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Investing in India

A Brief Overview of the Regulatory Framework

Atul Vaid

+91 98861 21328

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Vital Statistics - Physical & Political



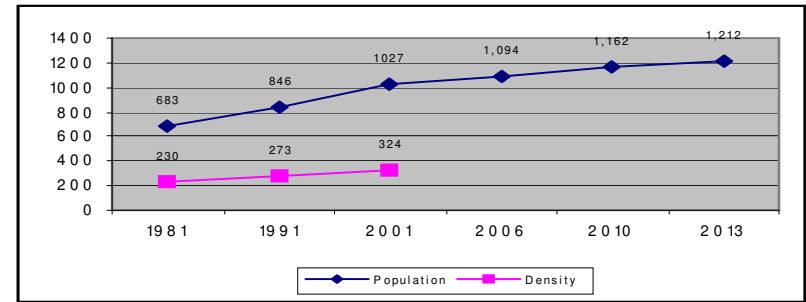
- 3.3 million square kilometers (World's seventh largest country)
- Range of climatic conditions - snowbound, tropical, desert, evergreen
- Legislature
 - ▶ Federal format – 28 Federal states and 7 Union territories,
 - ▶ 2-tier government comprising the Lok Sabha (Lower House) and Rajya Sabha (Upper House) supported by State Legislatures and local bodies.
 - ▶ Head of State is the President, Head of Government is the Prime Minister
- Executive
 - ▶ Consists of President, Vice-President and Council of Ministers led by the Prime Minister
- Judiciary
 - ▶ Independent of executive, National-level Supreme Court and State-Level High Courts



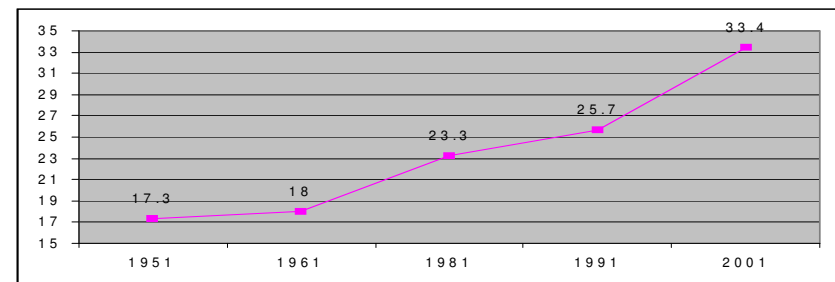
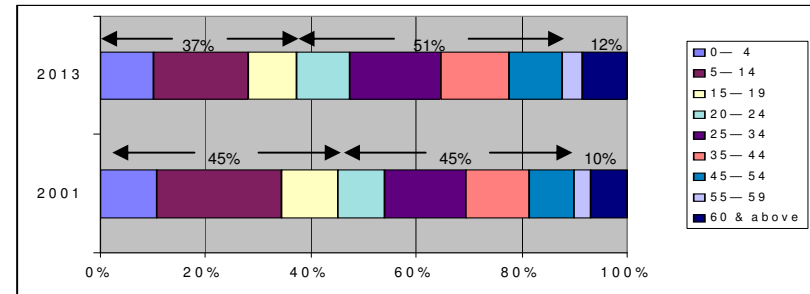
Vital Statistics – Population, Age Structure & Urbanization



- Despite slowing population growth rates (decadal CAGR of 2.41% to 2.18% 1981-2001), the population will reach 1.21 billion by 2013
- India will be one of the youngest countries in the world in 2013, with a median age of 29.
- The working age population will increase, with over half the population in the key income-earning 20-55 age-group.
- People are increasingly located in urban centers. The level of urbanization is accelerating, with increasing concentration of population in fewer towns.



Source: Census of India; Pop. in Million; Density in Per Sqkm



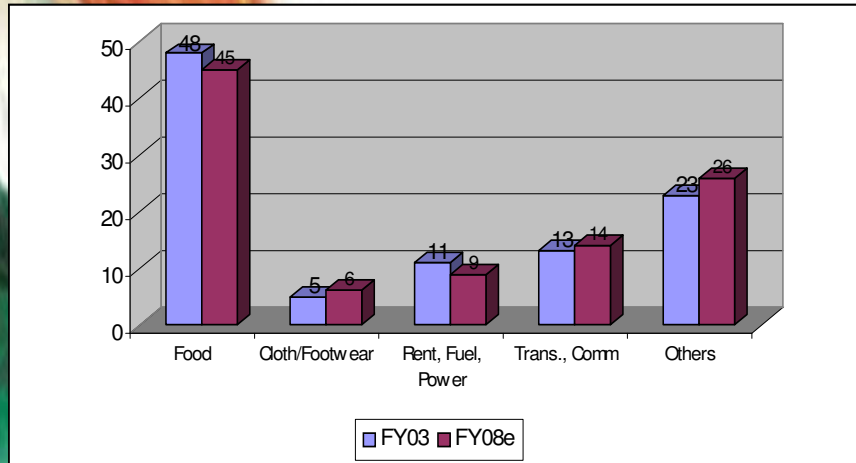
Source: Census of India; Tata Services

Vital Statistics – Income Categories, Purchase Patterns

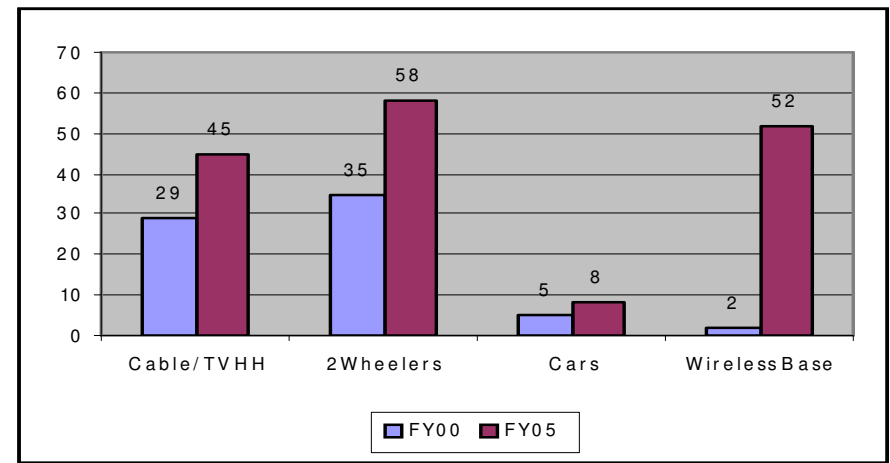
- Faster economic growth has improved affluence levels, and is driving consumption.
- Share of discretionary items in spend seems to be increasing
- Increasing penetration of durables.

Class	AHI	2001/02		2006/07		Growth
		MIln	%	MIln	%	
Very rich	Above 360,001	2.6	1%	5.2	3%	100%
Consuming	80,001-360,000	46.4	26%	75.5	38%	63%
Climbers	40,001-80,000	74.4	41%	81.7	41%	10%
Aspirants	28,001-40,000	33.1	18%	20.2	10%	-39%
Destitutes	<28,000	24.1	13%	16.5	8%	-32%
		180.6	100%	199.1	100%	10%

AHI = Annual Household Income in INR; MIln = Million Households; Source: NCAER



Source: Merrill Lynch, NSS

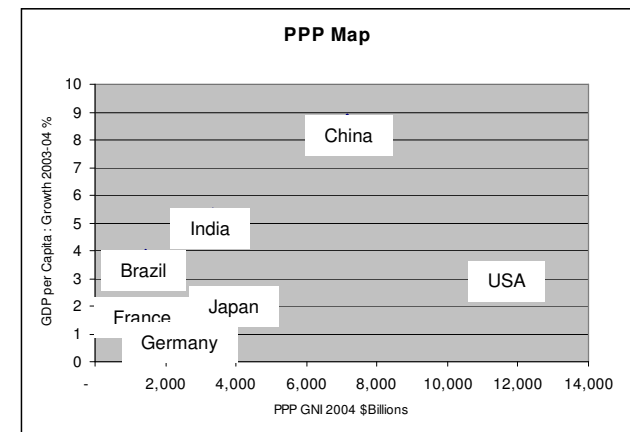
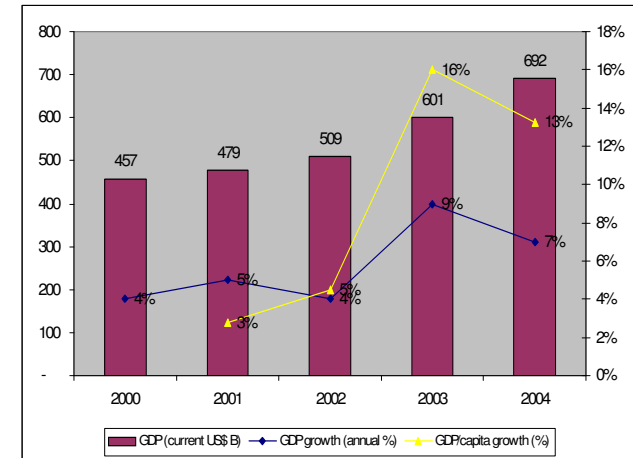


Source: Merrill Lynch, NSS

Vital Statistics – Accelerating Economic Growth



- A booming economy, of US\$ 830 Billion (GDP at current prices), growing at an average of 5.8% per annum over the last 5 years, accelerating to over 9% for the last two years, and expected to touch ~10% during this year.
- Good GDP per capita growth, accelerating strongly in the last 2 years
- Non-traditional source of growth of GDP
 - ▶ 1994-2003 : Agri. share down from 35% to 26%; Manufacturing down from 14.8% to 13.6%
 - ▶ World's 4th largest economy (purchasing power parity)
- Amongst the fastest per capita economic growths
 - ▶ 5.4% vs. 2.9% globally



Source: World Bank

Vital Statistics – Trade & Investment



- A robust and networked financial system
 - ▶ Commercial bank network has over 71,000 branches
 - ▶ Aggregate Deposits of US\$ 477 Billion
 - ▶ 22 Stock Exchanges with a market capitalization of over US\$ 950 Billion (as on May 3 2007).
 - ▶ Amount raised in primary market 2006-07 was US\$ 28 Billion

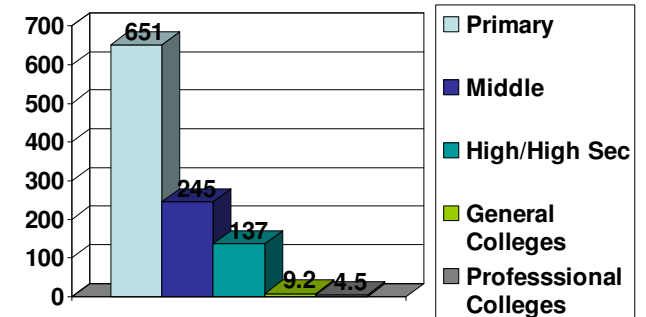
- Trade – membership of various trade blocs
 - ▶ Exports US\$Bn. - 102.7
 - ▶ Imports US\$Bn. - 149.2

- Foreign Direct Investment accelerating
 - ▶ Net FDI Apr2005-Mar2006 was US\$ 7.7 Billion
 - ▶ Net FDI Apr2006-Mar2007 was US\$ 17.7 Billion

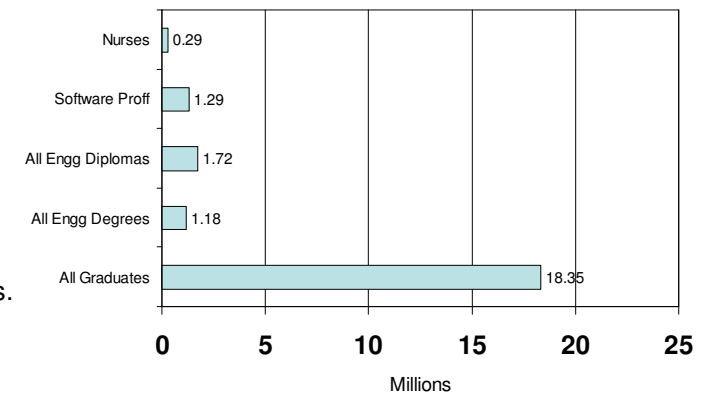
Vital Statistics – Education

- All levels of education, from primary to higher education, are overseen by Department of Higher Education (India) and Department of School Education and Literacy, and heavily subsidized by the Indian government.
- The system is divided into preprimary, primary, middle, secondary (or high school), and higher levels. Preprimary is usually composed of Lower Kindergarten and Higher Kindergarten. Primary school includes children of ages six to eleven, organized into classes one through five. Secondary school pupils aged eleven through fifteen are organized into classes six through ten, and higher secondary school students ages sixteen through seventeen are enrolled in classes Eleven through Twelve.
- In India, the main types of schools are those controlled by:
 - ▶ The state government boards like SSLC, in which the vast majority of Indian school-children are enrolled,
 - ▶ The Central Board of Secondary Education (CBSE) board,
 - ▶ The Council for the Indian School Certificate Examinations (CISCE) board,
 - ▶ National Open School
- Higher education in India has evolved in distinct and divergent streams with each stream monitored by an apex body, indirectly controlled by the Ministry of Human Resource Development. and funded by the state governments.
- There are 18 important universities called Central Universities, which are maintained by the Union Government. The increased funding of the central universities give them an advantage over state competitors.
- The private sector is strong in Indian higher education.
- Accreditation for universities in India are required by law unless it was created through an act of Parliament. Accreditation is overseen by autonomous institutions established by the University Grants Commission, such as All India Council for Technical Education (AICTE), the Distance Education Council (DEC), and others.

Institutions 2002-03 ('000)



Education Streams - Graduates 2006



Key Laws Relating to Business

- 
- Central Excise Act
 - Companies Act
 - Competition Act
 - Consumer Protection Act
 - Customs Act
 - Customs Tariff Act
 - Environment Protection Act
 - Factories Act
 - Foreign Exchange Management Act
 - Income Tax Act
 - Industrial Disputes Act & Workmen's Compensation Act
 - Industries (Development & Regulation) Act
 - Information Technology Act
 - Money Laundering Act
 - Patents Act, Copyright Act, Trade Marks Act
 - Central Sales Tax Act
 - Special Economic Zones Act
 - Right to Information Act

Regulatory Bodies Relevant to Foreign Investments


Inward

- Investment Commission
- Ministry of Commerce and Industry (MOCI)
- Secretariat for Industrial Assistance (within Ministry of Commerce and Industry) (SIA)
- Foreign Investment Promotion Board (FIPB)
- Foreign Investment Implementation Authority (FIIA)


Others

- Reserve Bank of India (RBI)
- Registrar of Companies (ROC)
- Securities & Exchange Board of India (SEBI)
- Central Board of Excise & Customs (CBEC)
- Central Board of Direct Taxes (CBDT)
- Authority for Advance Rulings (AAR)

Industrial Policy

- 
- Licensing has been removed and investors are free to set up industrial units with some exceptions, such as
 - ▶ Atomic Energy & Railways (reserved for the Public Sector)
 - ▶ Compulsory Licensing in
 - ◆ Alcohol, Cigars/Cigarettes, Electronic Aerospace/Defense equipment, Industrial Explosives, Hazardous Chemicals
 - ◆ Items reserved for Small Scale Industries (SSI) –326 assorted items. However, these items can be manufactured if 50% of output is exported.
 - Non-polluting units can be set up anywhere except in 23 identified urban areas with population of more than 1 million, where a license would be required. Polluting industries must be located 25 kilometers away from these areas, or in specified industrial areas. Electronics units, computer software and printing are exempt from these locational constraints.

Investing in India – Routes

- 
- Foreign investment in almost all sectors can be done in two ways:
 - ▶ Automatic without prior approval – except where the investor already has a venture in India. (This restriction doesn't apply for registered venture capital funds, where the investor holds less than 3% equity in the existing venture, or for a defunct/sick venture.)
 - ▶ By obtaining the approval of the FIPB, under the Ministry of Finance
 - Downstream investments by foreign-owned Indian firms are considered at par with the FIPB route.
 - Foreign investors can also acquire equity in an Indian firm, and can do so under the automatic route, provided SEBI guidelines are observed, and the share holding after transfer complies with sectoral limits under FDI policy.

Investing in India – Entity Options


Operating as a Foreign Company

- Liaison Office
 - ▶ Role limited to collecting information and not allowed to earn any income.
- Project Office
 - ▶ Temporary office based on very specific approval from RBI to execute specific projects. Only submission required is the details of the contract/project to the relevant Regional Office of the RBI.
- Branch Office
 - ▶ In general, allowed for non-manufacturing revenue-generating activities. However can be set up for manufacturing in a SEZ, subject to certain conditions.


Operating as an Indian Company

- Wholly-owned subsidiary
 - ▶ Treated as an Indian resident, and Indian company, and subject to all taxes and regulations.
- Joint Venture with Indian partner
 - ▶ Treated as an Indian resident, and Indian company, and subject to all taxes and regulations.

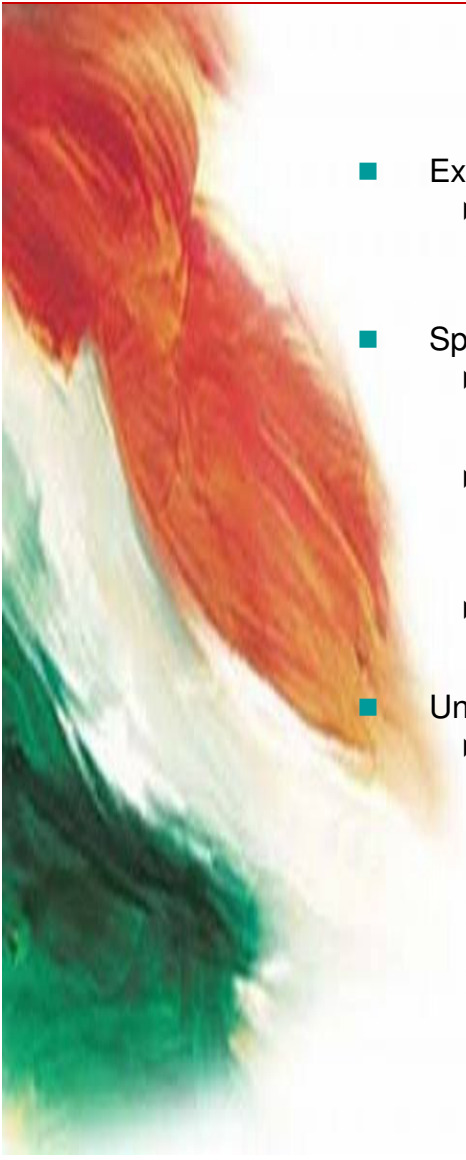
Funding Local Subsidiaries

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- Funding through Equity
 - ▶ In accordance with FDI guidelines.
 - ▶ Dividends paid in India are currently tax-free to the shareholder, while the company would pay a distribution tax.
 - ▶ Depending on the dividend level, there may be a statutory transfer to reserves of a portion of the distributable profits.
 - Funding through Preference Shares
 - ▶ This is treated as FDI (either automatic or FIPB route).
 - ▶ If convertible, these are included in the calculation of sectoral limits on foreign equity.
 - Funding through Foreign Currency Debt
 - ▶ External Commercial Borrowings (ECB) can be raised from foreign equity holders, conditions driven by the level of equity held.
 - ▶ Certain end-use conditions apply – so ECBs cannot be applied towards working capital, on-lending, investment in capital markets, and real estate investments. There are other conditions to be complied with w.r.t maturity and all-in-cost ceilings. If complying with all these conditions, no prior approvals are required.
 - ▶ Indian corporates can issue equity against ECBs, subject to meeting all tax liabilities and procedures.
 - Depository Receipts and Bonds
 - ▶ Global Depository Receipts (GDR), American Depository Receipts (ADR) and Foreign Currency Convertible Bonds (FCCB) are all treated as FDI, and can be issued under the Automatic Route (subject to sectoral caps on equity) upto US\$ 500 million.
 - ▶ Only publically-listed companies are allowed to raise capital through GDR/ADR/FCCB.

Exchange Controls

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- Exchange control is regulated under the Foreign Exchange Management Act (FEMA).
 - Fully convertible for current account transactions only. However, the RBI maintains a 'negative-list' of transactions which are prohibited, and prior approval is required for acquiring foreign currency above set limits for certain purposes.
 - Capital account transactions can be undertaken only to the limit permitted.
 - Foreign capital invested is usually repatriable after payment of due taxes. Other freely repatriations are - acquisition of immovable property in India, royalties or technical know-how fees, dividends and profits.

Tax Incentives

- 
- Export Oriented Units (EOU)-
 - ▶ These can be setup in a number of industries and are eligible for duty concessions on imports, subsidized consumables and tax holidays.
 - Special Economic Zones (SEZ)
 - ▶ These are duty-free enclaves. At the moment there are 22 operational, with plans for 200+.
 - ▶ SEZ units get 100% income tax holidays for 5 years, and 50% for the next 10, as well as exemption from other taxes.
 - ▶ SEZ developers are also provided with many concessions and incentives.
 - Units in Industrial Parks
 - ▶ Tax holidays and exemptions are available for units, and these vary from state to state.
 - EHTP and STP
 - ▶ Electronic Hardware Technology Parks (EHTP) and Software Technology Parks (STP) offer packages of incentives and facilities. Export oriented units such as call centers can also be registered as STPs.
 - ▶ These are eligible for deduction of 100% of export profits for 10 consecutive years.
 - Infrastructure/ Power/ Housing projects receive tax deduction of profits
 - ▶ Infrastructure development and maintenance – 100% tax deduction for 15-20 years, depending on the nature of the asset
 - Food Processing Units
 - ▶ A 100% tax holiday for 5 years, and 25%-30% deduction for the next 5 years.
 - Scientific Research & Development
 - ▶ A 100% tax holiday for 10 consecutive years
 - ▶ Deductions on expenditure, upto 150%, depending on meeting certain conditions.



About the Author

Atul Vaid has extensive experience in new strategic initiatives, industry assessment and market-entry consulting. With over 15 years of consulting and corporate experience, he has handled a large number of cross-border assignments involving marquee clients in India and the Middle East. At Trianz, Atul anchors the India-Entry Services of Trianz Consulting as a Director.

Reach Us

Reach Atul at contact@atulvaid.com

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