) (A) The value of benefit to the employee resulting from the payment or reimbursement by the employer, who is not liable to pay fringe benefit tax under Chapter XII-H of the Act, of any expenditure incurred (including the amount of annual or periodical fee) in a club by him or by any member of his household shall be determined to be the actual amount of expenditure incurred or reimbursed by such employer on that account. The amount so determined shall be reduced by the amount, if any paid or recovered from the employee for such benefit or amenity. However, where the employer has obtained corporate membership of the club and the facility is

enjoyed by the employee or any member of his household, the value of perquisite shall not include the initial fee paid for acquiring such corporate membership.

(B) Nothing contained in this sub-rule shall apply if such expenditure is incurred wholly and exclusively for business purposes and the following conditions are fulfilled:—

(a) complete details in respect of such expenditure are maintained by the employer which may, inter alia, include the date of expenditure, the nature of expenditure and its business expediency;

(b) the employer gives a certificate for such expenditure to the effect that the same was incurred wholly and exclusively for the performance of official duties;

(c) nothing contained in this sub-rule shall apply for use of health club, sports and similar facilities provided uniformly to all employees by the employer.]

(vii) The value of benefit to the employee resulting from the use by the employee or any member of his household of any movable asset (other than assets already specified in this rule and other than laptops and computers) belonging to the employer or hired by him shall be determined at 10% per annum of the actual cost of such asset or the amount of rent or charge paid or payable by the employer, as the case may be, as reduced by the amount, if any, paid or recovered from the employee for such use.

(viii) The value of benefit to the employee arising from the transfer of any movable asset belonging to the employer directly or indirectly to the employee or any member of his household shall be determined to be the amount representing the actual cost of such asset to the employer as reduced by the cost of normal wear and tear calculated at the rate of 10% of such cost for each completed year during which such asset was put to use by the employer and as further reduced by the amount, if any, paid or recovered from the employee being the consideration for such transfer:

Provided that in the case of computers and electronic items, the normal wear and tear would be calculated at the rate of 50% and in the case of motor cars at the rate of 20% by the reducing balance method.

(ix) The value of any other benefit or amenity, service, right or privilege provided by the employer shall be determined on the basis of cost to the employer under an arm's length transaction as reduced by the employee's contribution, if any:

Provided that nothing contained in this item shall apply to the expenses on telephones including a mobile phone actually incurred on behalf of the employee by the employer.

(8) [***]

(9) This rule shall come into force with effect from the 1st day of April, 2001

Provided that the employee may, at his option, compute the value of all perquisites made available to him or any member of his household for the period beginning on 1st day of April, 2001 and ending on 30th day of September, 2001 in accordance with the Rules as they stood prior to this amendment:

[Provided further that for an employee being an employee of an airline [***], the provisions of sub-rule (6) shall come into force with effect from the 1st day of April, 2002.]

***Explanation*.—For the purposes of this rule—**

(i) "accommodation" includes a house, flat, farm house or part thereof, or accommodation in a hotel, motel, service apartment, guest house, caravan, mobile home, ship or other floating structure;

(ii) "entertainment" includes hospitality of any kind and also, expenditure on business gifts other than free samples of the employers own product with the aim of advertising to the general public;

(iii) "hotel" includes licensed accommodation in the nature of motel, service apartment or guest house;

(iv) "member of household" shall include—

(a) spouse(s)

(b) children and their spouses

(c) parents

(d) servants and dependants;

(v) "remote area", for purposes of proviso to this sub-rule means an area that is located at least 40 kilometres away from a town having a population not exceeding 20,000 based on latest published all-India census;

(vi) "salary" includes the pay, allowances, bonus or commission payable monthly or otherwise or any monetary payment, by whatever name called from one or more employers, as the case may be, but does not include the following, namely:—

(a) dearness allowance or dearness pay unless it enters into the computation of superannuation or retirement benefits of the employee concerned;

(b) employer's contribution to the provident fund account of the employee;

(c) allowances which are exempted from payment of tax;

(d) the value of perquisites specified in clause (2) of section 17 of the Income-tax Act;

(e) any payment or expenditure specifically excluded under proviso to sub-clause (iii) of clause (2) or proviso

to clause (2) of section 17;

(vii) "maximum outstanding monthly balance" means the aggregate outstanding balance for each loan as on the last day of each

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 25 Table of Indices for Computation of Long-Term Capital Gains

No.	Financial Year	Cost Inflation Index
1.	1981–82	100
2.	1982–83	109
3.	1983–84	116
4.	1984–85	125
5.	1985–86	133
6.	1986–87	140
7.	1987–88	150
8.	1988–89	161
9.	1989–90	172
10.	1990–91	182
11.	1991–92	199
12.	1992–93	223
13.	1993–94	244
14.	1994–95	259
15.	1995–96	281
16.	1996–97	305
17.	1997–98	331
18.	1998–99	351
19.	1999–00	389
20.	2000-01	406
21.	2001-02	426
22.	2002–03	447
23.	2003–04	463
24.	2004–05	480
25.	2005-06	497
26.	2006–07	519
27.	2007–08	551
28.	2008–09	582
29.	2009–10	632

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 26 Depreciation Table

APPENDIX I
[Effective from assessment year 2006-2007]
[See rule 5]

TABLE OF RATES AT WHICH DEPRECIATION IS ADMISSIBLE

Block of assets	Depreciation allowance as percentage of written down

		value
I. BUILDING [See Notes 1 to 4 below this Table]		
1	Buildings which are used mainly for residential purposes except hotels and boarding houses	5
2	Buildings other than those used mainly for residential purposes and not covered by sub-items (1) above and (3) below	10
3	Buildings acquired on or after the 1st day of September, 2002 for installing machinery and plant forming part of water supply project or water treatment system and which is put to use for the purpose of business of providing infrastructure facilities under clause (i) of subsection (4) of section 80-IA	100
4	Purely temporary erections such as wooden structures	100
II. FURNITURE AND FITTINGS		
	Furniture and fittings including electrical fittings [See Note 5 below this Table]	10
III. MACHINERY AND PLANT		
1	Machinery and plant other than those covered by sub-items (2), (3) and (8) below	15
2	Motor cars, other than those used in a business of running them on hire, acquired or put to use on or after 1st day of April, 1990	15
3	(i) Aeroplanes – aeroengines	40
	(ii) Motor buses, motor lorries and motor taxis used in a business of running them on hire	30
	(iii) Commercial vehicle acquired by the assessee on or after the 1st day of October, 1998 but before the 1st day of April, 1999 and put to use for any period before the 1st day of April, 1999 for the purposes of business or profession in accordance with the third proviso to clause (ii) of sub-section (1) of section 32 [See Note 6 below this Table]	40
	(iv) New commercial vehicle which is acquired on or after the 1st day of October, 1998 but before the 1st day of April, 1999 in replacement of condemned vehicle of over 15 years of age and is put to use for any period before the 1st day of April, 1999 for the purposes of business or profession in accordance with the third proviso to clause (ii) of section (1) of sub-section 32 [See Note 6 below this Table]	60
	(v) New commercial vehicle which is acquired on or after the 1st day of April, 1999 but before the 1st day of April, 2000 in replacement of condemned vehicle of over 15 years of age and is put to use before the 1st day of April, 2000 for the purposes of business or profession in accordance with the second proviso to clause (ii) of sub-section (1) of section 32 [See Note 6 below this Table]	60
	(vi) New commercial vehicle which is acquired on or after the 1st day of April, 2001 but before the 1st day of April, 2002 and is put to use before the 1st day of April, 2002 for the purposes of business or profession [See Note 6 below this Table]	50
	(vii) Moulds used in rubber and plastic goods factories	30
	(viii) Air pollution control equipment, being —	
	a. Electrostatic precipitation systems	
	b. Felt-filter systems	
	c. Dust collector systems	100
	d. Scrubber-counter current/venturi/packed bed/cyclonic scrubbers	
	e. Ash handling system and evacuation system	
	(ix) Water pollution control equipment, being —	
	a. Mechanical screen systems	
	b. Aerated detritus chambers (including air compressor)	
	c. Mechanically skimmed oil and grease removal systems	
	d. Chemical feed systems and flash mixing equipment	
	e. Mechanical flocculators and mechanical reactors	
	f. Diffused air/mechanically aerated activated sludge systems	
	g. Aerated lagoon systems	
	h. Biofilters	100

	i. Methane-recovery anaerobic digester systems	
	j. Air flotation systems	
	k. Air/steam stripping systems	
	l. Urea Hydrolysis systems	
	m. Marine outfall systems	
	n. Centrifuge for dewatering sludge	
	o. Rotating biological contractor or bio disc	
	p. Ion exchange resin column	
	q. Activated carbon column	
	(x) a. Solid waste control equipment, being — caustic / lime / chrome / mineral / cryolite recovery systems,	100
	b. Solid waste recycling and resource recovery systems	
	(xi) Machinery and plant, used in semi-conductor industry covering all integrated circuits (ICs) (excluding hybrid integrated circuits) ranging from small scale integration (SSI) to large scale integration/very large scale integration (LSI/VLSI) as also discrete semi-conductor devices such as diodes, transistors, thyristors, triacs, etc., other than those covered by entries (viii), (ix) and (x) of this sub-item and sub-item (8) below	30
	(xia) Life saving medical equipment, being —	40
	(i) D.C. Defibrillators for internal use an pace makers	
	(ii) Haemodialysors	
	(iii) Heart lung machine	
	(iv) Cobalt Therapy Unit	
	(v) Colour Doppler	
	(vi) SPECT Gamma Camera	
	(vii) Vascular Angiography System including Digital Subtraction Angiography	
	(viii) Ventilator used with anesthesia apparatus	
	(ix) Magnetic Resonance Imaging System	
	(x) Surgical Laser	
	(xi) Ventilator other than those used with anesthesia	
	(xii) Gamma knife	
	(xiii) Bone marrow transplant equipment including silastic long standing intervenous catheters for chemotherapy	
	(xiv) Fibreoptic endorscopes including, Paediatric resectoscope/audit resectoscope, Peritoneoscopes, Arthoscope, Microlaryngoscope, Fibreoptic Flexible Nasal Pharyngo Bronchoscope, Fibreoptic Flexible Laryngo Bronchoscope, Video Laryngo Bronchoscope and Video Oesophago Gastroscope, Stroboscope, Fibreoptic Flexible Oesophago Gastroscope	
	(xv) Laparoscope (single incision)	
4	Containers made of glass or plastic used as refills	50
5	Computers including computer software [See Note 7 below this Table]	60
6	Machinery and plant, used in weaving, processing and garment sector of textile industry, which is purchased under TUFS on or after the 1st day of April, 2001 but before the 1st day of April, 2004 and is put to use before the 1st day of April, 2004 [See Note 8 below this Table]	50
7	Machinery and plant, acquired and installed on or after the 1st day of September, 2002 in a water supply project or a water treatment system and which is put to use for the purpose of business of providing infrastructure facility under clause (i) of sub-section (4) of section 80-IA [See Notes 4 and 9 below this Table]	100
8	(i) Wooden Parts used in artificial silk manufacturing machinery	100
	(ii) Cinematograph films — bulbs of studio lights	
	(iii) Match factories — Wooden match frames	
	(iv) Mines and quarries	
	(a) Tubs winding ropes, haulage ropes and sand stowing pipes	
	(b) Safety lamps	
	(v) Salt works	
	(vi) Flour mills — Rollers	80

	(vii) Iron and steel industry — Rolling mill rolls	
	(viii) Sugar works — Rollers	
	(ix) Energy saving devices, being	
	A. Specialized boilers and furnaces:	80
	(a) Ignifluid/fluidized bed boilers	
	(b) Flameless furnaces and continuous pusher type furnaces	
	(c) Fluidized bed type heat treatment furnaces	
	(d) High efficiency boilers (thermal efficiency higher than 75 per cent in case of coal fired and 80 per cent in case of oil/gas fired boilers)	
	B. Instrumentation and monitoring systems for monitoring energy flows:	80
	(a) Automatic electrical load monitoring systems	
	(b) Digital heat loss meters	
	(c) Micro-processor based control systems	
	(d) Infra-red thermography	
	(e) Meters for measuring heat losses, furnace oil flow, steam flow, electric maximum demand indicator and clamp on power meters	
	(f) Maximum demand indicator and clamp on power meters	
	(g) Exhaust gases analyzer	
	(h) Fuel oil Pump test bench	
	C. Waste heat recovery equipments	80
	(a) Economizers and feed water heaters	
	(b) Recuperators and air pre-heaters	
	(c) Heat pumps	
	(d) Thermal energy wheel for high and low temperature waste heat recovery	
	D. Co-generation systems	80
	(a) Back pressure pass out, controlled extraction, extraction-cum-condensing turbines for co-generation along with pressure boilers	
	(b) Vapor absorption refrigeration systems	
	(c) Organic ranking cycle power systems	
	(d) Low inlet pressure small steam turbines	
	E. Electrical equipment:	80
	(a) Shunt capacitors and synchronous condenser systems	
	(b) Automatic power cut off devices (relays) mounted on individual motors	
	(c) Automatic voltage controller	
	(d) Power factor controller for A.C. motors	
	(e) Solid state devices for controlling motor speeds	
	(f) Thermally energy-efficient stenters (which require 800 or less kilocalories of heat to evaporate one kilogram of water)	
	(g) Series compensation equipment	
	(h) Flexible AC Transmission (FACT) devices — Thyristor controlled series compensation equipment	
	(i) Time of Day (ToD) energy meters	
	(j) Equipment to establish transmission highway for National Power Grid to facilitate transfer of surplus power of one region to the deficient region	
	(k) Remote terminal units/intelligent electronic devices, computer hardware/software, router/bridges, other required equipment and associated communication systems for supervisory control and data acquisition systems, energy management systems and distribution management systems for power transmission systems	
	(l) Special energy meters for Availability Based Tariff (ABT)	
	F. Burners:	80
	(a) 0 to 10 per cent excess air burners	
	(b) Emulsion burners	
	(c) Burner using air with high pre-heat temperature (above 300^{O}C)	
	G. Other equipment:	80
	(a) Wet air oxidation equipment for recovery of chemicals and heat	
	(b) Mechanical vapor recompressors	

	(c) Thin film evaporators	
	(d) Automatic microprocessor based load demand controllers	
	(e) Coal based producer gas plants	
	(f) Fluid drives and fluid couplings	
	(g) Turbo charges/super-charges	
	(h) Sealed radiation sources for radiation processing plants	
	(x) Gas Cylinders including valves and regulators	60
	(xi) Glass manufacturing concerns — Direct fire glass melting furnaces	60
	(xii) Mineral oil concerns:	60
	(a) Plant used in field operations (above ground) distribution — Returnable packages	
	(b) Plant used in field operations (below ground), but not including kerbside pumps including under ground tanks and fittings used in field operations (distribution) by mineral oil concerns	
	(xiii) Renewable energy devices being —	80
	(a) Flat plate solar collectors	
	(b) Concentrating and pipe type solar collectors	
	(c) Solar cookers	
	(d) Solar water heaters and systems	
	(e) Air/Gas/fluid heating systems	
	(f) Solar crop criers and systems	
	(g) Solar refrigeration, cold storages and air conditioning systems	
	(h) Solar steels and desalination systems	
	(i) Solar power generating systems	
	(j) Solar pumps based on solar-thermal and solar-photovoltaic conversion	
	(k) Solar-photovoltaic modules and panels for water pumping and other applications	
	(l) Wind mills and any specially designed devices which run on wind mills	
	(m) Any special devices including electric generators and pumps running on wind energy	
	(n) Biogas-plant and biogas-engines	
	(o) Electrically operated vehicles including battery powered or fuel-cell powered vehicles	
	(p) Agricultural and municipal waste conversion devices producing energy	
	(q) Equipment for utilizing ocean waste and thermal energy	
	(r) Machinery and plant used in the manufacture of any of the above sub-items	
9	(i) Books owned by assessees carrying on a profession —	
	(a) Books, being annual publications	100
	(b) Books, other than those covered by entry (a) above	60
	(ii) Books, owned by assessees carrying on business in running lending libraries	100
IV. SHIPS		
1	Ocean-going ships, including dredgers, tugs, barges, survey launches and other similar ships used mainly for dredging purposes and fishing vessels with wooden hulls	20
2	Vessels ordinarily operating on inland waters, not covered by sub-item 3 below	20
3	Vessels ordinarily operating on inland waters being speed boats [See Note 10 below this Table]	25
	PART B INTANGIBLE ASSETS	
	Know-how, patents, copyrights, trademarks, licenses, franchises, or any other business or commercial rights of similar nature.	25

Notes

1. "Buildings" include roads, bridges, culverts, wells and tubewells.

2. A building shall be deemed to be a building used mainly for residential purposes, if the built-up floor area thereof

used for residential purposes is not less than sixty-six and two-third percent of its total built-up floor area and shall include any such building in the factory premises.

3. In respect of any structure or work by way of renovation or improvement in or in relation to a building referred to in Explanation I of clause (ii) of subsection (1) of section 32, the percentage to be applied will be the percentage specified against sub-item (1) or (2) of item 1, as may be appropriate to the class of building in or in relation to which the renovation or improvement is effected. Where the structure is constructed or the work is done by way of extension of any such building, the percentage to be applied would be such percentage as would be appropriate, as if the structure or work constituted a separate building.

4. Water treatment system includes system for desalination, demineralisation and purification of water.

5. "Electrical fittings" include electrical wiring, switches, sockets, other fittings and fans, etc.

6. "Commercial vehicle" means "heavy goods vehicle", "heavy passenger motor vehicle", "light motor vehicle", "medium goods vehicle" and "medium passenger motor vehicle" but does not include "maxi-cab", "motor-cab", "tractor" and "road-roller". The expressions "heavy goods vehicle", "heavy passenger motor vehicle", "light motor vehicle", "medium goods vehicle", "medium passenger motor vehicle", "maxi-cab", "motor-cab", "tractor" and "road-roller" shall have the meanings respectively assigned to them in section 2 of the Motor Vehicles Act, 1988 (59 of 1988).

7. "Computer software" means any computer program recorded on any disc, tape, perforated media or other information storage device.

8. "TUFS" means Technology Upgradation Fund Scheme announced by the Government of India in the form of a Resolution of the Ministry of Textiles vide no. 28/1/99-CTI of 31.3.1999.

9. Machinery and plant include pipes needed for delivery from the source of supply of raw water to the plant and from the plant to the storage facility.

10. "Speed boat" means a motor boat driven by a high speed internal combustion engine capable of propelling the boat at a speed exceeding 24 kilometers per hour in still water and so designed that when running at a speed, it will plane, i.e, its bow will rise from the water.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 27 Depreciation Table — Assets of an Undertaking Engaged in Generation or Generation and Distribution of Power

Appendix 1-A Table of rates at which depreciation is admissible

[See Rule 5(1A)]

Class of assets	Depreciation allowance as percentage of actual cost
1	2
a. Plant and machinery in generating stations including plant foundations:	
i. Hydro-electric	3.40
ii. Steam electric NHRS and waste heat recovery boilers/plants	7.84
iii. Diesel electric and gas plant	8.24
b. Cooling towers and circulating water systems	7.84
c. Hydraulic works forming part of hydro-electric system including:	
i. Dams, spillways, weirs, canals, reinforced concrete flumes and syphons	1.95
ii. Reinforced concrete pipelines and surge tanks, steel pipelines, sluice gates,	
steel surge (tanks), hydraulic control valves and other hydraulic works	3.40
d. Building and civil engineering works of permanent character, not mentioned above	
i. Offices and showrooms	3.02
ii. Containing thermo-electric generating plant	7.84
iii. Containing hydro-electric generating plant	3.40
iv. Temporary erections such as wooden structures	33.40
v. Roads other than kutcha roads	3.02
vi. Others	3.02
e. Transformers, transformer (kiosk) sub-station equipment and other fixed	

apparatus (including plant foundations)	
i. Transformers (including foundations) having a rating of 100 kilo volt amperes and over	7.81
ii. Others	7.84
f. Switchgear including cable connections	7.84
g. Lightning arrestor:	
i. Station type	7.84
ii. Pole type	12.77
iii. Synchronous condenser	5.27
h. Batteries	33.40
i. Underground cable including joint boxes and disconnectioned boxes	5.27
ii. Cable duct system	3.02
i. Overhead lines including supports:	
i. Lines on fabricated steel operating at nomina voltages higher than 66 kilovolts	5.27
ii. Lines on steel supports operating at nominal voltages higher than 13.2 kilovolts	
but not exceeding 66 kilovolts	7.84
iii. Lines on steel or reinforced concrete supports	7.84
iv. Lines on treated wood supports	7.84
j. Metres	12.77
k. Self propelled vehicles	33.40
l. Air conditioning plant	
i. Static	12.77
ii. Portable	33.40
m. i. Office furniture and fittings	12.77
ii. Office equipment	12.77
iii. Internal wiring including fittings and apparatus	12.77
iv. Street light fittings	12.77
n. Apparatus let on hire	
i. Other than motors	33.40
ii. Motors	12.77
o. Communication equipment	
i. Radio and high frequency carrier system	12.77
ii. Telephone lines and telephones	12.77
p. Any other assets not covered above	7.69

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 28 The Eleventh Schedule, Income Tax Act, 1961
List of Articles or Things

1. Beer, wine and other alcoholic spirits.

2. Tobacco and tobacco preparations, such as cigars and cheroots, cigarettes, biris, smoking mixtures for pipes and cigarettes, chewing tobacco and snuff.

3. Cosmetics and toilet preparations.

4. Tooth paste, dental cream, tooth powder and soap.

5. Aerated waters in the manufacture of which blended flavoring concentrates in any form are used.

Explanation — "Blended flavoring concentrates" shall include, and shall be deemed always to have included, synthetic essences in any form.

6. Confectionery and chocolates.

7. Gramophones, including record players, and gramophone records.

8. [Omitted by the Finance Act 1981, with effect from April 1, 1982.]

9. Projectors.

10. Photographic apparatus and goods.

11. – 21. [Omitted by the Finance Act 1981, with effect from April 1, 1982.]

22. Office machines and apparatus such as typewriters, calculating machines, cash registering machines, cheque writing machines, intercom machines and teleprinters.

Explanation — The expression "office machines and apparatus" includes all machines and apparatus used in offices, shops, factories, workshops, educational institutions, railway stations, hotels and restaurants for doing office work and for data processing (not being computers within the meaning of section 32AB)

23. Steel furniture, whether made partly or wholly of steel.

24. Safes, strong boxes, cash and deed boxes, and strong room doors.

25. Latex foam sponge and polyurethane foam.

26. Crown corks, or other fittings of cork, rubber, polyethylene or any other material.

27. Pilfer-proof caps for packaging or other fittings of cork, rubber, polyethylene or any other material.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 29 The Eighth Schedule, Income Tax Act, 1961
List of Industrially Backward States and Union Territories

(1) Arunachal Pradesh

(2) Assam

(3) Goa

(4) Himachal Pradesh

(5) Jammu and Kashmir

(6) Manipur

(7) Meghalaya

(8) Mizoram

(9) Nagaland

(10) Sikkim

(11) Tripura

(12) Andaman and Nicobar Islands

(13) Dadra and Nagar Haveli

(14) Daman and Diu

(15) Lakshadweep

(16) Pondicherry

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 30 The Thirteenth Schedule, Income Tax Act, 1961
List of Articles or Things

PART A
FOR THE STATE OF SIKKIM

S. No.	*Article or thing*
1.	Tobacco and tobacco products (including cigarettes, cigars and gutka, etc.)
2.	Aerated branded beverages
3.	Pollution-causing paper and paper products

PART B

FOR THE STATE OF HIMACHAL PRADESH AND THE STATE OF UTTARANCHAL

S. No.	*Activity or article or thing*	*Excise classification*	*Sub-class under National Industrial Classification (NIC), 1998*
1.	Tobacco and tobacco products including cigarettes and pan masala	24.01 to 24.04 and 21.06	1600
2.	Thermal Power Plant (coal/oil based)		40102 or 40103
3.	Coal washeries/dry coal processing		
4.	Inorganic Chemicals excluding medicinal grade oxygen (2804.11), medicinal grade hydrogen peroxide (2847.11), compressed air (2851.30)	Chapter 28	
5.	Organic chemicals excluding Provitamins/ vitamins, Hormones (29.36), Glycosides (29.39), sugars* (29.40)	Chapter 29	24117
6.	Tanning and dyeing extracts, tannins and their derivatives, dyes, colours, paints and varnishes; putty, fillers and other mastics; inks	Chapter 32	24113 or 24114
7.	Marble and mineral substances not classified elsewhere	25.04 25.05	14106 or 14107
8.	Flour mills/rice mills	11.01	15311
9.	Foundries using coal		
10.	Minerals fuels, mineral oils and products of their distillation; bituminous substances: mineral waxes	Chapter 27	
11.	Synthetic rubber products	40.02	24131
12.	Cement clinkers and asbestos, raw including fibre	2502.10, 2503.00	
13.	Explosive (including industrial explosives, detonators and fuses, fireworks, matches, propellant powders, etc.)	36.01 to 36.06	24292
14.	Mineral or chemical fertilizers 3	1.02 to 31.05	2412
15.	Insecticides, fungicides, herbicides and pesticides (basic manufacture and formulation)	3808.10	24211 or 24219
16.	Fibre glass and articles thereof	70.14	26102
17.	Manufacture of pulp—wood pulp, mechanical or chemical (including dissolving pulp)	47.01	21011
18.	Branded aerated water/soft drinks (non-fruit based)	2201.20, 2202.20	15541 or 15542
19.	Paper	4801	21011 to 21019
	Writing or printing paper, etc.	4802.10	
	Paper or paperboard, etc.	4802.20	
	Maplitho paper, etc.	4802.30	
	Newsprint, in rolls or sheets	4801.00	
	Craft paper, etc.	4804.10	
	Sanitary towels, etc.	4818.10	
	Cigarette paper	48.13	
	Grease-proof paper	4806.10	
	Toilet or facial tissue, etc.	4803	
	Paper and paper board, laminated internally with bitumen, tar or asphalt	4807.10	
	Carbon or similar copying paper	4809.10	
	Products consisting of sheets of paper or paperboard, impregnated, coated or covered with plastics, etc.		4811.20
	Paper and paperboard, coated, impregnated or covered with wax, etc.	4811.40	

	The following S. No. 19 and entries relating thereto shall be substituted for the existing S. No. 19 of Thirteenth Schedule by the Finance (No. 2) Act, 2009, w.e.f. 1-4-2010:		
19.	**Manufacture of pulp-wood pulp, mechanical or chemical (including dissolving pulp)**	**4701.00**	
	Newsprint in rolls or sheets	**4801.00**	
	Writing or printing paper for printing of educational textbooks	**4802.10**	
	Paper or paper board, in the manufacture of which—	**4802.20**	
	(a) the principal process of lifting the pulp is done by hand; and		
	(b) if power driven sheet forming equipment is used, the Cylinder Mould Vat does not exceeds 40 inches		
	Maplitho paper supplied to a Braille press against an indent placed by the National Institute for Visually Handicapped, Dehradun	**4802.30**	
	Others	**4802.90**	
	Toilet or facial tissue stock, towel or napkin stock and similar paper of a kind used for household or sanitary purposes, cellulose wadding and webs of cellulose fibres, whether or not creped, crinkled embossed, perforated, surfact-coloured, surface decorated or printed, in rolls of a width exceeding 36 cms or in rectangular (including square) sheets with at least one side exceeding 36 cms. in unfolded state.	**4803.00**	
	Kraft paper supplied to a Braille press against an indent placed by the National Institute for Visually Handicapped, Dehradun	**4804.10**	
	Kraft paper and paperboard used in the manufacture of cartons for packing of horticultural produce	**4804.20**	
	Others	**4804.90**	
	Other uncoated paper and paperboard, in roll or sheets, not further worked or processed than as specified in Note 2 to this Chapter.	**4805.00**	
	Grease-proof paper	**4806.10**	
	Glassine and other glazed transparent or translucent paper	**4806.20**	
	Others	**4806.90**	
	Straw Board, in the manufacture of which sun-drying process has been employed.	**4807.91**	
	Straw paper and other straw board, whether or not covered with paper other than straw paper.	**4807.92**	
	Other	**4807.99**	
	Carbon or similar copying papers	**4809.10**	
	Self-copy paper	**4809.20**	
	Others	**4809.90**	
	Paper and paperboard of a kind used for writing, printing or other graphic purposes.	**4810.10**	
	Kraft paper and paperboard other than that of a kind used for writing, printing or other graphic purposes.	**4810.20**	
	Other paper and paperboard	**4810.90**	
	Tarred, bituminized or asphalted paper and paperboard.	**4811.10**	
	Gummed or adhesive paper and paper-board	**4811.20**	

	Paper and paperboard coated, impregnated or covered with plastic (excluding adhesives).		
	Products consisting of sheets of paper or paperboard, impregnated, coated or covered with plastics (including thermoset resins or mixtures thereof or chemical formulations containing melamine, phenol, urea formaldehyde with or without curing agents or catalysts), compressed together in one or more operations; Products known commercially as decorative laminates.	4811.31	
	Others	4811.39	
	Paper and paperboard, coated, impregnated or covered with wax, paraffin wax, stearin, oil or glycerol.	4811.40	
	Other	4811.90	
	Cigarette paper, whether or not cut to size or in the form of booklets or tubes.	4813.00.	
20.	Plastics and articles thereof	39.09 to 39.15]	

PART C

FOR THE STATE OF JAMMU AND KASHMIR

S. No.	*Article or thing*
1.	Cigarettes/cigars of tobacco, manufactured tobacco and substitutes
2.	Distilled/brewed alcoholic drinks
3.	Aerated branded beverages and their concentrates.]

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 31 The Fourteenth Schedule, Income Tax Act, 1961 List of Articles or Things or Operations

PART A

FOR THE NORTH-EASTERN STATES

1. Fruit and Vegetable Processing industries manufacturing or producing—

(i) Canned or bottled products;

(ii) Aseptic packaged products;

(iii) Frozen products;

(iv) De-hydrated products;

(v) Oleoresins.

2. Meat and Poultry Product industries manufacturing or producing—

(i) Meat Products (buffalo, sheep, goat and pork);

(ii) Poultry production;

(iii) Egg Powder Plant.

3. Cereal Based Product industries manufacturing or producing—

(i) Maize Milling including starch and its derivatives;

(ii) Bread, Biscuits, Breakfast Cereal.

4. Food and Beverage industries manufacturing or producing—

(i) Snacks;

(ii) Non-alcoholic beverages;

(iii) Confectionery including chocolate;

(iv) Pasta products;

(v) Processed spices, etc.;

(vi) Processed pulses;

(vii) Tapioca products.

5. Milk and milk based product industries manufacturing or producing—

(i) Milk powder;
(ii) Cheese;
(iii) Butter/ghee;
(iv) Infant food;
(v) Weaning food;
(vi) Malted milk food.

6. Food packaging industry.

7. Paper products industry.

8. Jute and mesta products industry.

9. Cattle or poultry or fishery feed products industry.

10. Edible Oil processing or vanaspati industry.

11. Processing of essential oils and fragrances industry.

12. Processing and raising of plantation crops—tea, rubber, coffee, coconuts, etc.

13. Gas based Intermediate Products Industry manufacturing or producing—

(i) Gas exploration and production;
(ii) Gas distribution and bottling;
(iii) Power generation;
(iv) Plastics;
(v) Yarn raw materials;
(vi) Fertilizers;
(vii) Methanol;
(viii) Formaldehyde and FR resin melamine and MF resin;
(ix) Methylamine, Hexamethylene tetramine, Ammonium bi-carbonate;
(x) Nitric Acid and Ammonium Nitrate;
(xi) Carbon black;
(xii) Polymer chips.

14. Agro forestry based industry.

15. Horticulture industry.

16. Mineral based industry.

17. Floriculture industry.

18. Agro-based industry.

PART B

FOR THE STATE OF SIKKIM

S. No.	*Activity or article or thing or operation*
1.	Eco-Tourism including Hotels, Resorts, Spa, Amusement Parks and Ropeways.
2.	Handicrafts and handlooms.
3.	Wool and silk reeling, weaving and processing, printing, etc.
4.	Floriculture.
5.	Precision Engineering including watch making.
6.	Electronics including computronics hardware and software and Information Technology (IT) related industries.
7.	Food processing including Agro-based industries. Processing, preservation and packaging of fruits and vegetables (excluding conventional grinding/extraction units).
8.	Medicinal and aromatic Herbs?Plantation and Processing.
9.	Raising and processing of plantation crops, i.e., tea, oranges and carda-mom.
10.	Mineral based industry.
11.	Pharma products.
12.	Honey.

13.	Biotechnology.

PART C

FOR THE STATE OF HIMACHAL PRADESH AND THE STATE OF UTTARANCHAL

S. No.	*Activity or article or thing or operation*	*4/6 digit excise classification*	*Sub-class under NIC classification on 1998*	*ITC(HS) classification 4/6 digit*
1.	Floriculture	-	-	0603 or 060120 or 06029020 or 06024000
2.	Medicinal herbs and aromatic herbs, etc., processing	-	-	
3.	Honey	-	-	040900
4.	Horticulture and agro-based industries such as (a) Sauces, ketchup, etc. (b) Fruit juices and fruit pulp (c) Jams, jellies, vegetable juices, puree, pickles, etc. (d) Preserved fruits and vegetables (e) Processing of fresh fruits and vegetables including packaging (f) Processing, preservation, packaging of mushrooms	21.03 2202.40 20.01	15135 to 15137 and 15139	
5.	Food Processing Industry excluding those included in the Thirteenth Schedule	19.01 to 19.04		
6.	Sugar and its by-products	-	-	17019100
7.	Silk and silk products	50.04 50.05	17116	
8.	Wool and wool products	51.01 to 51.12	17117	
9.	Woven fabrics (Excisable garments)	-	-	6101 to 6117
10.	Sports goods and articles and equipment for general physical exercise and equipment for adventure sports/activities, tourism (to be specified, by notification, by the Central Government)	9506.00		
11.	Paper and paper products excluding those in the Thirteenth Schedule (as per excise classification)			
12.	Pharma products	30.03 to 30.05		
13.	Information and Communication Technology Industry, Computer hardware, Call Centres	84.71	30006/7	
14.	Bottling of mineral water	2201		
15.	Eco-tourism including hotels, resorts, spa, entertainment/ amusement parks and ropeways	-	55101	
16.	Industrial gases (based on atmospheric fraction)			
17.	Handicrafts			
18.	Non-timber forest product-based industries.]			

Working Papers

Worksheet 32 Form ITR-6 — Income Tax Return for Companies

Form ITR-6 — Income Tax Return for Companies

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 33 Form 34C — Application by a Nonresident for Obtaining an Advance Ruling Under Section 245Q(1) of the Income Tax Act, 1961

FORM NO. 34C

[*See* rule 44E]

Form of application for obtaining an advance ruling under section 245Q(1) of the Income-tax Act, 1961

(PLEASE READ THE NOTES CAREFULLY BEFORE FILLING THIS FORM) BEFORE THE AUTHORITY FOR ADVANCE RULINGS

Application No. _ of _

1. Full name and address of the applicant

2. Telephone and Fax No.

3. Country of which he is resident

4. Status

5. Basis of claim for being a non-resident

6. The Commissioner having jurisdiction over the applicant (only in the case of existing assessees)

7. Permanent Account Number (only in the case of existing assessees)

8. Question(s) relating to the transaction on which the advance ruling is required

9. Statement of the relevant facts having a bearing on the aforesaid question(s)

10. Statement containing the applicant's interpretation of law or facts, as the case may be, in respect of the aforesaid question(s)

11. List of documents/statements attached

12. Particulars of account payee demand draft accompanying the application

13. Name and address of authorised representative in India, if any

Signed

(Applicant)

Verification

I, _____ [name in full and in block letters] son/daughter/wife of _____ do hereby solemnly declare that to the best of my knowledge and belief what is stated above and in the annexure(s), including the documents accompanying such annexure(s), is correct and complete. I further declare that I am making this application in my capacity as _____ (designation) and that I am competent to make this application and verify it.

I also declare that the question on which the advance ruling is required is not pending in my case before any income-tax authority, the Appellate Tribunal or any court.

Verified today the _____ day of _____

Place _____

Signed

(Applicant)

Notes:

1. The application must be filled in English or Hindi in quadruplicate.

2. The number and year of receipt of the application will be filled in the office of the Authority for Advance Rulings.

3. If the space provided for answering any item in the application is found insufficient, separate enclosures may be

used for the purpose. These should be signed by the applicant.

4. The application must be accompanied by an account payee demand draft of two thousand five hundred Indian rupees drawn in favour of Authority for Advance Rulings, payable at New Delhi. Particulars of the draft should be given in reply to item No. 12.

5. In reply to item No. 3, if the applicant is a company, association of persons or Hindu undivided family, etc., the country of residence thereof is to be given and not of the individual who is filing the application on behalf of such person.

6. In reply to item No. 4, the applicant must state whether he/it is an individual, Hindu undivided family, firm, association of persons or company.

7. For item No. 5, the reply must be given in the context of the provisions regarding `residence' in India as contained in section 6 of the Income-tax Act. The position in this regard is as follows:

An individual is said to be `resident' in any financial year, if he has been in India during that year:

- For a period or periods of 182 days or more ; or

- For a period or periods of 60 days or more and has also been in India within the preceding four years for a period or periods of 365 days or more.

However, the period of 60 days is increased to 150 days in the case of a citizen of India or a person of Indian origin who has been outside India and comes on a visit to India, and to 182 days in a case when a citizen of India leaves India for purposes of employment outside India, or as a member of the crew of an Indian ship. An association of persons or a Hindu undivided family is resident in India in every case except where the control and management of its affairs is situated wholly outside India.

A company is resident in India, if it is an Indian company or the control and management of its affairs is situated wholly in India.

A person who is not resident in India as above, is non-resident in India.

8. Regarding item No. 8, the question(s) should be based on actual or proposed transactions. Hypothetical questions will not be entertained.

9. In respect of item No. 9, in Annexure I, the applicant must state in detail the relevant facts and also disclose the nature of his business or profession and the likely date and purpose of the proposed transaction(s).

Relevant facts reflected in documents submitted along with the application must be included in the statement of facts and not merely incorporated by reference.

10. For item No. 10, in Annexure II, the applicant must clearly state his interpretation of law or facts in respect of the question(s) on which the advance ruling has been sought.

11. The application, the verification appended thereto, the annexures to the application and the statements and documents accompanying the annexures, must be signed,-

(a) in the case of an individual,-

(i) by the individual himself, and

(ii) where, for any unavoidable reason, it is not possible for the individual to sign the application, by any person duly authorised by him in this behalf:

Provided that in a case referred to in sub-clause (ii), the person signing the application holds a valid power of attorney from the individual to do so, which shall be attached to the application;

(b) in the case of a Hindu undivided family,-

(i) by the karta thereof, and

(ii) where, for any unavoidable reason, it is not possible for the karta to sign the application, by any other adult member of such family;

(c) in the case of a company,-

(i) by the Managing Director thereof, or where for any unavoidable reason such Managing Director is not able to sign and verify the application, or where there is no Managing Director, by any Director thereof;

(ii) where, for any unavoidable reason, it is not possible for the Managing Director or the Director to sign the application, by any person duly authorised by the company in this behalf:

Provided that in the case referred to in sub-clause (ii), the person signing the application holds a valid power of attorney from the company to do so, which shall be attached to the application;

(d) in the case of a firm, by the managing partner thereof, or where for any unavoidable reason such managing partner is not able to sign and verify the application, or where there is no managing partner as such, by any partner thereof, not being a minor;

(e) in the case of an association of persons, by any member of the association or the principal officer thereof; and

(f) in the case of any other person, by that person or by some person competent to act on his behalf.

ANNEXURE I

Statement of the relevant facts having a bearing on the question(s) on which the advance ruling is required

_____

_____

Signed

(Applicant)

Place _____

Date _____

ANNEXURE II

Statement containing the applicant's interpretation of law or facts, as the case may be, in respect of the question(s) on which advance ruling is required

_____

_____

_____

Signed

(Applicant)

Place _____

Date _____

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 34 Rules for Determining Arm's Length Price, Information and Documents to Be Furnished Under Transfer Pricing Regulations Pursuant to Sections 92 to 92F of ITA

Rule 10A. Meaning of expressions used in computation of arm's length price.—For the purposes of this rule and rules 10B to 10E,—

(a) 'uncontrolled transaction' means a transaction between enterprises other than associated enterprises, whether resident or non-resident;

(b) 'property' includes goods, articles or things, and intangible property;

(c) 'services' include financial services;

(d) 'transaction' includes a number of closely linked transactions.

Rule 10B. Determination of arm's length price under section 92C.—

(1) For the purposes of sub-section (2) of section 92C, the arm's length price in relation to an international transaction shall be determined by any of the following methods, being the most appropriate method, in the following manner, namely:—

(a) comparable uncontrolled price method, by which,—

(i) the price charged or paid for property transferred or services provided in a comparable uncontrolled transaction, or a number of such transactions, is identified;

(ii) such price is adjusted to account for differences, if any, between the international transaction and the comparable uncontrolled transactions or between the enterprises entering into such transactions, which could materially affect the price in the open market;

(iii) the adjusted price arrived at under sub-clause (ii) is taken to be an arm's length price in respect of the property transferred or services provided in the international transaction;

(b) resale price method, by which,—

(i) the price at which property purchased or services obtained by the enterprise from an associated enterprise is resold or are provided to an unrelated enterprise, is identified;

(ii) such resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions;

(iii) the price so arrived at is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services;

(iv) the price so arrived at is adjusted to take into account the functional and other differences, including differences in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market;

(v) the adjusted price arrived at under sub-clause (iv) is taken to be an arm's length price in respect of the purchase of the property or obtaining of the services by the enterprise from the associated enterprise;

(c) cost plus method, by which,—

(i) the direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an associated enterprise, are determined;

(ii) the amount of a normal gross profit mark-up to such costs (computed according to the same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction, or a number of such transactions, is determined;

(iii) the normal gross profit mark-up referred to in sub-clause (ii) is adjusted to take into account the functional and other differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market;

(iv) the costs referred to in sub-clause (i) are increased by the adjusted profit mark-up arrived at under sub-clause (iii);

(v) the sum so arrived at is taken to be an arm's length price in relation to the supply of the property or provision of services by the enterprise;

(d) profit split method, which may be applicable mainly in international transactions involving transfer of unique intangibles or in multiple international transactions which are so inter-related that they cannot be evaluated separately for the purpose of determining the arm's length price of any one transaction, by which—

(i) the combined net profit of the associated enterprises arising from the international transaction in which they are engaged, is determined;

(ii) the relative contribution made by each of the associated enterprises to the earning of such combined net profit, is then evaluated on the basis of the functions performed, assets employed or to be employed and risks assumed by each enterprise and on the basis of reliable external market data which indicates how such contribution would be evaluated by unrelated enterprises performing comparable functions in similar circumstances;

(iii) the combined net profit is then split amongst the enterprises in proportion to their relative contributions, as evaluated under sub-clause (ii);

(iv) the profit thus apportioned to the assessee is taken into account to arrive at an arm's length price in relation to the international transaction:

Provided that the combined net profit referred to in sub-clause (i) may, in the first instance, be partially allocated to each enterprise so as to provide it with a basic return appropriate for the type of international transaction in which it is engaged, with reference to market returns achieved for similar types of transactions by independent enterprises, and thereafter, the residual net profit remaining after such allocation may be split amongst the enterprises in proportion to their relative contribution in the manner specified under sub-clauses (ii) and (iii), and in such a case the aggregate of the net profit allocated to the enterprise in the first instance together with the residual net profit apportioned to that enterprise on the basis of its relative contribution shall be taken to be the net profit arising to that enterprise from the international transaction;

(e) transactional net margin method, by which,—

(i) the net profit margin realised by the enterprise from an international transaction entered into with an associated enterprise is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;

(ii) the net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;

(iii) the net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;

(iv) the net profit margin realised by the enterprise and referred to in sub-clause (i) is established to be the same as the net profit margin referred to in sub-clause (iii);

(v) the net profit margin thus established is then taken into account to arrive at an arm's length price in relation to

the international transaction.

(2) For the purposes of sub-rule (1), the comparability of an international transaction with an uncontrolled transaction shall be judged with reference to the following, namely:—

(a) the specific characteristics of the property transferred or services provided in either transaction;

(b) the functions performed, taking into account assets employed or to be employed and the risks assumed, by the respective parties to the transactions;

(c) the contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions;

(d) conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, the laws and Government orders in force, costs of labour and capital in the markets, overall economic development and level of competition and whether the markets are wholesale or retail.

(3) An uncontrolled transaction shall be comparable to an international transaction if—

(i) none of the differences, if any, between the transactions being compared, or between the enterprises entering into such transactions are likely to materially affect the price or cost charged or paid in, or the profit arising from, such transactions in the open market; or

(ii) reasonably accurate adjustments can be made to eliminate the material effects of such differences.

(4) The data to be used in analysing the comparability of an uncontrolled transaction with an international transaction shall be the data relating to the financial year in which the international transaction has been entered into:

Provided that data relating to a period not being more than two years prior to such financial year may also be considered if such data reveals facts which could have an influence on the determination of transfer prices in relation to the transactions being compared.

Rule 10C. Most appropriate method.—

(1) For the purposes of sub-section (1) of section 92C, the most appropriate method shall be the method which is best suited to the facts and circumstances of each particular international transaction, and which provides the most reliable measure of an arm's length price in relation to the international transaction.

(2) In selecting the most appropriate method as specified in sub-rule (1), the following factors shall be taken into account, namely:—

(a) the nature and class of the international transaction;

(b) the class or classes of associated enterprises entering into the transaction and the functions performed by them taking into account assets employed or to be employed and risks assumed by such enter-prises;

(c) the availability, coverage and reliability of data necessary for application of the method;

(d) the degree of comparability existing between the international transaction and the uncontrolled transaction and between the enterprises entering into such transactions;

(e) the extent to which reliable and accurate adjustments can be made to account for differences, if any, between the international transaction and the comparable uncontrolled transaction or between the enterprises entering into such transactions;

(f) the nature, extent and reliability of assumptions required to be made in application of a method.

Rule 10D. Information and documents to be kept and maintained under section 92D.—

(1) Every person who has entered into an international transaction shall keep and maintain the following information and documents, namely:—

(a) a description of the ownership structure of the assessee enterprise with details of shares or other ownership interest held therein by other enterprises;

(b) a profile of the multinational group of which the assessee enterprise is a part along with the name, address, legal status and country of tax residence of each of the enterprises comprised in the group with whom international transactions have been entered into by the assessee, and ownership linkages among them;

(c) a broad description of the business of the assessee and the industry in which the assessee operates, and of the business of the associated enterprises with whom the assessee has transacted;

(d) the nature and terms (including prices) of international transactions entered into with each associated enterprise, details of property transferred or services provided and the quantum and the value of each such transaction or class of such transaction;

(e) a description of the functions performed, risks assumed and assets employed or to be employed by the assessee

and by the associated enterprises involved in the international transaction;

(f) a record of the economic and market analyses, forecasts, budgets or any other financial estimates prepared by the assessee for the business as a whole and for each division or product separately, which may have a bearing on the international transactions entered into by the assessee;

(g) a record of uncontrolled transactions taken into account for analysing their comparability with the international transactions entered into, including a record of the nature, terms and conditions relating to any uncontrolled transaction with third parties which may be of relevance to the pricing of the international transactions;

(h) a record of the analysis performed to evaluate comparability of uncontrolled transactions with the relevant international transaction;

(i) a description of the methods considered for determining the arm's length price in relation to each international transaction or class of transaction, the method selected as the most appropriate method along with explanations as to why such method was so selected, and how such method was applied in each case;

(j) a record of the actual working carried out for determining the arm's length price, including details of the comparable data and financial information used in applying the most appropriate method, and adjustments, if any, which were made to account for differences between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions;

(k) the assumptions, policies and price negotiations, if any, which have critically affected the determination of the arm's length price;

(l) details of the adjustments, if any, made to transfer prices to align them with arm's length prices determined under these rules and consequent adjustment made to the total income for tax purposes;

(m) any other information, data or document, including information or data relating to the associated enterprise, which may be relevant for determination of the arm's length price.

(2) Nothing contained in sub-rule (1) shall apply in a case where the aggregate value, as recorded in the books of account, of international transactions entered into by the assessee does not exceed one crore rupees:

Provided that the assessee shall be required to substantiate, on the basis of material available with him, that income arising from international transactions entered into by him has been computed in accordance with section 92.

(3) The information specified in sub-rule (1) shall be supported by authentic documents, which may include the following:

(a) official publications, reports, studies and data bases from the Government of the country of residence of the associated enterprise, or of any other country;

(b) reports of market research studies carried out and technical publications brought out by institutions of national or international repute;

(c) price publications including stock exchange and commodity market quotations;

(d) published accounts and financial statements relating to the business affairs of the associated enterprises;

(e) agreements and contracts entered into with associated enterprises or with unrelated enterprises in respect of transactions similar to the international transactions;

(f) letters and other correspondence documenting any terms negotiated between the assessee and the associated enterprise;

(g) documents normally issued in connection with various transactions under the accounting practices followed.

(4) The information and documents specified under sub-rules (1) and (2), should, as far as possible, be contemporaneous and should exist latest by the specified date referred to in clause (iv) of section 92F:

Provided that where an international transaction continues to have effect over more than one previous year, fresh documentation need not be maintained separately in respect of each previous year, unless there is any significant change in the nature or terms of the international transaction, in the assumptions made, or in any other factor which could influence the transfer price, and in the case of such significant change, fresh documentation as may be necessary under sub-rules (1) and (2) shall be maintained bringing out the impact of the change on the pricing of the international transaction.

(5) The information and documents specified in sub-rules (1) and (2) shall be kept and maintained for a period of eight years from the end of the relevant assessment year.

Rule 10E. Report from an accountant to be furnished under section 92E.—

The report from an accountant required to be furnished under section 92E by every person who has entered into an international transaction during a previous year shall be in Form No. 3CEB and be verified in the manner indicated therein";

(ii) rule 11 shall be omitted;

(iii) in the appendix, after Form No. 3CEA, the following Form shall be inserted, namely:—

Form No. 3CEB
[*See* rule10E]

Report from an accountant to be furnished under section 92E relating to international transaction(s)

1. *I/We have examined the accounts and records of ...(name and address of the assessee with PAN) relating to the international transactions entered into by the assessee during the previous year ending on 31st March, ...

2. In *my/our opinion proper information and documents as are prescribed have been kept by the assessee in respect of the international transaction(s) entered into so far as appears from *my/our examination of the records of the assessee.

3. The particulars required to be furnished under section 92E are given in the annexure to this Form. In *my/our opinion and to the best of my/our information and according to the explanations given to *me/us, the particulars given in the annexure are true and correct.

_____

****Signed**

Name _____

Address _____

Membership No. _____

Place: _____

Date: _____

Notes:

1. *Delete whichever is not applicable.

2. **This report has to be signed by—

(i) a chartered accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949); or

(ii) any person who, in relation to any State, is, by virtue of the provisions in sub-section (2) of section 226 of the Companies Act, 1956 (1 of 1956), entitled to be appointed to act as an auditor of companies registered in that State.

Annexure to Form No. 3CEB	
Particulars relating to international transactions required to be furnished under section 92E of the Income-tax Act, 1961	
Part A	
1. Name of the assessee:	
2. Address:	
3. Permanent account number:	
4. Status:	
5. Previous year ended:	
6. Assessment year:	
Part B	
7. List of associated enterprises with whom the assessee has entered into international transactions, with the following details:	
(a) Name of the associated enterprise.	
(b) Nature of the relationship with the associated enterprise as referred to in section 92A(2).	
(c) Brief description of the business carried on by the associated enterprise.	
8. Particulars in respect of transactions in tangible property:	
A. Has the assessee entered into any international trans action(s) in respect of purchase/sale of raw material, consumables or any other supplies for assembling/ processing/ manufacturing of goods / articles from/to associated enterprises?	**Yes/No**
If 'yes', provide the following details in respect of each associated enterprise and each transaction or class of transaction:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Description of transaction and quantity purchased/ sold.	

(c) Total amount paid/received or payable / receivable in the transaction	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(d) Method used for determining the arm's length price [see section 92C(1)]	
B. Has the assessee entered into any international trans action(s) in respect of purchase/sale of traded/finished goods?	Yes/No
If 'yes' provide the following details in respect of each associated enterprise and each transaction or class of transaction:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Description of transaction and quantity purchased/ sold.	
(c) Total amount paid/received or payable / receivable in the transaction	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(d) Method used for determining the arm's length price [see section 92C(1)]	
C. Has the assessee entered into any international trans action(s) in respect of purchase/sale of any other tangible moveable/immovable property or lease of such property?	Yes/No
If 'yes' provide the following details in respect of each associated enterprise and each transaction or class of transaction:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Description of the property and nature of transaction.	
(c) Number of units of each category of moveable/ immovable property involved in the transaction.	
(d) Amount paid / received or payable / receivable in each transaction of purchase /sale, or lease rent paid / received or payable/receivable in respect of each lease provided / entered into	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(e) Method used for determining the arm's length price [see section 92C(1)]	
9. Particulars in respect of transactions in intangible property:	
Has the assessee entered into any international transaction(s) in respect of purchase/sale/use of intangible property such as know-how, patents, copyrights, licensees, etc.?	Yes/No
If 'yes' provide the following details in respect of each associated enterprise and each category of intangible property:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Description of intangible property and nature of transaction.	
(c) Amount paid/received or payable/receivable for pur chase /sale / use of each category of intangible property	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(d) Method used for determining the arm's length price [see section 92C(1)]	
10. Particulars in respect of providing of services:	
Has the assessee entered into any international transaction(s) in respect of services such as financial, administrative, technical, commercial services, etc.?	Yes/No
If 'yes' provide the following details in respect of each associated enterprise and each category of service:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Description of services provided/availed of/from the associated enterprise.	
(c) Amount paid / received or payable / receivable for the services provided /taken	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(d) Method used for determining the arm's length price [see section 92C(1)]	
11. Particulars in respect of lending or borrowing money:	
Has the assessee entered into any international transaction(s) in respect of granting/receiving loans/ advances to or from associated enterprise?	Yes/No

If 'yes' provide the following details in respect of each associated enterprise and each loan/advance:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Nature of financing agreement.	
(c) Currency in which loan/advance granted/received.	
(d) Interest rate charged/paid in respect of each loan/ advance.	
(e) Amount paid/received or payable/receivable in the transaction	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(f) Method used for determining the arm's length price [see section 92C(1)]	
12. Particulars in respect of mutual agreement or arrangement:	
Has the assessee entered into any international transaction with an associated enterprise or enterprises by way of a mutual agreement or arrangement for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises?	Yes/No
If 'yes' provide the following details in respect of each agreement /arrangement:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Description of such mutual agreement or arrangement.	
(c) Amount paid / received or payable / receivable in each such transaction	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(d) Method used for determining the arm's length price [see section 92C(1)]	
13. Particulars in respect of any other transaction:	
Has the assessee entered into any other international transaction not specifically referred to above, with associated enterprise?	Yes/No
If 'yes' provide the following details in respect of each associated enterprise and each transaction:	
(a) Name and address of the associated enterprise with whom the international transaction has been entered into.	
(b) Description of the transaction.	
(c) Amount paid/received or payable/receivable in the transaction	
(i) as per books of account.	
(ii) as computed by the assessee having regard to the arm's length price.	
(d) Method used for determining the arm's length price [see section 92C(1)]	

_____

****Signed**

Name _____

Address _____

Place: _____

Date: _____

Notes: **This annexure has to be signed by—

(i) a chartered accountant within the meaning of the Chartered Accountants Act, 1949 (38 of 1949); or

(ii) any person who, in relation to any State, is, by virtue of the provisions in sub-section (2) of section 226 of the Companies Act, 1956 (1 of 1956), entitled to be appointed to act as an auditor of companies registered in that State.".

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 35 1989 India-United States Income Tax Treaty

(In force)

Date of signature: September 12, 1989.

Date of entry into force:	**December 18, 1990.**
Effective date:	**See Article 30(2).**

Convention between the Government of the United States of America and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income

The Government of the United States of America and the Government of the Republic of India, desiring to conclude a Convention for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income, have agreed as follows:

Article 1

General Scope

1. This Convention shall apply to persons who are residents of one or both of the Contracting States, except as otherwise provided in the Convention.

2. The Convention shall not restrict in any manner any exclusion, exemption, deduction, credit, or other allowance now or hereafter accorded:

(a) by the laws of either Contracting State; or

(b) by any other agreement between the Contracting States.

3. Notwithstanding any provision of the Convention except paragraph 4, a Contracting State may tax its residents (as determined under Article 4 (Residence)), and by reason of citizenship may tax its citizens, as if the Convention had not come into effect. For this purpose, the term "citizen" shall include a former citizen whose loss of citizenship had as one of its principal purposes the avoidance of tax, but only for a period of 10 years following such loss.

4. The provisions of paragraph 3 shall not affect

(a) the benefits conferred by a Contracting State under paragraph 2 of Article 9 (Associated Enterprises), under paragraphs 2 and 6 of Article 20 (Private Pensions, Annuities, Alimony, and Child Support), and under Articles 25 (Relief From Double Taxation), 26 (Non-Discrimination), and 27 (Mutual Agreement Procedure); and

(b) the benefits conferred by a Contracting State under Articles 19 (Remuneration and Pensions in Respect of Government Service), 21 (Payments Received by Students and Apprentices), 22 (Payments Received by Professors, Teachers and Research Scholars) and 29 (Diplomatic Agents and Consular Officers), upon individuals who are neither citizens of, nor have immigrant status in, that State.

Article 2

Taxes Covered

1. The existing taxes to which this Convention shall apply are:

(a) in the United States, the Federal income taxes imposed by the Internal Revenue Code (but excluding the accumulated earnings tax, the personal holding company tax, and social security taxes), and the excise taxes imposed on insurance premiums paid to foreign insurers and with respect to private foundations (hereinafter referred to as "United States tax"); provided, however, the Convention shall apply to the excise taxes imposed on insurance premiums paid to foreign insurers only to the extent that the risks covered by such premiums are not re-insured with a person not entitled to exemption from such taxes under this or any other Convention which applies to these taxes; and

(b) in India:

(i) the income tax including any surcharge thereon, but excluding income tax on undistributed income of companies, imposed under the Income-tax Act; and

(ii) the surtax (hereinafter referred to as "Indian tax"). Taxes referred to in (a) and (b) above shall not include any amount payable in respect of any default or omission in relation to the above taxes or which represent a penalty imposed relating to those taxes.

2. The Convention shall apply also to any identical or substantially similar taxes which are imposed after the date of signature of the Convention in addition to, or in place of, the existing taxes. The competent authorities of the Contracting States shall notify each other of any significant changes which have been made in their respective taxation laws and of any official published material concerning the application of the Convention.

Article 3

General Definitions

1. In this Convention, unless the context otherwise requires:

(a) the term "India" means the territory of India and includes the territorial sea and airspace above it, as well as any other maritime zone in which India has sovereign rights, other rights and jurisdiction, according to the Indian law and in accordance with international law;

(b) the term "United States", when used in a geographical sense means all the territory of the United States of America, including its territorial sea, in which the laws relating to United States tax are in force, and all the area

beyond its territorial sea, including the seabed and subsoil thereof, over which the United States has jurisdiction in accordance with international law and in which the laws relating to United States tax are in force;

(c) the terms "a Contracting State" and "the other Contracting State" mean India or the United States as the context requires;

(d) the term "tax" means Indian tax or United States tax, as the context requires;

(e) the term "person" includes an individual, an estate, a trust, a partnership, a company, any other body of persons, or other taxable entity;

(f) the term "company" means any body corporate or any entity which is treated as a company or body corporate for tax purposes;

(g) the terms "enterprise of a Contracting State" and "enterprise of the other Contracting State" mean respectively an enterprise carried on by a resident of a Contracting State and an enterprise carried on by a resident of the other Contracting State;

(h) the term "competent authority" means, in the case of India, the Central Government in the Ministry of Finance (Department of Revenue) or their authorized representative, and in the case of the United States, the Secretary of the Treasury or his delegate;

(i) the term "national" means any individual possessing the nationality or citizenship of a Contracting State;

(j) the term "international traffic" means any transport by a ship or aircraft operated by an enterprise of a Contracting State, except when the ship or aircraft is operated solely between places within the other Contracting State;

(k) the term "taxable year" in relation to Indian Tax means "previous year" as defined in the Income-tax Act. 1961.

2. As regards the application of the Convention by a Contracting State any term not defined therein shall, unless the context otherwise requires or the competent authorities agree to a common meaning pursuant to the provisions of Article 27 (Mutual Agreement Procedure), have the meaning which it has under the laws of that State concerning the taxes to which the Convention applies.

Article 4

Residence

1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, citizenship, place of management, place of incorporation, or any other criterion of a similar nature, provided, however, that

(a) this term does not include any person who is liable to tax in that State in respect only if income from sources in that State; and

(b) in the case of income derived or paid by a partnership, estate, or trust, this term applies only to the extent that the income derived by such partnership, estate, or trust is subject to tax in that State as the income of a resident, either in its hands or in the hands of its partners or beneficiaries.

2. Where by reason of the provisions of paragraph 1, an individual is a resident of both Contracting States, then his status shall be determined as follows:

(a) he shall be deemed to be a resident of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident of the State with which his personal and economic relations are closer (centre of vital interests);

(b) if the State in which he has his centre of vital interests cannot be determined, or if he does not have a permanent home available to him in either State, he shall be deemed to be a resident of the State in which he has an habitual abode;

(c) if he has an habitual abode in both States or in neither of them, he shall be deemed to be a resident of the State of which he is a national;

(d) if he is a national of both States or of neither of them, the competent authorities of the Contracting States shall settle the question of mutual agreement.

3. Where, by reason of paragraph 1, a company is a resident of both Contracting States, such company shall be considered to be outside the scope of this Convention except for purposes of paragraph 2 of Article 10 (Dividends), Article 26 (Non-Discrimination), Article 27 (Mutual Agreement Procedure), Article 28 (Exchange of Information and Administrative Assistance) and Article 30 (Entry Into Force).

4. Where, by reason of the provisions of paragraph 1, a person other than an individual or a company is a resident of both Contracting States, the competent authorities of the Contracting States shall settle the question by mutual agreement and determine the mode of application of the Convention of such person.

Article 5

Permanent Establishment

1. For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

2. The term "permanent establishment" includes especially:

(a) a place of management;

(b) a branch;

(c) an office;

(d) a factory;

(e) a workshop;

(f) a mine, an oil or gas well, a quarry, or any other place of extraction of natural resources;

(g) a warehouse, in relation to a person providing storage facilities for others;

(h) a farm, plantation or other place where agriculture, forestry, plantation or related activities are carried on;

(i) a store or premises used as a sales outlet;

(j) an installation or structure used for the exploration or exploitation of natural resources, but only if so used for a period of more than 120 days in any twelve month period.

(k) a building site or construction, installation or assembly project or supervisory activities in connection therewith, where such site, project or activities together with other such sites, projects or activities, if any) continue for a period of more than 120 days in any twelve month period;

(l) the furnishing of services, other than included services as defined in Article 12 (Royalties and Fees for Included Services), within a Contracting State by an enterprise through employees or other personnel, but only if:

(i) activities of that nature continue within that State for a period or periods aggregating more than 90 days within any twelve-month period; or

(ii) the services are performed within that State for a related enterprise (within the meaning of paragraph 1 of Article 9 (Associated Enterprises)).

3. Notwithstanding the preceding provisions of this Article, the term "permanent establishment" shall be deemed not to include any one or more of the following:

(a) the use of facilities solely for the purpose of storage, display, or occasional delivery of goods or merchandise belonging to the enterprise;

(b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display, or occasional delivery;

(c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

(d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise, or of collecting information, for the enterprise;

(e) the maintenance of a fixed place of business solely for the purpose of advertising, for the supply of information, for scientific research or for other activities which have a preparatory or auxiliary character, for the enterprise.

4. Notwithstanding the provisions of paragraphs 1 and 2, where a person—other than an agent of an independent status to whom paragraph 5 applies—is acting in a Contracting State on behalf of an enterprise of the other Contracting State, that enterprise shall be deemed to have a permanent establishment in the first-mentioned State if:

(a) he has an habitually exercises in the first-mentioned State an authority to conclude contracts on behalf of the enterprise, unless his activities are limited to those mentioned in paragraph 3 which, if exercised through a fixed place of business, would not make that fixed place of business a permanent establishment under the provisions of that paragraph;

(b) he has no such authority but habitually maintains in the first-mentioned State a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the enterprise, and some additional activities conducted in that State on behalf of the enterprise have contributed to the sale of the goods or merchandise; or

(c) he habitually secures orders in the first-mentioned State, wholly or almost wholly for the enterprise.

5. An enterprise of a Contracting State shall not be deemed to have a permanent establishment in the other Contracting State merely because it carries on business in that other State through a broker, general commission agent, or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business. However, when the activities of such an agent are devoted wholly or almost wholly on behalf of that enterprise and the transactions between the agent and the enterprise are not made under arm's-length conditions, he shall not be considered an agent of independent status within the meaning of this paragraph.

6. The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.

Article 6

Income From Immovable Property (Real Property)

1. Income derived by a resident of a Contracting State from immovable property (real property), including income from agriculture or forestry, situated in the other Contracting State may be taxed in that other State.

2. The term "immovable property" shall have the meaning which it has under the law of the contracting State in which the property in question is situated.

3. The provisions of paragraph 1 shall also apply to income derived from the direct use, letting, or use in any other form of immovable property.

4. The provisions of paragraphs 1 and 3 shall also apply to the income from immovable property of an enterprise and to income from immovable property used for the performance of independent personal services.

Article 7

Business Profits

1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to (a) that permanent establishment; (b) sales in the other State of goods or merchandise of the same or similar kind as those sold through that permanent establishment; or c) other business activities carried on in the other State of the same or similar kind as those effected through that permanent establishment.

2. Subject to the provisions of paragraph 3, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and independent enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly at arm's-length with the enterprise of which it is a permanent establishment and other enterprises controlling, controlled by or subject to the same common control as that enterprise. In any case where the correct amount of profits attributable to a permanent establishment is incapable of determination or the determination thereof presents exceptional difficulties, the profits attributable to the permanent establishment may be estimated on a reasonable basis. The estimate adopted shall, however, be such that the result shall be in accordance with the principles contained in this Article.

3. In the determination of the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the business of the permanent establishment, including a reasonable allocation of executive and general administrative expenses, research and development expenses, interest, and other expenses incurred for the purposes of the enterprise as a whole (or the part thereof which includes the permanent establishment), whether incurred in the State in which the permanent establishment is situated or elsewhere, in accordance with the provisions of and subject to the limitations of the taxation laws of that State. However, no such deduction shall be allowed in respect of amounts, if any, paid (otherwise than toward reimbursement of actual expenses) by the permanent establishment to the head office of the enterprise or any of its other offices, by way of royalties, fees or other similar payments in return for the use of patents, know-how or other rights, or by way of commission or other charges for specific services performed or for management, or, except in the case of banking enterprises, by way of interest on moneys lent to the permanent establishment. Likewise, no account shall be taken, in the determination of the profits of a permanent establishment, for amounts charged (otherwise than toward reimbursement of actual expenses), by the permanent establishment to the head office of the enterprise or any of its other offices, by way of royalties, fees or other similar payments in return for the use of patents, know-how or other rights, or by way of commission or other charges for specific services performed or for management, or, except in the case of a banking enterprise, by way of interest on moneys lent to the head office of the enterprise or any of its other offices.

4. No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.

5. For the purposes of this Convention, the profits to be attributed to the permanent establishment as provided in paragraph 1(a) of this Article shall include only the profits derived from the assets and activities of the permanent establishment and shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.

6. Where profits include items of income which are dealt with separately in other Articles of the Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.

7. For the purposes of the Convention, the term "business profits" means income derived from any trade or business including income from the furnishing of services other than included services as defined in Article 12 (Royalties and Fees for Included Services) and including income from the rental of tangible personal property other than property described in paragraph 3(b) of Article 12 (Royalties and Fees for Included Services).

Article 8

Shipping and Air Transport

1. Profits derived by an enterprise of a Contracting State from the operation by that enterprise of ships or aircraft in international traffic shall be taxable only in that State.

2. For the purposes of this Article, profits from the operation of ships or aircraft in international traffic shall mean profits derived by an enterprise described in paragraph 1 from the transportation by sea or air respectively of passengers, mail, livestock or goods carried on by the owners or lessees or charterers of ships or aircraft including—

(a) the sale of tickets for such transportation on behalf of other enterprises;

(b) other activity directly connected with such transportation; and

(c) the rental of ships or aircraft incidents to any activity directly connected with such transportation.

3. Profits of an enterprise of a Contracting State described in paragraph 1 from the use, maintenance, or rental of containers (including trailers, barges, and related equipment for the transport of containers) used in connection with the operation of ships or aircraft in international traffic shall be taxable only in that State.

4. The provisions of paragraphs 1 and 3 shall also apply to profits from participation in a pool, a joint business, or an international operating agency.

5. For the purposes of this Article, interest on funds connected with the operation of ships or aircraft in international traffic shall be regarded as profits derived from the operation of such ships or aircraft, and the provisions of Article 11 (Interest) shall not apply in relation to such interest.

6. Gains derived by an enterprise of a Contracting State described in paragraph 1 from the alienation of ships, aircraft or containers owned and operated by the enterprise, the income from which is taxable only in that State, shall be taxed only in that State.

Article 9

Associated Enterprises

1. Where:

(a) an enterprise of a Contracting State participates directly or indirectly in the management, control or capital of an enterprise of the Contracting State; or

(b) the same persons participate directly or indirectly in the management, control, or capital of an enterprise of a Contracting State and an enterprise of the other Contracting State, and in either case conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which, but for those conditions would have accrued to one of the enterprises, but by reason of those conditions have not so accrued, may be included in the profits of that enterprise and taxed accordingly.

2. Where a Contracting State includes in the profits of an enterprise of that State, and taxes accordingly, profits on which an enterprise of the other Contracting State has been charged to tax in that other State, and the profits so included are profits which would have accrued to the enterprise of the first-mentioned State if the conditions made between the two enterprises had been those which would have been made between independent enterprises, then that other State shall make an appropriate adjustment to the amount of the tax charged therein on those profits. In determining such adjusting, due regard shall be had to the other provisions of this Convention and the competent authorities of the Contracting State shall if necessary consult each other.

ARTICLE 10

Dividends

1. Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State.

2. However, such dividends may also be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the laws of the State, but if the beneficial owner of the dividends is a resident of the other Contracting State, the tax so charged shall not exceed:

(a) 15 percent of the gross amount of the dividends if the beneficial owner is a company which owns at least 10 percent of the voting stock of the company paying the dividends;

(b) 25 percent of the gross amount of the dividends in all other cases. Subparagraph (b) and not subparagraph (a) shall apply in the case of dividends paid by a United States person which is a Regulated Investment Company. Subparagraph (a) shall not apply to dividends paid by a United States person which is a Real Estate Investment Trust, and subparagraph (b) shall only apply if the dividend is beneficially owned by an individual holding a less than 10 percent interest in the Real Estate Investment Trust. This paragraph shall not effect the taxation of the company in respect of the profits out of which the dividends are paid.

3. The term "dividends" as used in this Article means income from shares or other rights not being debt-claims, participating in profits, income from other corporate rights which are subjected to the same taxation treatment as income from shares by the taxation laws of the State of which the company making the distribution is a resident; and income from arrangements, including debt obligations, carrying the right to participate in profits, to the extent so characterized under the laws of the Contracting State in which the income arises.

4. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the dividends, being a resident of a Contracting State, carries on business in the other Contracting State, of which the company paying the dividends is a resident, through a permanent establishment situated therein, or performs in that other State independent personal

services from a fixed based situated therein, and the dividends are attributable to such permanent establishment or fixed base. In such case the provisions of Article 7 (Business Profits) or Article 15 (Independent Personal Services), as the case ma be, shall apply.

5. Where a company which is a resident of a Contracting State derives profits or income from the other Contracting State, that other State may not impose any tax on the dividends paid by the company except insofar as such dividends are paid to a resident of that other State or insofar as the holding in respect of which the dividends are paid is effectively connected with a permanent establishment or a fixed base situated in that other State, nor subject the company's undistributed profits to a tax on the company's undistributed profits, even if the dividends paid or the undistributed profits consist wholly or partly of profits or income arising in such other State.

ARTICLE 11

Interest

1. Interest arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such interest may also be taxed in the Contracting State in which it arises, and according to the laws of that State, but if the beneficial owner of the interest is a resident of the other Contracting State, the tax so charged shall not exceed:

(a) 10 percent of the gross amount of the interest if such interest is paid on a loan granted by a bank carrying on a bona fide banking business or by similar financial institution (including an insurance company); and

(b) 15 percent of the gross amount of the interest in all other cases.

3. Notwithstanding the provisions of paragraph 2 of this Article, interest arising in a Contracting State:

(a) and derived and beneficially owned by the Government of the other Contracting State, a political subdivision or local authority thereof, the Reserve Bank of India, or the Federal Reserve Banks of the United States, as the case may be, and such other institutions of either Contracting State as the competent authorities may agree pursuant to Article 27 (Mutual Agreement Procedure);

(b) with respect to loans or credits extended or endorsed

(i) by the Export Import Bank of the United States, when India is the first-mentioned Contracting State; and

(ii) by the EXIM Bank of India, when the United States is the first-mentioned Contracting State; and

(c) to the extent approved by the Government of that State, and derived and beneficially owned by any person, other than a person referred to in subparagraph (a) and (b), who is a resident of the other Contracting State, provided that the transaction giving rise to the debt-claim has been approved in this behalf by the Government of the first-mentioned Contracting State; shall be exempt from tax in the first-mentioned Contracting State.

4. The term "interest" as used in this Convention means income from debt-claims of every kind, whether or not secured by mortgage, and whether or not carrying a right to participate in the debtor's profits, and in particular, income from government securities, and income from bonds or debentures, including premiums or prizes attaching to such securities, bonds, or debentures. Penalty charges for late payment shall not be regarded as interest for the purposes of the Convention. However, the term "interest" does not include income dealt with in Article 10 (Dividends).

5. The provisions of paragraphs 2 and 3 shall not apply if the beneficial owner of the interest, being a resident of a Contracting State, carries on business in the other Contracting State in which the interest arise, through a permanent establishment situated therein, or performs in the other State independent personal services from a fixed base situated therein, and the interest is attributable to such permanent establishment or fixed base. In such case the provisions of Article 7 (Business Profits) or Article 15 (Independent Personal Services), as the case may be, shall apply.

6. Interest shall be deemed to arise in a Contracting State when the payer is that State itself or a political subdivision, local authority, or resident of that State. Where, however, the person paying the interest, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base, and such interest is borne by such permanent establishment or fixed base, then such interest shall be deemed to arise in the Contracting State in which the permanent establishment or fixed base is situated.

7. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the interest, having regard to the debt-claim for which it is paid, exceeds the amount which would have been agreed upon by the payer and the beneficial owner in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of the Convention.

Article 12

Royalties and Fees for Included Services

1. Royalties and fees for included services arising in a Contracting State and paid to a resident of the other Contracting State may be taxed in that other State.

2. However, such royalties and fees for included services may also be taxed in the Contracting State in which they

arise and according to the laws of that State; but if the beneficial owner of the royalties or fees for included services is a resident of the other Contracting State, the tax so charged shall not exceed:

(a) in the case of royalties referred to in sub-paragraph (a) of paragraph 3 and fees for included services as defined in this Article (other than services described in sub-paragraph (b) of this paragraph):

(i) during the first five taxable years for which this Convention has effect.

(A) 15 percent of the gross amount of the royalties or fees for included services as defined in this Article, where the payer of the royalties or fees is the Government of that Contracting State, a political subdivision or a public sector company; and

(B) 20 percent of the gross amount of the royalties or fees for included services in all other cases; and

(ii) during the subsequent years, 15 percent of the gross amount of royalties or less for included services; and

(b) in the case of royalties referred to in sub-paragraph (b) of paragraph 3 and fees for included services as defined in this Article that are ancillary and subsidiary to the enjoyment of the property for which payment is received under paragraph 3(b) of this Article, 10 percent of the gross amount of the royalties or fees for included services.

3. The term "royalties" as used in this Article means:

(a) payments of any kind received as a consideration for the use of, or the right to use, any copyright of a literary, artistic, or scientific work, including cinematograph films or work on film, tape or other means of reproduction for use in connection with radio or television broadcasting, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience, including gains derived from the alienation of any such right or property which are contingent on the productivity, use, or disposition thereof; and

(b) payments of any kind received as consideration for the use of, or the right to use, any industrial, commercial, or scientific equipment, other than payments derived by an enterprise described in paragraph 1 of Article 8 (Shipping and Air Transport) from activities described in paragraph 2(c) or 3 of Article 8.

4. Four purposes of this Article, "fees for included services" means payments of any kind to any person in consideration for the rendering of any technical or consultancy services (including through the provision of services of technical or other personnel) if such services:

(a) are ancillary and subsidiary to the application or enjoyment of the right, property or information for which a payment described in paragraph 3 is received; or

(b) make available technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design.

5. Notwithstanding paragraph 4, "fees for included services" does not include amounts paid:

(a) for services that are ancillary and subsidiary, as well as inextricably and essentially linked, to the sale of property other than a sale described in paragraph 3(a);

(b) for services that are ancillary and subsidiary to the rental of ships, aircraft, containers or other equipment used in connection with the operation of ships or aircraft in international traffic;

(c) for teaching in or by educational institutions;

(d) for services for the personal use of the individual or individuals making the payment; or

(e) to an employee of the person making the payments or to any individual or firm of individuals (other than a company) for professional services as defined in Article 15 (Independent Personal Services).

6. The provisions of paragraphs 1 and 2 shall not apply if the beneficial owner of the royalties or fees for included services, being a resident of a Contracting State, carries on business in the other Contracting States, in which the royalties or fees for included services arises, through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the royalties or fees for included services are attributable to such permanent establishment or fixed base. In such case the provisions of Article 7 (Business Profits) or Article 15 (Independent Personal Services), as the case may be, shall apply.

7. (a) Royalties and fees for included services shall be deemed to arise in a Contracting State when the payer is that State itself, a political subdivision, a local authority, or a resident of that State. Where, however, the person paying the royalties or fees for included services, whether he is a resident of a Contracting State or not, has in a Contracting State a permanent establishment or a fixed base in connection with which the liability to pay the royalties or fees for included services was incurred, and such royalties or fees for included services are borne by such permanent establishment or fixed base, then such royalties or fees for included services shall be deemed to arise in the Contracting State in which the permanent establishment or fixed base is situated.

(b) Where under subparagraph (a) royalties or fees for included services do not arise in one of the Contracting States, and the royalties relate to the use of, or the right to use, the right or property, or the fees for included services relate to services performed, in one of the Contracting States, the royalties or fees for included services shall be deemed to arise in that Contracting State.

8. Where, by reason of a special relationship between the payer and the beneficial owner or between both of them and some other person, the amount of the royalties or fees for included services paid exceeds the amount which

would have been paid in the absence of such relationship, the provisions of this Article shall apply only to the last-mentioned amount. In such case, the excess part of the payments shall remain taxable according to the laws of each Contracting State, due regard being had to the other provisions of the Convention.

Article 13

Gains

Except as provided in Article 8 (Shipping and Air Transport) of this Convention, each Contracting State may tax capital gains in accordance with the provisions of its domestic law.

Article 14

Permanent Establishment Tax

1. A company which is a resident of India may be subject in the United States to a tax in addition to the tax allowable under the other provisions of this Convention.

(a) Such tax, however, may be imposed only on:

(i) the portion of the business profits of the company subject to tax in the United States which represents the dividend equivalent amount; and

(ii) the excess, if any, of interest deductible in the United States in computing the profits of the company that are subject to tax in the united States and either attributable to a permanent establishment in the United States or subject to tax in the United States under Article 6 (Income From Immovable Property (Real Property)), Article 12 (Royalties and Fees for Included Services) as fees for included services, or Article 13 (Gains) of this Convention over the interest paid by or from the permanent establishment or trade or business in the United States.

(b) For purposes of this article, business profits means profits that are effectively connected (or treated as effectively connected) with the conduct of a trade or business within the United States and are either attributable to a permanent establishment in the United States or subject to tax in the United States under Article 6 (Income From Immovable Property (Real Property)), Article 12 (Royalties and Fees for Included Services) as fees for included services or Article 13 (Gains) of this Convention.

(c) The tax referred to in subparagraph (a) shall not be imposed at a rate exceeding:

(i) the rate specified in paragraph 2(a) of Article 10 (Dividends) for the tax described in subparagraph (a)(i); and

(ii) the rate specified in paragraph 2 (a) or (b) (whichever is appropriate) of Article 11 (Interest) for the tax described in subparagraph (a)(ii).

2. A company which is a resident of the United States may be subject to tax in India at a rate higher than that applicable to the domestic companies. The difference in the tax rate shall not, however, exceed the existing difference of 15 percentage points.

3. In the case of a banking company which is a resident of the United States, the interest paid by the permanent establishment of such a company in India to the head office may be subject in India to a tax addition to the tax impossible under the other provisions of this Convention at a rate which shall not exceed the rate specified in paragraph 2(a) of Article (Interest).

Article 15

Independent Personal Services

1. Income derived by a person who is an individual or firm of individuals (other than a company) who is a resident of a Contracting State from the performance in the other Contracting State of professional services or other independent activities of a similar character shall be taxable only in the first-mentioned State except in the following circumstances when such income may also be taxed in the other Contracting State:

(a) if such person has a fixed base regularly available to him in the other Contracting State for the purpose of performing his activities; in that case, only so much of the income as is attributable to that fixed base may be taxed in that other State; or

(b) if the person's stay in the other Contracting State in for a period or periods amounting to or exceeding in the aggregate 90 days in the relevant taxable year.

2. The term "professional services" includes independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, surgeons, lawyers, engineers, architects, dentists and accountants.

Article 16

Dependent Personal Services

1. Subject to the provisions of Articles 17 (Directors' Fees), 18 (Income Earned by Entertainers and Athletes), 19 (Remuneration and Pensions in Respect of Government Service), 20 (Private Pensions, Annuities, Alimony, and Child Support), 21 (Payments Received by Students and Apprentices) and 22 (Payments Received by Professors, Teachers and Research Scholars), salaries, wages, and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that

other State.

2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if:

(a) the recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in the relevant taxable year;

(b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other State; and

(c) the remuneration is not borne by a permanent establishment or a fixed base or a trade or business which the employer has in the other State.

3. Notwithstanding the preceding provisions of this Article, remuneration derived in respect of an employment exercised aboard a ship or aircraft operated in international traffic by an enterprise of a Contracting State may be taxed in that State.

Article 17

Directors' Fees

Directors' fees and similar payments derived by a resident of a Contracting State in his capacity as a member of the board of directors of a company which is a resident of the other Contracting State may be taxed in that other State.

Article 18

Income Earned by Entertainers and Athletes

1. Notwithstanding the provisions of Articles 15 (Independent Personal Services) and 16 (Dependent Personal Services), income derived by a resident of a Contracting State as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as an athlete, from his personal activities as such exercised in the other Contracting State, may be taxed in that other State, except where the amount of the net income derived by such entertainer or athlete from such activities (after deduction of all expense incurred by him in connection with his visit and performance) does not exceed one thousand five hundred United States dollars ($1,500) or its equivalent Indian rupees for the taxable year concerned.

2. Where income in respect of activities exercised by an entertainer or an athlete in his capacity as such accrues not to the entertainer or athlete but to another person, that income of that other person may, notwithstanding the provisions of Articles 7 (Business Profits), 15 (Independent Personal Services) and 16 (Dependent Personal Services), be taxed in the Contracting State in which the activities of the entertainer or athlete are exercised unless the entertainer, athlete, or other person establishes that neither the entertainer or athlete nor persons related thereto participate directly or indirectly in the profits of that other person in any manner, including the receipt of deferred remuneration, bonuses, fees, dividends, partnership distributions, or other distributions.

3. Income referred to in the preceding paragraphs of this Article derived by a resident of a Contracting State in respect of activities exercised in the other Contracting State shall not be taxed in that other State if the visit of the entertainers or athletes to that other State is supported wholly or substantially from the public funds of the Government of the first-mentioned Contracting State, or of a political subdivision or local authority thereof.

4. The competent authorities of the Contracting States may, by mutual agreement, increase the dollar amounts referred to in paragraph 1 to reflect economic or monetary developments.

Article 19

Remuneration and Pensions in Respect of Government Service

1. (a) Remuneration, other than a pension, paid by a Contracting State or a political sub-division or a local authority thereof to an individual in respect of services rendered to that State or sub-division or authority shall be taxable only in that State.

(b) However, such remuneration shall be taxable only in the other Contracting State if the services are rendered in that other State and the individual is a resident of that State who:

(i) is a national of that State; or

(ii) did not become a resident of that State solely for the purpose of rendering the services.

2. (a) Any pension paid by, or out of funds created by, a Contracting State or a political subdivision or a local authority thereof to an individual in respect of services rendered to that state or subdivision or authority shall be taxable only in that State.

(b) However, such pension shall be taxable only in the other Contracting State if the individual is a resident of, and a national of, that State.

3. The provisions of Articles 16 (Dependent Personal Services), 17 (Directors' Fees), 18 (Income Earned by Entertainers and Athletes) and 20 (Private Pensions, Annuities, Alimony and Child Support) shall apply to remuneration and pensions in respect of services rendered in connection with a business carried on by a Contracting State or a political subdivision or a local authority thereof.

Article 20

Private Pensions, Annuities, Alimony and Child Support

1. Any pension, other than a pension referred to in Article 19 (Remuneration and Pensions in Respect of Government Service), or any annuity derived by a resident of a Contracting State from sources within the other contracting State maybe taxed only in the first-mentioned Contracting State.

2. Notwithstanding paragraph 1, and subject to the provisions of Article 19 (Renumeration and Pension in Respect of Government Service), social security benefits and other public pensions paid by a Contracting State to a resident of the other Contracting State or a citizen of the United States shall be taxable only in the first-mentioned State.

3. The term "pension" means a periodic payment made in consideration of past services or by way or compensation for injuries received in the course of performance of services.

4. The term "annuity" means stated sums payable periodically at stated times during life or during a specified or ascertainable number of years, under an obligation to make the payments in return for adequate and full consideration in money or money's worth (but not for services rendered).

5. Alimony paid to a resident of a Contracting State shall be taxable only in that State. The term "alimony" as used in this paragraph means periodic payments made pursuant to a written separation agreement or a decree of divorce, separate maintenance, or compulsory support, which payments are taxable to the recipient under the laws of the State of which he is a resident.

6. Periodic payments for the support of a minor child made pursuant to a written separation agreement or a decree of divorce, separate maintenance or compulsory support, paid by a resident of a Contracting State to a resident of the other Contracting State, shall be taxable only in the first-mentioned State.

Article 21

Payments Received by Students and Apprentices

1. A student or business apprentice who is or was a resident of one of the Contracting States immediately before visiting the other Contracting State and who is present in that other State principally for the purpose of his education or training shall be exempt from tax in that other State, on payments which arise outside that other State for the purposes of his maintenance, education or training.

2. In respect of grants, scholarships and remuneration from employment not covered by paragraph 1, a student or business apprentice described in paragraph 1 shall, in addition, be entitled during such education or training to the same exemptions, reliefs or reductions in respect of taxes available to residents of the State which he is visiting.

3. The benefits of this Article shall extend only for such period of time as may be reasonable or customarily required to complete the education or training undertaken.

4. For the purposes of this Article, an individual shall be deemed to be a resident of a Contracting State if he is resident in that Contracting State in the taxable year in which he visits the other Contracting State or in the immediate proceeding taxable year.

Article 22

Payments Received by Professors, Teachers and Research Scholars

1. An individual who visits a Contracting State for a period not exceeding two years for the purpose of teaching or engaging in research at a university, college or other recognized educational institution in that State, and who was immediately before that visit a resident of the other Contracting State, shall be exempted from tax by the first-mentioned Contracting State on any remuneration for such teaching or research for a period not exceeding two years from the date he first visits that State for such purpose.

2. This Article shall apply to income from research only if such research is undertaken by the individual in the public interest and not primarily for the benefit of some other private person or persons.

Article 23

Other Income

1. Subject to the provisions of paragraph 2, items of income of a resident of a Contracting State, wherever arising, which are not expressly dealt with in the foregoing Articles of this Convention shall be taxable only in that Contracting State.

2. The provisions of paragraph 1 shall not apply to income, other than income from immovable property as defined in paragraph 2 of Articles 6 (Income from Immovable Property (Real Property)), if the beneficial owner of the income, being a resident of a Contracting State, carries on business in the other Contracting State through a permanent establishment situated therein, or performs in that other State independent personal services from a fixed base situated therein, and the income is attributable to such permanent establishment or fixed base. In such case the provisions of Article 7 (Business Profits) or Article 15 (Independent Personal Services), as the case may be, shall apply.

3. Notwithstanding the provisions of paragraphs 1 and 2, items of income of a resident of a Contracting State not dealt with in the foregoing articles of this Convention and arising in the other Contracting State may also be taxed in that other State.

Article 24

Limitation on Benefits

1. A person (other than an individual) which is a resident of a Contracting State and derives income from the other Contracting State shall be entitled under this Convention to relief from taxation in that other Contracting State only if:

(a) more than 50 percent of the beneficial interest in such person (or in the case of a company, more than 50 percent of the number of shares of each class of the company's shares) is owned, directly or indirectly, by one or more individual residents of one of the Contracting States, one of the Contracting States or its political subdivisions or local authorities, or other individuals subject to tax in either Contracting State or their worldwide incomes, or citizens of the United States; and

(b) the income of such person is not used in substantial part, directly or indirectly, to meet liabilities (including liabilities for interest or royalties) to persons who are not residents of one of the Contracting States, one of the contracting States or its political subdivisions or local authorities, or citizens of the United States.

2. The provisions of paragraph 1 shall not apply if the income derived from the other Contracting State is derived in connection with, or is incidental to, the active conduct by such person of a trade or business in the first-mentioned State (other than the business of making or managing investments, unless these activities are banking or insurance activities carried on by a bank or insurance company).

3. The provisions of paragraph 1 shall not apply if the person deriving the income is a company which is a resident of a Contracting State in whose principal class of shares there is substantial and regular trading on a recognized stock exchange. For purposes of the preceding sentence, the term "recognized stock exchange" means:

(a) in the case of the United States, the NASDAQ System owned by the National Association of Securities Dealers, Inc. and any stock exchange registered with the Securities and Exchange Commission as a national securities exchange for purposes of the Securities Act of 1934;

(b) in the case of India, any stock exchange which is recognized by the Central Government under the Securities Contracts Regulation Act, 1956; and

(c) any other stock exchange agreed upon by the competent authorities of the Contracting States.

4. A person that is not entitled to the benefits of this Convention pursuant to the provisions of the preceding paragraphs of this Article may, nevertheless, be granted the benefits of the Convention if the competent authority of the State in which the income in question arises so determines.

Article 25

Relief From Double Taxation

1. In accordance with the provisions and subject to the limitations of the law of the united States (as it may be amended from time to time without changing the general principle hereof), the United States shall allow to a resident or citizen of the United States as a credit against the United States tax on income

(a) the income tax paid to India by or on behalf of such citizen or resident; and

(b) in the case of a United States company owning at least 10 percent of the voting stock of a company which is a resident of India and from which the United States company receives dividends, the income tax paid to India by or on behalf of the distributing company with respect to the profits out of which the dividends are paid.

For the purposes of this paragraph, the taxes referred to in paragraphs 1(b) and 2 of Article 2 (Taxes Covered) shall be considered income taxes.

2. (a) Where a resident of India derives income which, in accordance with the provisions of this Convention, may be taxed in the United States, India shall allow as a deduction from the tax on the income of that resident an amount equal to the income tax paid in the United States, whether directly or by deduction. Such deduction shall not, however, exceed that part of the income tax (as computed before the deduction is given) which is attributable to the income which may be taxed in the United States.

(b) Further, where such resident is a company by which a surtax is payable in India, the deduction in respect of income tax paid in the United States shall be allowed in the first instance from income tax payable by the company in India and as to the balance, if any, from surtax payable by it in India.

3. For the purposes of allowing relief from double taxation pursuant to this Article, income shall be deemed to arise as follows:

(a) income derived by a resident of a Contracting State which may be taxed in the other Contracting State in accordance with this Convention (other than solely by reason of citizenship in accordance with paragraph 3 of Article 1 (General Scope)) shall be deemed to arise in that other State;

(b) income derived by a resident of a Contracting State which may not be taxed in the other Contracting State in accordance with the Convention shall be deemed to arise in the first-mentioned State. Notwithstanding the proceeding sentence, the determination of the source of income for purposes of this Article shall be subject to such source rules in the domestic laws of the Contracting States as apply for the purpose of limiting the foreign tax credit. The preceding sentence shall not apply with respect to income dealt with in Article 12 (Royalties and Fees for Included Services). The rules of this paragraph shall not apply in determining credits against United States tax for foreign taxes other than the taxes referred to in paragraphs (b) and 2 of Article 2 (Taxes Covered).

Article 26

Non-discrimination

1. National of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances are or may be subjected. This provision shall apply to persons who are not residents of one or both of the Contracting States.

2. Except where the provisions of paragraph 3 of Article 7 (Business Profits) apply, the taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favorably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities. This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs, and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents.

3. Except where the provisions of paragraph 1 of Article 9 (Associated Enterprises), paragraph 7 of Article 11 (Interest), or paragraph 8 of Article 12 (Royalties and Fees for Included Services) apply, interest, royalties, and other disbursements paid by a resident of a Contracting State to a resident of the other Contracting State shall, for the purposes of determining the taxable profits of the first-mentioned resident, be deductible under the same conditions as if they had paid to a resident of the first-mentioned State.

4. Enterprises of a Contracting State, the capital of which is wholly or partly owned or controlled, directly or indirectly, by one or more residents of the other Contracting State, shall not be subjected in the first-mentioned State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which other similar enterprises of the first-mentioned State are or may be subjected.

5. Nothing in this article shall be construed as preventing either Contracting State from imposing the taxes described in Article 14 (Permanent Establishment Tax) or the limitations described in paragraph 3 of Article 7 (Business Profits).

Article 27

Mutual Agreement Procedure

1. Where a person considers that the actions of one or both of the Contracting States result or will result for him in taxation not in accordance with the provisions of this Convention, he may, irrespective of the remedies provided by the domestic law of those States, present his case to the competent authority of the Contracting State of which he is a resident or national. This case must be presented within three years of the date of receipt of notice of the action which gives rise to taxation not in accordance with the Convention.

2. The competent authority shall endeavor, if the objection appears to it to be justified and if it is not itself able to arrive at a satisfactory solution, to resolve the case by mutual agreement with the competent authority of the other Contracting State, with a view to the avoidance of taxation which is not in accordance with the Convention. Any agreement reached shall be implemented notwithstanding any time limits or other procedural limitations in the domestic law of the Contracting States.

3. The competent authorities of the Contracting States shall endeavor to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention. They may also consult together for the elimination of double taxation in cases not provided for in the Convention.

4. The competent authorities of the Contracting States may communicate with each other directly for the purpose of reaching an agreement in the sense of the preceding paragraphs. The competent authorities, through consultations, shall develop appropriate bilateral procedures, conditions, methods and techniques for the implementation of the mutual agreement procedure provided for in this Article. In addition, a competent authority may devise appropriate unilateral procedures, conditions, methods and techniques to facilitate the above-mentioned bilateral actions and the implementation of the mutual agreement procedure.

Article 28

Exchange of Information and Administrative Assistance

1. The competent authorities of the Contracting States shall exchange such information (including documents) as is necessary for carrying out the provisions of this Convention or of the domestic laws of the Contracting States concerning taxes covered by the Convention insofar as the taxation thereunder is not contrary to the Convention, in particular, for the prevention of fraud or evasion of such taxes. The exchange of information is not restricted by Article 1 (General Scope). Any information received by a Contracting State shall be treated as secret in the same manner as information obtained under the domestic laws of that State. However, if the information is originally regarded as secret in the transmitting State, it shall be disclosed only to persons or authorities (including courts and administrative bodies) involved in the assessment, collection, or administration of, the enforcement or prosecution in respect of, or the determination of appeals in relation to, the taxes which are the subject of the Convention. Such persons or authorities shall use the information only for such purposes, but may disclose the information in public court proceedings or in judicial decisions. The competent authorities shall, through consultation, develop appropriate conditions, methods and techniques concerning the matters in respect of which such exchange of information shall be made, including, where appropriate, exchange of information regarding tax avoidance.

2. The exchange of information or documents shall be either on a routine basis or on request with reference to particular cases, or otherwise. The competent authorities of the Contracting States shall agree from time to time on

the list of information or documents which shall be furnished on a routine basis.

3. In no case shall the provisions of paragraph 1 be construed so as to impose on a Contracting State the obligation:

(a) to carry out administrative measures at variance with the laws and administrative practice of that or of the other Contracting State;

(b) to supply information which is not obtainable under the laws or in the normal course of the administration of that or of the other Contracting State;

(c) to supply information which would disclose any trade, business, industrial, commercial, or professional secret or trade process, or information the disclosure of which would be contrary to public policy (ordre public).

4. If information is requested by a Contracting State in accordance with this Article, the other Contracting State shall obtain the information to which the request relates in the same manner and in the same form as if the tax of the first-mentioned State were the tax of that other State and were being imposed by that other State. If specifically requested by the competent authority of a Contracting State, the competent authority of the other Contracting State shall provide information under this Article in the form of depositions of witnesses and authenticated copies of unedited original documents (including books, papers, statements, records, accounts, and writings), to the same extent such depositions and documents can be obtained under the laws and administrative practices of that other State with respect to its own taxes.

5. For the purposes of this Article, the Convention shall apply, notwithstanding the provisions of Article 2 (Taxes Covered):

(a) in the United States, to all taxes imposed under Title 26 of the United States Code; and

(b) in India, to the income tax, the wealth tax and the gift tax.

Article 29

Diplomatic Agents and Consular Officers

Nothing in this Convention shall affect the fiscal privileges of diplomatic agents or consular officers under the general rules of international law or under the provisions of special agreements.

Article 30

Entry Into Force

1. Each Contracting State shall notify the other Contracting State in writing, through diplomatic channels, upon the completion of their respective legal procedures to bring this Convention into force.

2. The Convention shall enter into force on the date of the latter of such notifications and its provisions shall have effect:

(a) in the United States

(i) in respect of taxes withheld at source, for amounts paid or credited on or after the first day of January next following the date on which the Convention enters into force;

(ii) in respect of other taxes, for taxable periods beginning on or after the first day of January next following the date on which the Convention enters into force; and

(b) in India, in respect of income arising in any taxable year beginning on or after the first day of April next following the calendar year in which the Convention enters into force.

Article 31

Termination

This Convention shall remain in force indefinitely but either of the Contracting States may, on or before the thirtieth day of June in any calendar year beginning after the expiration of a period of five years from the date of the entry into force of the Convention, give the other Contracting State through diplomatic channels, written notice of termination and, in such event, this Convention shall cease to have effect:

(a) in the United States

(i) in respect of taxes withheld at source, for amounts paid or credited on or after the first day of January next following the calendar year in which notice of termination is given; and

(ii) in respect of other taxes, for taxable periods beginning on or after the first day of January next following the calendar year in which the notice of termination is given; and

(b) in India, in respect of income arising in any taxable year beginning on or after the first day of April next following the calendar year in which the notice of termination is given.

IN WITNESS WHEREOF, the undersigned, being duly authorized by their respective Governments, have signed this Convention.

DONE at New Delhi in duplicate, this 12th day of September, 1989, in the English and Hindi languages, both texts being equally authentic. In case of divergence between the two texts, the English text shall be the operative one.

For the Government of the United States of America: John R. Hubbard, Ambassador.

For the Government of the Republic of India: N.K. Sengupta, Secretary to the Government of India.

Protocol

At the signing today of the Convention between the United States of America and the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income, the undersigned have agreed upon the following provisions, which shall form an integral part of the Convention:

I. Ad Article 5

It is understood that where an enterprise of a Contracting State has a permanent establishment in the other Contracting State in accordance with the provisions of paragraphs 2(j), 2(k) or 2(l) of Article 5 (Permanent Establishment), and the time period referred to in that paragraph extends over two taxable years, a permanent establishment shall not be deemed to exist in a year, if any, in which the use, site, project or activity, as the case may be, continues for a period or periods aggregating less than 30 days in that taxable year. A permanent establishment will exist in the other taxable year, and the enterprise will be subject to tax in that other Contracting State in accordance with provisions of Article 7 (Business Profits), but only on income arising during that other taxable year.

II. Ad Article 7

Where the law of the Contracting State in which a permanent establishment is situated imposes, in accordance with the provisions of paragraph 3 of Article 7 (Business Profits), a restriction on the amount of executive and general administrative expenses which may be allowed as a deduction in determining the profits of such permanent establishment, it is understood that in making such a determination of profits the deduction in respect of such executive and general administrative expenses in no case shall be less than that allowable under the Indian Income?tax Act as on the date of signature of this Convention.

III. Ad Articles 7, 10, 11, 12, 15, and 23

It is understood that for the implementation of paragraphs 1 and 2 of Article 7 (Business Profits), paragraph 4 of Article 10 (Dividends), paragraph 5 of Article 11 (Interest), paragraph 6 of Article 12 (Royalties and Fees for Included Services), paragraph 1 of Article 15 (Independent Personal Services), and paragraph 2 of Article 23 (Other Income), any income attributable to a permanent establishment or fixed base during its existence is taxable in the Contracting State in which such permanent establishment or fixed base is situated even if the payments are deferred until such permanent establishment or fixed base has ceased to exist.

IV. Ad Article 12

It is understood that fees for included services, as defined in paragraph 4 of Article 12 (Royalties and Fees for included Services) will, in accordance with United States law, be subject to income tax in the United States based on net income and, when earned by a company, will also be subject to the taxes described in paragraph 1 of Article 14 (Permanent Establishment Tax). The total of these taxes which may be imposed on such fees, however, may not exceed the amount computed by multiplying the gross fee by the appropriate tax rate specified in subparagraph (a) or (b), whichever is applicable, of paragraph 2 of Article 12.

V. Ad Article 14

It is understood that references in paragraph 1 of Article 14 (Permanent Establishment Tax) to profits that are subject to tax in the United States under Article 6 (Income from Immovable Property (Real Property)), under Article 12 (Royalties and Fees for Included Services), as fees for included services as defined in that Article, or under Article 13 (Gains) of this Convention, are intended to refer only to cases in which the profits in question are subject to United States tax based on net income (i.e., by virtue of being effectively connected, or being treated as effectively connected, with the conduct of a trade or business in the United States). Any income which is subject to tax under those Articles based on gross income is not subject to tax under Article 14.

IN WITNESS WHEREOF, the undersigned, being duly authorized by their respective Governments, have signed this Protocol.

DONE at New Delhi in duplicate, this 12th day of September, 1989, in the English and Hindi languages, both texts being equally authentic. In case of divergence between the two texts, the English text shall be the operative one.

For the Government of the United States of America: John R. Hubbard, Ambassador.

For the Government of the Republic of India: N.K. Sengupta, Secretary to the Government of India.

LETTER OF SUBMITTAL

Department of State

Washington, October 24, 1989.

The President,

The White House.

Dear Mr. President: I have the honor to submit to you, with a view to its transmission to the Senate for advice and consent to ratification, the convention between the Government of the United States of America and the Government of the Republic of India for the Avoidance of Double Taxation and the prevention of Fiscal Evasion with Respect to Taxes on Income, together with a related Protocol, signed at New Delhi on September 12, 1989.

The Convention provides maximum rates of tax at source on payments of dividends, interest and royalties which, in each case, are higher than the rates specified in the United States Model. Dividend from a subsidiary to a parent corporation are taxable at a maximum rate of 15 percent; other dividends may be taxable at source at a 25 percent rate. Interest is, in general, taxable at source at a maximum rate of 15 percent, although interest received by a financial institution is taxable at a maximum rate of 10 percent, and interest received by either of the two Governments, by certain governmental financial institutions, and by residents of a Contracting State on certain Government approved loans, is exempt from tax at source.

The royalty provisions contain several significant departures from standards United States tax treaty policy. In general, industrial and copyright royalties are taxable to source at a maximum rate of 20 percent for the first five years, dropping to 15 percent thereafter. Where the payor of the royalty is one of the Governments, a political subdivision or a public sector corporation, tax will be imposed from the date of entry into force of the treaty at a maximum rate of 15 percent. Payments or these of, or the right to use, industrial, commercial or scientific equipment are treated as royalties, rather than as business profits, and are subject to a maximum rate of tax at source of 10 percent. The most significant departure from past policy in the royalty article is the fact that certain service fees, referred to in the Convention as "fees for included services", are treated in the same manner as royalties, and not, as would normally be the case, as business profits. Included service are defined as technical consultancy service which either: (i) are ancillary and subsidiary to the licensing of an intangible or the rental of tangible personal property, both of which give rise to royalty payments, or, (ii) if not ancillary or subsidiary, make available to the payor of the service fee some technical knowledge, experience, skill, etc., or transfer to that person a technical plan or design. A detailed memorandum of understanding was developed by the negotiators to provide guidance as to the intended scope of the concept of "included services" and the effect of the memorandum is agreed to in an exchange of notes. These are included for information only. Fees or all other services are treated either as business profits or as independent personal services income. Although not reflected in the convention, under Indian law, certain service fees related to defense contracts are exempt from Indian tax.

The Convention preserves for the United States the right to impose the branch profits tax. It preserves for both Contracting States their statutory taxing rights with respect to capital gains.

The Convention also contains rules for the taxation of business profits which, consistent with other United States tax treaties with developing countries, provide a broader range of circumstances under which one partner may tax the business profits of a resident of the other. The Convention defines permanent establishment to include a construction site or a drilling rig where the site or activity continues or a period of 120 days in a year. This compares with a twelve-month threshold under the United States model, and six months under the typical developing country tax treaty. In addition, the Convention contains reciprocal exemption at source for shipping and aircraft operating income, including income from the incidental leasing of ships, aircraft or containers (i.e., where the lessor is an operator of ships and aircraft). The Convention differs from the United States Model in that income from the non-incidental leasing of ships, aircraft or containers (i.e., where the lessor is not an operator of ships or aircraft) is not covered by the article. Income from such non-incidental leasing is treated as a royalty, taxable at source at a maximum rate of 10 percent.

The treatment under the Convention of various classes of personal service income is similar to that under the United States tax treaties with developing countries. The Convention contains provisions designed to prevent third-country residents from treaty shopping, i.e., from taking unwarranted advantage of the Convention by routing income from one Contracting State through an entity created in the other. These provisions consistent with recent tax legislation, identify treaty shopping in terms both of third-country ownership of an entity, and of the substantial use of the entity's income to meet liabilities to third-country persons. Notwithstanding the presence of these factors, however, treaty benefits will be allowed if the income is incidental to or earned in connection with the active conduct of a trade or business in the State of residence, if the shares of the company earning the income are traded on a recognized stock exchange, or if the competent authority of the source State so determines.

As with all United States tax treaties, the Convention prohibits tax discrimination, creates a dispute resolution mechanism and provides for the exchange of otherwise confidential tax information between the tax authorities of the parties. The Convention authorizes access by the General Accounting Office and the tax writing committees of Congress to certain information exchanged under the Convention which is relevant to the functions of these bodies in overseeing the administration of United States laws.

In an exchange of notes, the United States and India agree that although the Convention does not contain a tax sparing credit, if United States policy changes in this regard, the Convention will be promptly amended to incorporate a tax sparing provision. These notes are also included for information only.

A technical memorandum explaining in detail the provisions of the Convention and the related Protocol is being prepared by the Department of the Treasury and will be submitted separately to the Senate Committee on Foreign Relations.

The Department of the Treasury, with the cooperation of the Department of the State, was primarily responsible for the negotiation of the Convention and related Protocol,

Respectfully submitted,

James A. Baker III.

Enclosures: As stated.

Embassy of the United States of America

New Delhi, September 12, 1989.

His Excellency, Dr. N.K. SENGUPTA,

Secretary (Revenue),

Ministry of Finance, New Delhi.

EXCELLENCY: I have the honor to refer to the Convention between the Government of the United States of America and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income which was signed today (hereinafter referred to as "the Convention") and to conform, on behalf of the Government of the United States of America, the following understandings reached between the two Governments:

Both sides agree that a tax sparing credit shall not be provided in Article 25 (Relief from Double Taxation) of the Convention at this time. However, the Convention shall be promptly amended to incorporate a tax sparing credit provision if the United States hereafter amends its laws concerning the provision of tax sparing credits, or the United States reaches agreement on the provision of a tax sparing credit with any other country.

Both sides also agree that, for purposes of paragraph 4(c) of Article 5 (Permanent Establishment) of the Convention, a person shall be considered to habitually secure orders in a Contracting State, wholly or almost wholly for an enterprise, only if:

1. **such person frequently accepts orders for goods or merchandise on behalf of the enterprise;**
2. **substantially all of such person's sales-related activities in the Contracting State consist of activities for the enterprise;**
3. **such person habitually represents to persons offering to buy goods or merchandise that acceptance of an order by such person constitutes the agreement of the enterprise to supply goods or merchandise under the terms and conditions specified in the order; and**
4. **the enterprise takes actions that give purchasers the basis for a reasonable belief that such person has authority to bind the enterprise.**

I have the honor to request your Excellency to confirm the foregoing understandings of Your Excellency's Government.

Accept, Excellency, the renewed assurances of my highest consideration.

JOHN R. HUBBARD,

Ambassador.

Government of India,

Ministry of Finance, Department of Revenue,

New Delhi, September 12, 1989.

His Excellency, Dr. John R. Hubbard,

Ambassador of the United States of America,

New Delhi.

Excellency: I have the honor to acknowledge receipt of Your Excellency's Note of today's date, which reads as follows:

"I have the honor to refer to the Convention between the Government of the United States of America and the Government of the Republic of India for the Avoidance of Double Taxation and the prevention of Fiscal Evasion with Respect to Taxes on Income with was signed today (hereinafter referred to as "the Convention") and to confirm, on behalf of the Government of the United States of America, the following understanding reached between the two Governments:

Both sides agree that a tax sparing credit shall not be provided in Article 25 (Relief from Double Taxation) of the Convention at this time. However, the Convention shall be promptly amended to incorporate a tax sparing credit provision if the United States hereafter amends its laws concerning the provision of tax sparing credits, or the United States reaches agreement on the provision of a tax sparing credit with any other country.

Both sides also agree that, for purposes of paragraph 4(c) of Article 5 (Permanent Establishment) of the Convention, a person shall be considered to habitually secure orders in a Contracting State, wholly or almost wholly or an enterprise, only if:

1. **such person frequently accepts orders for goods or merchandise on behalf of the enterprise;**
2. **substantially all of such person's sales-related activities in the Contracting State consist of activities for the enterprise;**
3. **such person habitually represents to persons offering to buy goods or merchandise that acceptance of an**

order by such person constitutes the agreement of the enterprise to supply goods or merchandise under the terms and conditions specified in the order; and

4. the enterprise takes actions that give purchasers the basis for a reasonable belief that such person has authority to bind the enterprise."

I have the honor to confirm the understandings contained in Your Excellency's Note, on behalf of the Government of the Republic of India.

Accept, Excellency, the renewed assurances of my highest consideration.

N.K. Sengupta,

Secretary.

Embassy of the United States of America,

New Delhi, September 12, 1989.

His Excellency, Dr. N.K. Sengupta,

Secretary (Revenue),

Ministry of Finance, New Delhi.

Excellency: I have the honor to refer to the Convention signed today between the United States of America and the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and to inform you on behalf of the United States of America of the following:

During the course of the negotiations leading to conclusion of the Convention signed today, the negotiators developed and agreed upon memorandum of understanding intended to give guidance both to the taxpayers and the tax authorities of our two countries in interpreting aspects of Article 12 (Royalties and Fees for Included Services) relating to the scope of included services. This memorandum of understanding represents the current views of the United States Government with respect to the these aspects of Article 12, and it is my Government's understanding that it also represents the current views of the Indian Government. It is also my Government's view that a our Governments gain experience in administering the Convention, and particularly Article 12, the competent authorities may develop and publish amendments to the memorandum of understanding and further understandings and interpretations of the Convention.

If this position meets with the approval of the Government of the Republic of India, this letter and your reply thereto will indicate that our Governments share a common view of the purpose of the memorandum of understanding relating to Article 12 of the Convention. Accept, Excellency, the renewed assurances of my highest consideration.

John R. Hubbard,

Ambassador.

GOVERNMENT OF INDIA,

MINISTRY OF FINANCE, DEPARTMENT OF REVENUE,

New Delhi, September 12, 1989.

His Excellency, Dr. JOHN R. HUBBARD,

Ambassador of the United States of America,

New Delhi.

EXCELLENCY: I have the honor to acknowledge receipt of Your Excellency's Note of today's date, which reads as follows:

"I have the honor to refer to the Convention signed today between the United States of America and the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and to inform you on behalf of the United States of America of the following:

During the course of the negotiations leading to conclusion of the Convention signed today, the negotiators developed and agreed upon a memorandum of understanding intended to give guidance both to the taxpayers and the tax authorities of our two countries in interpreting aspects of Article 12 (Royalties and Fees for Including Services) relating to the scope of included services. This memorandum of understanding represents the current views of the United States Government with respect to these aspects of Article 12, and it is my Government's understanding that it also represents the current views of the Indian Government. It is also may Government's view that as our Governments gain experience in administrating the Convention, and particularly Article 12, the competent authorities may develop and publish amendments to the memorandum of understanding and further understandings and interpretations of the Convention.

If this position meets with the approval of the Government of the Republic of India, this letter and your reply thereto will indicate that our Governments share a common view of the purpose of the memorandum of understanding relating to Article 12 of the Convention."

I have the honor to confirm the understandings contained in Your Excellency's Note, on behalf of the Government of the Republic of India.

Accept, Excellency, the renewed assurances of my highest consideration.

N.K. SENGUPTA,

Secretary.

MAY 15, 1989.

U.S.-INDIA TAX TREATY

Memorandum of Understanding Concerning Fees for Included Services in Article 12

Paragraph 4 (in general)

This memorandum describes in some detail the category of services defined in paragraph 4 of Article 12 (Royalties and Fees for Included Services). It also provides examples of services intended to be covered within the definition of included services and those intended to be excluded, either because they do not satisfy the tests of paragraph 4, or because, notwithstanding the fact that they meet the tests of paragraph 4, they are dealt with under paragraph 5. The examples in either case are not intended as an exhaustive list but rather as illustrating a few typical cases. For ease of understanding, the examples in this memorandum describe U.S. persons providing services to Indian persons, but the rules of Article 12 are reciprocal in application.

Article 12 includes only certain technical and consultancy services. By technical services, we mean in this context services requiring expertise in a technology. By consultancy services, we mean in this context advisory services. The categories of technical and consultancy services are to some extent overlapping because a consultancy service could also be a technical service. However, the category of consultancy services also includes an advisory service, whether or not expertise in a technology is required to perform it.

Under paragraph 4, technical and consultancy services are considered included services only to the following extent: (1) as described in paragraph 4(a), if they are ancillary and subsidiary to the application or enjoyment of a right, property or information for which a royalty payment is made; or (2) as described in paragraph 4(b), if they make available technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design. Thus, under paragraph 4(b), consultancy services which are not of a technical nature cannot be included services.

Paragraph 4(a)

Paragraph 4(a) of Article 12 refers to technical or consultancy services that are ancillary and subsidiary to the application or enjoyment of any right, property, or information for which a payment described in paragraph 3(a) or (b) is received. Thus, paragraph 4(a) includes technical and consultancy services that are ancillary and subsidiary to the application or enjoyment of an intangible for which a royalty is received under a license or sale as described in paragraph 3(a), as well as those ancillary and subsidiary to the application or enjoyment of industrial, commercial, or scientific equipment for which a royalty is received under a lease as described in paragraph 3(b).

It is understood that, in order for a service fee to be considered "ancillary and subsidiary" to the application or enjoyment of some right, property, or information for which a payment described in paragraph 3(a) or (b) is received, the service must be related to the application or enjoyment of the right, property, or information. In addition, the clearly predominant purpose of the arrangement under which the payment of the service fee and such other payment are made must be the application or enjoyment of the right, property, or information described in paragraph 3. The question of whether the service is related to the application or enjoyment of the right, property, or information described in paragraph 3 and whether the clearly predominant purpose of the arrangement is such application or enjoyment must be determined by reference to the facts and circumstances of each case. Factors which may be relevant to such determination (although not necessarily controlling) include:

1. **the extent to which the services in question facilitate the effective application or enjoyment of the right, property, or information described in paragraph 3;**
2. **the extent to which such services are customarily provided in the ordinary course of business arrangements involving royalties described in paragraph 3;**
3. **whether the amount paid for the services (or which would be paid by parties operating at arm's length) is an insubstantial portion of the combined payments for the services and the right, property, or information described in paragraph 3;**
4. **whether the payment made for the services and the royalty described in paragraph 3 are made under a single contract (or a set of related contracts); and**
5. **whether the person performing the services is the same person as, or a related person to, the person receiving the royalties described in paragraph 3 (for this purpose, persons are considered related if their relationship is described in Article 9 (Associated Enterprises) or if the person providing the service is doing so in connection with an overall arrangement which include the payor and recipient of the royalties).**

To the extent that services are not considered ancillary and subsidiary to the application or enjoyment of some right,

property, or information for which a royalty payment under paragraph 3 is made, such services shall be considered "included services" only to the extent that they are described in paragraph 4(b).

Example (1)

***Facts*: A U.S. manufacturer grants rights to an Indian company to use manufacturing processes in which the transferor has exclusive rights by virtue of process patents or the protection otherwise extended by law to the owner of a process. As part of the contractual arrangement, the U.S. manufacturer agrees to provide certain consultancy service to the Indian company in order to improve the effectiveness of the latter's use of the processes. Such services include, for example, the provision of information and advice on sources of supply of materials needed in the manufacturing process, and on the development of sales and service literature for the manufactured product. The payments allocable to such services do not form a substantial part of the total consideration payable under the contractual arrangement. Are the payments for these services fees for "included services"?**

***Analysis*: The payments are fees for included services. The services described in this example are ancillary and subsidiary to the use of a manufacturing process protected by law as described in paragraph 3(a) of Article 12 because the services are related to the application or enjoyment of the intangible and the granting of the right to use the intangible is the clearly predominant purpose of the arrangement. Because the services are ancillary and subsidiary to the use of the manufacturing process, the fees for these services are considered fees for included services under paragraph 4(a) of Article 12, regardless of whether the services are described in paragraph 4(b).**

Example (2)

***Facts*: An Indian manufacturing company produces a product that must be manufactured under sterile conditions using machinery that must be kept completely free of bacterial or other harmful deposits. A U.S. company has developed a special cleaning process for removing such deposits from that type of machinery. The U.S. company enters into a contract with the Indian company under which the former will clean the latter's machinery on a regular basis. As part of the arrangement, the U.S. company leases to the Indian company a piece of equipment which allows the Indian company to measure the level of bacterial deposits on its machinery in order for it to know when cleaning is required. Are the payment for the services fees for included services?**

***Analysis*: In this example, the provision of cleaning services by the U.S. company and the rental of the monitoring equipment are related to each other. However, the clearly predominant purpose of the arrangement is the provision of cleaning services. Thus, although the cleaning service might be considered technical service, they are not ancillary and subsidiary" to the rental of the monitoring equipment. Accordingly, the cleaning services are not "included services" within the meaning of paragraph 4(a).**

Paragraph 4(b)

Paragraph 4(b) of Article 12 refers to technical or consultancy services that make available to the person acquiring the service technical knowledge, experience, skill, know-how, or processes, or consist of the development and transfer of a technical plan or technical design to such person. (For this purpose, the person acquiring the service shall be deemed to include an agent, nominee, or transferee of such person). This category is narrower than the category described in paragraph 4(a) because it excludes any service that does not make technology available to the person acquiring the service. Generally speaking, technology will be considered "made available" when the person acquiring the service is enabled to apply the technology. The fact that the provision of the service may require technical input by the person providing the service does not per se mean that technical knowledge, skills, etc. are made available to the person purchasing the service, within the meaning of paragraph 4(b). Similarly, the use of a product which embodies technology shall not per se be considered to make the technology available.

Typical categories of services that generally involve either the development and transfer of technical plans or technical designs, or making technology available as described in paragraph 4(b), include:

1. **engineering services (including the subcategories of bioengineering and aeronautical, agricultural, ceramics, chemical, civil, electrical, mechanical, metallurgical, and industrial engineering);**
2. **architectural services; and**
3. **computer software development.**

Under paragraph 4(b), technical and consultancy services could make technology available in a variety of settings, activities and industries. Such services may, for example, relate to any of the following areas:

1. **bio-technical services;**
2. **food processing;**
3. **environmental and ecological services;**
4. **communication through satellite or otherwise;**
5. **energy conservation;**
6. **exploration or exploitation of mineral oil or natural gas;**
7. **geological surveys;**
8. **scientific services; and**
9. **technical training.**

The following examples indicate the scope of the conditions in paragraph 4(b):

Example (3)

***Facts*: A U.S. manufacturer has experience in the use of a process for manufacturing wallboard for interior walls of houses which is more durable than the standard products of its type. An Indian builder wishes to produce this product for its own use. It rents a plant and contracts with the U.S. company to send experts to India to show engineers in the Indian company how to produce the extra-strong wallboard. The U.S. contractors work with the technicians in the Indian firm for a few months. Are the payments to the U.S. firm considered to be payments for "included services"?**

***Analysis*: The payments would be fees for included services. The services are of a technical or consultancy nature; in the example, they have elements of both types of services. The services make available to the Indian company technical knowledge, skill, and processes.**

Example (4)

***Facts*: A U.S. manufacturer operates a wallboard fabrication plant outside India. An Indian builder hires the U.S. company to produce wallboard at that plant for a fee. The Indian company provides the raw materials, and the U.S. manufacturer fabricates the wallboard in its plant, using advanced technology. Are the fees in this example payments for included services?**

***Analysis*: The fees would not be for included services. Although the U.S. company is early performing a technical service, no technical knowledge, skill, etc., a made available to the Indian company, nor is there any development and transfer of a technical plan or design. The U.S. company is merely performing a contract manufacturing service.**

Example (5)

***Facts*: An Indian firm owns inventory control software for use in its chain of retail outlets throughout India. It expands its sales operation by employing a team of travelling salesmen to travel around the countryside selling the company's wares. The company wants to modify its software to permit the salesmen to access the company's central computers for information on what products are available in inventory and when they can be delivered. the Indian firm hires a U.S. computer programming firm to modify its software for this purpose. Are the fees which the Indian firm pays treated as fees for included services?**

***Analysis*: The fees re for included services: The U.S. company clearly performs a technical service for the Indian company, and it transfers to the Indian company the technical plan (i.e., the computer program) which it has developed.**

Example (6)

***Facts*: An Indian vegetable oil manufacturing company wants to produce a cholesterol-free oil from a plant which produces oil normally containing cholesterol. An American company has developed a process for refining the cholesterol out of the oil. the Indian company contracts with the U.S. company to modify the formulas which it uses so as to eliminate the cholesterol, and to train the employees of the Indian company in applying the new formulas. Are the fees paid by the Indian company for included services?**

***Analysis*: The fees are for included services. The services are technical, and the technical knowledge is made available to the Indian company.**

Example (7)

***Facts*: The Indian vegetable oil manufacturing firm has mastered the science of producing cholesterol-free oil and wishes to market the product world-wide. It hires an American marketing consulting firm to do is computer simulation of the world market for such oil and to advise it on marketing strategies. Are the fees paid to the U.S. company for included services?**

***Analysis*: The fees would not be for included services. The American company is providing a consultancy service which involves the use of substantial technical skill and expertise. It is not, however, making available to the Indian company any technical experience, knowledge or skill, etc., nor is it transferring a technical plan or design. What is transferred to the Indian company through the service contract is commercial information., The fact that technical skills were required by the performer of the service in order to perform the commercial information service does not make the service a technical service within the meaning of paragraph 4(b). Paragraph 5 paragraph 5 of Article 12 describes several categories of services which are not intended to be treated as included services even if they satisfy the tests of paragraph 4. Set forth below are examples of cases where fees would be included under paragraph 4, but are excluded because of the conditions of paragraph 5.**

Example (8)

***Facts*: An Indian company purchases a computer from a U.S. computer manufacturer. As part of the purchase agreement, the manufacturer agrees to assist the Indian company in setting up the computer and installing the operating system, and to ensure that the staff of the Indian company is able to operate the computer. Also, as part of the purchase agreement, the seller agrees to provide, for a period of ten years, any update. Both of these service elements to the contract would qualify under paragraph 4(b) as an included service. Would either or both be excluded from the category of included services, under paragraph 5(a), because they are ancillary and subsidiary, as well as inextricably and essentially linked, to the sale of the computer?**

***Analysis*: The installation assistance and initial training are ancillary and subsidiary to the sale of the computer, and they are also inextricably and essentially linked to the sale. The computer would be of little value to the Indian purchaser without these services, which are most readily and usefully provided by the seller. The fees for installation assistance and initial training, therefore, are not fees for included services, since these services are not the predominant purpose of the arrangement.**

The services of updating the operating system and providing associated necessary training may well be ancillary and subsidiary to the sale of the computer, but they are not inextricably and essentially linked to the sale. Without the upgrades, the computer will continue to operate as it did when purchased, and will continue to accomplish the same functions. Acquiring the updates cannot, therefore, be said to be inextricably and essentially linked to the sale of the computer.

Example (9)

***Facts*: An Indian hospital purchases an X-ray machine from a U.S. manufacturer. As part of the purchase agreement, the manufacturer agrees to install the machine, to perform an initial inspection of the machine in India, to train hospital staff in the use of the machine, and to service the machine periodically during the usual warranty period (2 years). Under an optional service contract purchased by the hospital, the manufacturer also agrees to perform certain other services throughout the life of the machine, including periodic inspections and repair services, advising the hospital about developments in X-ray film or techniques which could improve the effectiveness of the machine, and training hospital staff in the application of those new developments. The cost of the initial installation, inspection, training, and warranty service is relatively minor as compared with the cost of the X-ray machine. Is any of the service described here ancillary and subsidiary, as well as inextricably and essentially linked, to the sale of the X-ray machine?**

***Analysis*: The initial installation, inspection, and training services in India and the periodic service during the warranty period and ancillary and subsidiary, as well as inextricably and essentially linked, to the sale of the X-ray machine because the usefulness of the machine to the hospital depends on this service, the manufacturer has full responsibility during the period, and the cost of the services is a relatively minor component of the contract. Therefore, under paragraph 5(a) these fees are not fees for included services, regardless of whether they otherwise would fall within paragraph 4(b).**

Neither the post-warranty period inspection and repair services, nor the advisory and training services relating to new developments are "inextricably and essentially linked" to the initial purchase of the X-ray machine. Accordingly, fees for these services may be treated as fees for included services if they meet the tests of paragraph 4(b).

Example (10)

***Facts*: An Indian automobile manufacturer decides to expand into the manufacture of helicopters. It sends a group of engineers from its design staff to a course of study conducted by the Massachusetts Institute of Technology (MIT) for two years to study aeronautical engineering. The Indian firm pays tuition fees to MIT on behalf of the firm's employees. Is the tuition fee a fee for an included service within the meaning of Article 12?**

***Analysis*: The tuition fee is clearly intended to acquire a technical service for the firm. However, the fee paid is for teaching by an educational institution, and is, therefore, under paragraph 5(c), not an included service. It is irrelevant for this purpose whether MIT conducts the course on its campus or at some other location.**

Example (11)

***Facts*: As in Example (10), the automobile manufacturer wishes to expand into the manufacture of helicopters. It approaches an Indian university about establishing a course of study in aeronautical engineering. The university contracts with a U.S. helicopter manufacturer to send an engineer to be a visiting professor of aeronautical engineering on its faculty for a year. Are the amounts paid by the university for these teaching services fees for included services?**

***Analysis*: The fees are for teaching in an educational institution. As such, pursuant to paragraph 5(c), they are not fees for included services.**

Example (12)

***Facts*: An Indian wishes to install a computerized system in his home to control lighting, heating and air conditioning, a stereo sound system and a burglar and fire alarm system. He hires an American electrical engineering firm to design the necessary wiring system, adapt standard software, and provide instructions for installation. Are the fees paid to the American firm by the Indian individual fees for included services?**

***Analysis*: The services in respect of which the fees are paid are of the type which would generally be treated as fees for included services under paragraph 4(b). However, because the services are for the personal use of the individual making the payment, under paragraph 5(d) the payments would not be fees for included services.**

LETTER OF TRANSMITTAL

The White House, October 31, 1989.

To the Senate of the United States:

I transmit herewith for Senate advice and consent to ratification the Convention between the Government of the

United States of America and the Government of the Republic of India for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income, together with a related Protocol, signed at New Delhi on September 12, 1989. I also transmit the report of the Department of State on the convention.

The convention would be the first tax treaty between the United States and India. It includes special provisions that take into account India's status as a developing nation and that reflect changes in U.S. tax treaty policy resulting from the Tax Reform Act of 1986.

Of particular importance are the provisions limiting the withholding tax rates on various categories of investment income, as well as those designed to prevent third-country residents from taking unwarranted advantage of the convention by routing income from one Contracting State through an entity created in the other. The convention also provides for the exchange of information by the competent authorities of the Contracting States.

I recommend the Senate give early and favorable consideration to the convention, together with a related protocol, and give its advice and consent to ratification.

George Bush.

Memorandum Of Understanding Regarding Deferment Of Assessment And/Or Suspension Of Collection Of Taxes During Mutual Agreement Procedure

Having regard to the hardship faced by the taxpayers during the pendency of a mutual agreement procedure, the Competent Authorities of India and the United States under the Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (the "Convention") have determined and agreed that efficient processing of Mutual Agreement Procedure ("MAP") cases will be facilitated by deferring assessment or suspending collection of any amounts of tax, including also any related interest or penalties, for any taxable years which are the subject of MAP proceedings.

WHEREAS:

(A) The Competent Authorities have arranged and desired to agree that with regard to amounts of taxes covered under Article 2 of the Convention and potentially payable to the government of the United States, the Internal Revenue Service will either defer assessment or suspend collection proceedings pursuant to its published procedures regarding MAP proceedings (currently set forth in Rev. Proc. 2002-52 or any successor procedure), until putting into effect a mutually agreed disposition of the MAP proceedings concerning the amounts in question; and

(B) The Competent Authorities have arranged and desired to agree that with regard to amounts of taxes covered under Article 2 of the Convention and potentially payable to the government of India, the Assessing Officer will suspend collection until putting into effect a mutually agreed disposition of the MAP proceedings concerning the amounts in question.

NOW THEREFORE, in consideration of the premises, covenants and conditions herein contained and in implementing this arrangement:

IT IS HEREBY AGREED between the Competent Authorities as follows:

(1) The tax authorities of India and the United States shall retain the right to demand security in appropriate cases, as deemed fit and necessary to avoid prejudicing the interests of their respective governments.

(2) In India, as security, a taxpayer shall provide an irrevocable Bank Guarantee issued by any scheduled bank, or by an Indian branch of a foreign bank approved by the Reserve Bank of India to carry out banking business in India, as per annexure 'A' to this Memorandum.

(3) In the United States, as security, a taxpayer shall, upon demand, provide an irrevocable Letter of Credit issued by a United States bank that is a member of the Federal Reserve System, or by a United States branch or agency of a foreign bank that is on the National Association of Insurance Commissioners list of banks from which a Letter of Credit may be accepted.

(4) The amount, if any, for which security is demanded under paragraph (2) or (3) above, as the case may be, shall not exceed the amount of additional tax proposed or demanded by the tax authority requiring the security (aggregated for all the period(s) pending before the Competent Authorities), as adjusted by the Assessing Officer in accordance with domestic laws, and subject to further adjustment for interest on these amounts calculated at the statutory rate on non-payments.

(5) Collection and assessment (if applicable) of any interest or penalty levied from the concerned taxpayer, in relation to amounts suspended from collection or deferred from assessment (if applicable) under this Agreement, shall also be suspended.

(6) The amounts of tax(es) identified under Recitals (A) and (B) above, shall include but are not limited to:

(i) Tax demands that have arisen as a result of tax audit or appeal proceedings pending at the time of this agreement.

(ii) Tax demands, as a result of a tax assessment or re-assessment proceeding, or a tax appeal, or on a review by a Commissioner of Income Tax of an assessment (or re-assessment) proceeding on the grounds that it is prejudicial to the interests of the revenue that could arise subsequent to this agreement.

(iii) Withholding tax on income or other similar advance taxes that are the subject of MAP proceedings for prior, current or future taxable years.

(7) The Competent Authorities shall endeavour to either resolve or close the case within a period of two years from the date on which one Competent Authority notifies the other that the application from the Taxpayer(s) for assistance under the MAP has been received.

(8) Any draw-down upon a Bank Guarantee or Letter of Credit referred to in paragraph (2) or (3) above will be authorised only after notice by one Competent Authority to the other.

(9) In the event of a lapse of security under paragraph (2) or (3), the taxpayer shall be permitted to substitute another form of security under such paragraph, provided such substitution takes effect not less than 30 days prior to the lapse of the prior security. Such substitution will relieve the bank which provided the first Bank Guarantee or Letter of Credit from its obligations to the concerned Government of India or the United States under that first security.

(10) The terms of this Memorandum may be reviewed by the Competent Authorities at anytime in the future upon the request of either party.

ANNEXURE A

To,

The President of India acting through and represented by

[*Designation*], Income Tax Department,

Ministry of Finance, Government of India, New Delhi

Bank Guarantee

Bank Guarantee as security for keeping the recovery of tax demand in abeyance during the pendency of a Mutual Agreement Procedure ("MAP")

[*Applicable in case of non-resident assessees, and Indian companies and other entities affiliated with United States companies, who have invoked the Mutual Agreement Procedure*]

This Deed of Bank Guarantee made this _____ day of _____, 20__, by [*INSERT name and address of Guaranteeing Bank*] (hereinafter called "the Bank", which expression shall, unless excluded by or repugnant to the context, include its successors and assignees) to the President of India acting through and represented by [*Designation*], Income Tax Department, Ministry of Finance, Government of India, New Delhi (hereinafter called "the Government").

WHEREAS the Government has agreed that [*INSERT name, address, permanent account number of the Assessee*] (hereinafter called "the Assessee", which expression shall, unless excluded by or repugnant to the context, include its successors and assignees) shall furnish a Bank Guarantee in respect of a demand of Rs. [*INSERT Amount of Tax in dispute*] for the assessment year(s) _____, in lieu of which the recovery of any part of such demand shall not be enforced until 30 days after the Assessing Officer receives written notice of the MAP Agreement between the Competent Authorities of the Governments of India and the United States, and the Assessee will not be treated as in default for the above assessment year(s);

AND WHEREAS THE Bank has at the request of the Assessee agreed to execute these presents:

NOW THEREFORE THIS DEED WITNESSES AS FOLLOWS

In consideration of the Government agreeing to treat the Assessee as not in default for Rs [*INSERT Amount of Tax in dispute, plus interest specified in paragraph (1) below*] for the assessment year(s) _____,

(1) The Bank irrevocably guarantees and undertakes, for the term provided in paragraph (2) below, that the Bank shall indemnify and keep indemnified the Government to the extent of the said sum of Rs [*INSERT Amount of Tax in dispute*] (Rupees [*written text*]) and interest accruing at the rate specified in the Income Tax Act of 1961 as amended from time to time, for non-payment of taxes on this amount after [*INSERT date from which recovery could otherwise be made*] or any amount as adjusted by the order of the Assessing Officer which may be passed after the furnishing of the guarantee. On advice from the Government that the Assessee has failed and neglected to observe any of its obligations to the Government with regard to the terms and conditions of the agreements between the Assessee and the Government that may underlie this Bank Guarantee, the decision of the Government as to whether any amount should be paid out by the Bank to the Government hereunder shall be final and binding.

(2) The Bank further agrees that the guarantee herein contained shall remain in full force and effect for a period of 3 years from the date hereof, i.e., till [*INSERT date*]; and further agrees to renew this guarantee for another 3 years on the following terms: the Bank will provide the Government with written notice no later than 60 days prior to the expiration date of this Bank Guarantee if the taxpayer has not renewed the agreements between the Assessee and the Bank that underlie this Bank Guarantee for an additional period of 3 years. If the Government does not receive a renewal of this Bank Guarantee or a substitute Bank Guarantee for the amounts of tax and interest in dispute prior to 30 days before the expiration date of this Bank Guarantee, the Government may instruct the Bank to pay the guaranteed amounts prior to expiration of the Bank Guarantee.

Provided further that, notwithstanding any other things contained herein, the liabilities of the Bank shall be limited to

the maximum of the guaranteed amount of Rs. [*INSERT amount of tax in dispute*] (Rupees [*INSERT written text*]), as increased by interest pursuant to paragraph (1) during the term of this Bank Guarantee; and unless a claim in writing is lodged with the Bank, or action to enforce the claim under the guarantee is filed or initiated against the Bank, within six months from the date of expiry of the guarantee period fixed hereunder or where such period is extended under the terms of this guarantee from the date of such extended period as the case may be, all the rights of the Government under this guarantee shall be forfeited and the Bank shall be relieved and discharged from liabilities hereunder.

(3) The obligations of the Bank to the Government under this Bank Guarantee will terminate upon the occurrence of any of the following for the taxable years in question: (i) the payment by the Bank or the Assessee to the Government of the guaranteed amounts; (ii) the payment by the Assessee to the Government of all amounts owed, as agreed to by the Competent Authorities in a MAP Agreement; (iii) a MAP Agreement by the Competent Authorities that the Government will not seek to recover any part of the previously-demanded amounts; or (iv) the Assessee furnishes to the Government similar security from another Bank.

(4) The guarantee herein contained shall not be discharged or affected by any change in the constitution either of the Assessee or of the Bank.

(5) The Government shall have the fullest liberty without affecting the guarantee to postpone for any time, or from time to time, any of the powers exercisable by it against the Assessee, or to either enforce or forbear any of the terms and conditions under this guarantee or under the Income Tax Act and Income Tax Rules, and the Bank shall not be released from its liabilities under this guarantee by any exercise by the Government of the liberty with reference to the matter aforesaid or by reasons of time being given to the Assessee, or by any other act of forbearance or enforcement on the part of the Government, or by any indulgence by the Government to the Assessee, or by any other matter or thing whatsoever which under the law relating to sureties would but for these provisions have the effect of so releasing the Bank from its such liability.

The Bank hereby agrees and undertakes that any claim which the Bank may have against the Assessee shall be subject and subordinate to the prior payment and performance in full of all the obligations of the Bank hereunder and the Bank will not without prior written consent of the Government exercise any legal rights or remedies of any kind in respect of any such payment or performance so long as the obligations of the Bank hereunder remain owing and outstanding, regardless of the insolvency, liquidation or bankruptcy of the Assessee or otherwise howsoever. The Bank will not counter claim or set off against its liabilities to the Government hereunder any sum outstanding to the credit of the Government with it.

(6) This Bank Guarantee shall be governed by and construed in accordance with the laws of the Republic of India (without regard to its principles of conflict of laws).

(7) The Bank undertakes not to revoke this Guarantee during its currency except with the previous consent of the Government in writing.

(8) Notwithstanding anything stated above, liability of the Bank under this guarantee is restricted to Rs. [*INSERT Amount of Tax in dispute, plus interest specified in paragraph (1) above*] (Rupees [*written text*]) and is valid for the period(s) described in paragraph (2) above. Unless a demand or claim under this guarantee is lodged with the Bank on or before [*INSERT date, as established in paragraph (2) above*], all rights of the Government under the said guarantee shall be forfeited and the Bank shall be relieved and discharged from all liabilities thereunder whether or not this document shall have been returned to the Bank.

IN WITNESS WHEREOF, the Bank, through its duly authorized representative, has set its hand stamp on this _____ Day of _____ at _____

Witness	**For and on Behalf of the Bank**
(Signature)	**(Designation with Bank Stamp)**
Name	**(Attorney as per power of Attorney No. _____)**
	Date

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Working Papers

Worksheet 36 List of Comprehensive Double Taxation Agreements and Related Protocols Signed by India as of August 1, 2010

Treaty Partner	Type of Agreement	Concerning Taxes on	Date of Signature	Date of Entry Into Force	Status
Algeria	Treaty	Income	Jan. 25, 2001	—-	Not yet in force
Armenia	Treaty	Income	Oct. 31, 2003	Sep. 9, 2004	In force
Australia	Treaty	Income	Jul. 25, 1991	Dec. 30, 1991	In force

Austria	**Treaty**	**Income**	**Sep. 24, 1963**	**Apr. 5, 1965**	**Terminated**
	Treaty and protocol	**Income**	**Nov. 8, 1999**	**Sep. 5, 2001**	**In force**
Bangladesh	**Treaty**	**Income**	**Aug. 27, 1991**	**May 27, 1992**	**In force**
Belarus	**Treaty and protocol**	**Income and capital**	**Sep. 27, 1997**	**Jul. 17, 1998**	**In force**
Belgium	**Treaty and protocol**	**Income**	**Feb. 7, 1974**	**Jul. 6, 1975**	**Terminated**
	2nd protocol		**Oct. 20, 1984**	**Jan. 23, 1988**	**Terminated**
	Treaty and protocol	**Income**	**Apr. 26, 1993**	**Oct. 1, 1997**	**In force**
Botswana	**Treaty**	**Income**	**Dec. 8, 2006**	**Jan. 30, 2008**	**In force**
Brazil	**Treaty and protocol**	**Income**	**Apr. 26, 1988**	**Mar. 11, 1992**	**In force**
Bulgaria	**Treaty and protocol**	**Income and capital**	**May 26, 1994**	**Jun. 23, 1995**	**In force**
Canada	**Treaty and protocol**	**Income**	**Oct. 30, 1985**	**Sep. 16, 1986**	**Terminated**
	Treaty and protocol	**Income and capital**	**Jan. 11, 1996**	**May 6, 1997**	**In force**
Ceylon	**Treaty**	**Income**	**Sep. 10, 1956**	**Feb. 8, 1957**	**Terminated**
China (PRC)	**Treaty and protocol**	**Income**	**Jul. 18, 1994**	**Nov. 19, 1994**	**In force**
Cyprus	**Treaty**	**Income and capital**	**Jun. 13, 1994**	**Dec. 21, 1994**	**In force**
Czechoslovakia	**Treaty and protocol**	**Income**	**Jan. 27, 1986**	**Mar. 13, 1987**	**Terminated for Czech Republic, in force for Slovak Republic**
Czech Republic	**Treaty**	**Income and capital**	**Oct. 1, 1998**	**Sep. 27, 1999**	**In force**
Denmark	**Treaty**	**Income**	**Sep. 16, 1959**	**Mar. 1, 1960**	**Terminated**
	Treaty and protocols [1]	**Income and capital**	**Mar. 8, 1989**	**Jun. 13, 1989**	**In force**
Finland	**Treaty**	**Income**	**Jun. 23, 1961**	**Dec. 29, 1961**	**Terminated**
	Treaty	**Income and capital**	**Jun. 10, 1983**	**Nov. 18, 1984**	**In force**
	Protocol		**Apr. 9, 1997**	**Jan. 10, 1998**	**In force**
	Treaty and protocol	**Income**	**Jan. 15, 2010**	**Apr. 19, 2010**	**In force**
France	**Treaty**	**Income**	**Mar. 26, 1969**	**Mar. 20, 1970**	**Terminated**
	Treaty and protocol	**Income and capital**	**Sep. 29, 1992**	**Aug. 1, 1994**	**In force**
Germany	**Treaty**	**Income**	**Mar. 18, 1959**	**Oct. 13, 1960**	**Terminated**
	Protocol		**Jun. 28, 1984**	**Sep. 26, 1985**	**Terminated**
	Treaty and protocol	**Income, capital**	**Jun. 19, 1995**	**Oct. 26, 1996**	**In force**
Greece	**Treaty**	**Income**	**Feb. 11, 1965**	**Mar. 17, 1967**	**In force**
Hungary	**Treaty and protocol**	**Income**	**Oct. 30, 1986**	**Jan. 7, 1987**	**Terminated**
	Treaty and protocol	**Income**	**Nov. 3, 2003**	**Mar. 4, 2005**	**In force**
Iceland	**Treaty and protocol**	**Income**	**Nov. 23, 2007**	**Dec. 21, 2007**	**In force**
Indonesia	**Treaty and protocol**	**Income**	**Aug. 7, 1987**	**Dec. 19, 1987**	**In force**
Ireland	**Treaty and protocol**	**Income**	**Nov. 6, 2000**	**Dec. 26, 2001**	**In force**
Israel	**Treaty and protocol**	**Income and capital**	**Jan. 29, 1996**	**May 15, 1996**	**In force**
Italy	**Treaty and protocol**	**Income**	**Jan. 12, 1981**	**Apr. 8, 1986**	**Terminated**

	Treaty and protocol	Income	Feb. 19, 1993	Nov. 23, 1995	In force
Japan	Treaty and protocol	Income	Jan. 5, 1960	Jun. 13, 1960	Terminated
	2nd Protocol		Apr. 8, 1969	Nov. 15, 1970	Terminated
	Treaty	Income	Mar. 7, 1989	Dec. 29, 1989	In force
	Protocol		Feb. 24, 2006	June 28, 2006	In force
Jordan	Treaty and protocol	Income	Apr. 20, 1999	Oct. 16, 1999	In force
Kazakhstan	Treaty	Income and capital	Dec. 9, 1996	Oct. 2, 1997	In force
Kenya	Treaty	Income	Apr. 12, 1985	Aug. 20, 1985	In force
Korea (ROK)	Treaty and protocol	Income	Jul. 19, 1985	Aug. 1, 1986	In force
Kuwait	Treaty	Income	June 15, 2006	Oct. 17, 2007	In force
Kyrgyzstan	Treaty and protocol	Income	Apr. 13, 1999	Jan. 10, 2001	In force
Libya	Treaty	Income	Mar. 2, 1981	Jul. 1, 1982	In force
Luxembourg	Treaty and protocol	Income and capital	Jun. 2, 2008	Jul. 9, 2009	In force
Malaysia	Treaty and protocol	Income	Oct. 25, 1976	Apr. 1, 1977	Terminated
	Treaty and protocol	Income	May 14, 2001	Aug. 14, 2003	In force
Malta	Treaty	Income	Sep. 28, 1994	Feb. 8, 1995	In force
Mauritius	Treaty	Income	Aug. 24, 1982	Dec. 6, 1983	In force
Mexico	Treaty and protocol	Income	Sep. 10, 2007	Feb. 1, 2010	In force
Mongolia	Treaty	Income and capital	Feb. 22, 1994	Mar. 29, 1996	In force
Morocco	Treaty	Income	Oct. 30, 1998	Jan. 30, 2000	In force
Myanmar	Treaty and protocol	Income	Apr. 2, 2008	Jan. 30, 2009	In force
Namibia	Treaty	Income	Feb. 15, 1997	Feb. 16, 1999	In force
Nepal	Treaty	Income	Jan. 18, 1987	Nov. 1, 1988	In force
Netherlands	Treaty and protocol	Income and capital	Jul. 30, 1988	Jan. 21, 1989	In force
New Zealand	Treaty	Income	Oct. 17, 1986	Dec. 23, 1986	In force
	Protocol		Aug. 29, 1996	Jan. 9, 1997	In force
	2nd Protocol		June 21, 1999	Dec. 17, 1999	In force
Norway	Treaty	Income	Jul. 20, 1959	Mar. 23, 1960	Terminated
	Treaty and protocol	Income and capital	Dec. 31, 1986	Jul. 2, 1987	In force
Oman	Treaty and protocol	Income	Apr. 2, 1997	Jun. 3, 1997	In force
Pakistan	Treaty	Income	Dec. 10, 1947	Dec. 10, 1947	Terminated
Philippines	Treaty and protocol	Income	Feb. 12, 1990	Mar. 21, 1994	In force
Poland	Treaty	Income	Jun. 21, 1989	Oct. 26, 1989	In force
Portugal	Treaty and protocol	Income	Sep. 11, 1998	Apr. 30, 2000	In force
Qatar	Treaty	Income	Apr. 7, 1999	Jan. 15, 2000	In force
Romania	Treaty	Income	Mar. 10, 1987	Nov. 14, 1987	In force
Russia	Treaty and protocol	Income	Mar. 25, 1997	Apr. 11, 1998	In force
Saudi Arabia	Treaty	Income	Jan. 25, 2006	Nov. 1, 2006	In force
Serbia and Montenegro	Treaty and protocol	Income and capital	Feb. 8, 2006	Sep. 23, 2008	In force [4]
Singapore	Treaty	Income	Apr. 20, 1981	Jan. 6, 1982	Terminated
	Treaty	Income	Jan. 24, 1994	May 24, 1994	In force
	Protocol		Jun. 29, 2005	Aug. 1, 2005	In force

Slovenia	Treaty and protocol	Income and capital	Jan. 13, 2003	Feb. 17, 2005	In force
South Africa	Treaty and protocol	Income	Dec. 4, 1996	Nov. 28, 1997	In force
Soviet Union	Treaty	Income	Nov. 20, 1988	Jun. 5, 1989	See below [2]
Spain	Treaty and protocol	Income and capital	Feb. 8, 1993	Jan. 12, 1995	In force
Sri Lanka	Treaty and protocol	Income and capital	Jan. 27, 1982	Mar. 24, 1983	In force
Sudan	Treaty	Income	Oct. 22, 2003	Apr. 15, 2004	In force
Sweden	Treaty	Income	Jul. 30, 1958	Jan. 23, 1959	Terminated
	Treaty and protocol	Income and capital	Jun. 7, 1988	Dec. 12, 1988	Terminated
	Treaty and protocol	Income and capital	Jun. 24, 1997	Dec. 25, 1997	In force
Switzerland	Treaty and protocol	Income	Nov. 2, 1994	Dec. 29, 1994	In force
	2nd Protocol		Feb. 16, 2000	Dec. 20, 2000	In force
Syria	Treaty	Income	Feb. 6, 1984	Jun. 25, 1985	Terminated
	Treaty and protocol	Income	Jun. 18, 2008	Nov. 10, 2008	In force
Tajikistan	Treaty	Income	Nov. 20, 2008	Apr. 10, 2009	In force
Tanzania	Treaty	Income	Sep. 5, 1979	Oct. 16, 1981	In force
Thailand	Treaty	Income	Mar. 22, 1985	Mar. 13, 1986	In force
Trinidad and Tobago	Treaty	Income	Feb 8, 1999	Oct. 13, 1999	In force
Turkey	Treaty and protocol	Income	Jan. 31, 1995	Dec. 30, 1996	In force
Turkmenistan	Treaty and protocol	Income and capital	Feb. 25, 1997	Jul. 7, 1997	In force
Uganda	Treaty	Income	Apr. 30, 2004	Aug. 27, 2004	In force
Ukraine	Treaty	Income and capital	Apr. 7, 1999	Oct. 31, 2001	In force
United Arab Emirates	Treaty and protocol	Income and capital	Apr. 29, 1992	Sep. 22, 1993	In force
	2nd Protocol		Mar. 26, 2007	Nov. 28, 2007	In force
United Arab Republic [3]	Treaty	Income	Feb. 20, 1969	Sep. 30, 1969	In force
United Kingdom	Treaty	Income	Apr. 16, 1981	Oct. 21, 1981	Terminated
	Treaty	Income	Jan. 25, 1993	Oct. 25, 1993	In force
United States	Treaty	Income	Nov. 10, 1959	—-	Never entered into force
	Treaty and protocol	Income	Sep. 12, 1989	Dec. 18, 1990	In force
Uzbekistan	Treaty	Income and capital	Jul. 29, 1993	Jan. 25, 1994	In force
Vietnam	Treaty	Income	Sep. 7, 1994	Feb. 2, 1995	In force
Zambia	Treaty	Income	Jun. 5, 1981	Jan. 18, 1984	In force

[1] The 1989 India-Denmark treaty is extended to the Faroe Islands in accordance with terms of the second of the two Protocols to that treaty.

[2] The status of the treaty with the former Soviet Union is as follows: New treaties are in effect with Armenia, Belarus, Kazakhstan, Kyrgyzstan, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan. The status of the 1988 India-Soviet Union treaty with respect to all other CIS Member States is uncertain.

[3] I.e., Egypt.

[4] Serbia and Montenegro ceased to exist on June 5, 2006. The India-Serbia and Montenegro treaty will remain applicable in relation to Serbia. India has yet to confirm whether it will apply the treaty in relation to Montenegro.

OFFICIAL

Statutes (as amended):

The Companies Act, 1956.

Securities Exchange Board of India Act, 1992.

Industrial (Development and Regulation) Act, 1951.

Foreign Exchange Management Act, 1999.

The Competition Act, 2000.

Limited Liability Partnership Act, 2008.

Income Tax Act, 1961.

Wealth Tax Act, 1957.

Gift Tax Act, 1958.

Central Excise Act, 1944.

The Central Excise Tariff Act, 1985.

The Customs Act, 1962.

The Customs Tariff Act, 1975.

Indian Stamp Act, 1899.

Rules:

Income Tax Rules, 1962.

Wealth Tax Rules, 1957.

Notifications Issued under Foreign Exchange Management Act, 1999.

Foreign Income Portfolios
Business Operations Abroad (Countries)
Portfolio 966-4th: Business Operations in India
Bibliography

UNOFFICIAL

Reference Books:

Chaturvedi & Pisthisaria, *Income Tax Law*, Fifth Edition 2001, Wadhwa and Company.

Harish D.M., *Harish on Income Tax*, First Edition, 1998, Snow White Publications Pvt. Ltd., Bombay.

Kanga, Palkhivala & Vyas, *The Law and Practice of Income Tax*, Ninth Edition, 2004, Lexis Nexis (A division of Reed Elsevier India Pvt. Ltd.), New Delhi.

Mittal D.P., *Indian Double Taxation Agreements & Tax Laws*, Fifth Edition, 2008, Taxmann Allied Services (P) Ltd., New Delhi.

Ramaiya A, *Guide to the Companies Act,* Sixteenth Edition Reprint, 2006, Wadhwa and Company, Nagpur.

***Foreign Exchange Management Manual*, An authorized publication of the Reserve Bank of India, Fifteenth Edition, 2009, Taxmann Publications Pvt. Ltd., New DeInternlhi.**

Sampath Iyengar, *Law of Income Tax*, Ninth Edition, 1998, Bharat Law House Pvt. Ltd., New Delhi.

Santhanam R., *Tax Planning for Collaborations*, Fifth Edition, 2001, Commercial Publishing House, New Delhi.

***International Taxation — A Compendium,* Revised Edition, 2008, The Chamber of Tax Consultants, Mumbai.**

Law Reports:

Income Tax Reports (ITR), Company Law Institute of India Private Limited, Chennai.

Income Tax Tribunal Decisions (ITD), Taxman Publication, New Delhi.

Contact us at http://www.bna.com.proxy.wm.edu/contact/index.html or call 1-800-372-1033

ISSN 1947-3923
Copyright © 2010, The Bureau of National Affairs, Inc. Reproduction or redistribution, in whole or in part, and in any form, without express written permission, is prohibited except as permitted by the BNA Copyright Policy.
http://www.bna.com.proxy.wm.edu/corp/index.html#V