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Preface

This book was prepared by Ernst & Young, India with the intention of giving busy executives a quick overview of the investment climate, taxation, forms of business organizations, business and accounting practices in India. The complex decision-making process involved in undertaking foreign operations requires an intimate knowledge of a country's commercial climate, along with a realization that the climate is constantly evolving. Companies doing business in India, or planning to do so, are well-advised to obtain current and detailed information from experienced professionals. This book reflects information current at December 31, 2005.

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Glossary of frequently used terms

ADRs	American Depository Receipt
BCTT	Banking Cash Transaction Tax
BPO	Business Process Outsourcing
BTP	Biotechnology Park
CAGR	Compounded Annual Growth Rate
CBDT	Central Board of Direct Taxes
CCI	Competition Commission of India
DDT	Dividend Distribution Tax
EHTP	Electronic Hardware Technology Park
EOU	Export Oriented Units
EPZ	Export Processing Zone
FBT	Fringe Benefit Tax
FCCBs	Foreign Currency Convertible Bond
FDI	Foreign Direct Investment
FEMA	Foreign Exchange Management Act, 1999
FII	Foreign Institutional Investors
FIPB	Foreign Investment Promotion Board
FTP	Foreign Trade Policy
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GDRs	Global Depository Receipt
IRDA	Insurance Regulatory and Development Authority
IT	Information Technology
ITA	Information Technology Agreement
ITES	IT Enabled Services
MNCs	Multi National Corporations
MoF	Ministry of Finance
MoP	Ministry of Power
NBFCs	Non-Banking Financial Companies
NHPC	National Hydel Power Corporation
NPC	Nuclear Power Corporation
NRI	Non-resident Indians
NTPC	National Thermal Power Corporation
PIO	Person of Indian Origin
PSBs	Public Sector Banks
PSUs	Public Sector Units
RBI	Reserve Bank of India
Rs	Indian rupee
SDRs	Special Drawing Rights
SEBI	Securities and Exchange Board of India
SEZA	Special Economic Zones Act, 2005
SEZs	Special Economic Zones
STP	Software Technology Park
STT	Securities Transaction Tax
TRAI	The Telecom Regulatory Authority of India
WTO	World Trade Organization



Introduction

Basic Statistics

Geographical location: Between latitudes 8°4' and 37°6' North and longitudes 68°7' and 97°25' East

Land area: 3.29 million square kilometres

Climate: Mainly tropical with temperatures ranging from 10 °C-40 °C in most parts of the country

Capital: New Delhi

Population: 1.091 billion (estimated as at October 2004)

Population growth rate: 1.95 per cent per annum (between 1991 and 2001)

Population density: 324 persons / square kilometre

Life expectancy at birth: 63.9 years, male; 66.9 years, female

Literacy rate: 64.84 per cent (as per 2001 Census)

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

Major religions: Hinduism, Islam, Christianity, Sikhism, Buddhism and Jainism

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

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

The Land

Topography

Spread over 3 million square kilometres and located entirely in the northern hemisphere, India is the seventh largest country in the world in terms of geographical size. The Himalayas in the north, the Indian Ocean in the south, the Bay of Bengal in the east and the Arabian Sea in the west form natural boundaries for the country. India's neighbours are Bangladesh and Myanmar in the east; Bhutan, China and Nepal in the north; Pakistan in the west and Sri Lanka in the south.

India's topography is quite varied. While the extreme north is mountainous comprising mainly of the Himalyas, lower down is the fertile Indo-Gangetic plain that stretches across the country from the north to the east, and is fed by several perennial rivers. The arid Thar desert lies in the north-west region, while the north-east region, which receives some of the heaviest rainfall in the world, is covered with forest. The Deccan plateau largely forms the southern part of the country, and

is the source of several seasonal rivers that flow into the Bay of Bengal. The Eastern and Western Ghats are mountain ranges that separate the Coromandel (east) and Konkan (west) coastal regions from the Deccan plateau.

Climate

India has a tropical monsoon climate with the following seasons – winter, spring, summer and monsoon. The intensity of the weather varies depending on the region one is in. In general, the northern and central parts of the country experience extreme temperatures during summer (above 40 °C) and winter (below 5 °C), while the southern and the coastal regions enjoy relatively milder weather.

The south-west monsoon and the north-east monsoon are the two seasonal winds that affect the climate and rainfall in the country. The south west monsoon, also known as the summer monsoon, blows from sea to land during the period from June to September. This monsoon accounts for most of the rainfall in the country. The north east monsoon, also known as the winter monsoon, blows from land to sea in the months of October and November. This monsoon brings rainfall to the south-eastern part of the country.

The People

Population

As per the last census carried out in 2001, India had a population of approximately 1.029 billion. Based on historical growth rates, the population as at October 1, 2004 was an estimated 1.091 billion, and the country is expected to overtake China and become the most populous nation by 2045. The cities having a population of more than 5 million (as per the 2001 Census) are: Greater Mumbai (16.4 million), Kolkata (13.2 million), Delhi (12.8 million), Chennai (6.4 million), Bangalore (5.7 million) and Hyderabad (5.5 million). The country's population presents a kaleidoscope of rich and diverse culture.

The government is actively promoting family planning and the small family norm. According to its National Population Policy, the goal is to bring down the total fertility rate to replacement levels by 2010, and to achieve a stable population by 2045, at a level consistent with the requirements of sustainable economic growth, social development and environment protection.

Language

Given its cultural diversity, scores of languages and dialects are spoken in the country. Of these, twenty-two languages are recognized in the Indian Constitution, which include Bangla, Gujarati, Hindi, Kannada, Malayalam, Marathi, Oriya, Punjabi, Sanskrit, Tamil, Telugu and Urdu. Hindi, written in the Devanagari script, is the national language, while English is the business language. Although government organizations have initiatives to enhance the use of Hindi, both the government and the business community conduct their activities in English. English is also used for the purpose of communication between the central government and the governments of states which have not adopted Hindi as their official language.

Religion

As India is a secular country, it does not advocate any one religion, and all religions are accorded equal status before the law. The various religions practiced in the country and the approximate size of their following (as per the 2001 Census) are: Hinduism (827.6 million or 80.5 per cent of the population), Islam (138.2 million or 13.4 per cent of the population), Christianity (24.1 million or 2.3 per cent of the population), Sikhism (19.2 million or 1.9 per cent of the population), Buddhism (7.9 million or 0.8 per cent of the population) and Jainism (4.2 million or 0.4 per cent of the population). Judaism and Zoroastrianism are also practiced but are represented by relatively small-sized followings, mostly concentrated on the west coast.

Education and Literacy

India has a vast educational infrastructure, which can be broadly categorized into schools (primary, secondary and higher secondary education), colleges (higher secondary and undergraduate education in technical and non-technical fields), and postgraduate technical and professional educational institutes (covering a wide range of fields such as pure sciences, engineering sciences, medicine, information technology, business management, hospitality, law, fine arts, architecture, fashion technology, etc.). As per latest available information, there are over one million schools and around 9,200 colleges (graduate and postgraduate degrees) in general fields, 4,600 colleges (graduate and postgraduate degrees) in professional fields and 300 universities / institutions of national importance. The professional education institutes, with a combined intake of over half a million students per annum, constantly add to the country's large pool of skilled English-speaking work force, which is a tremendous competitive advantage vis-à-vis other nations.

India has a large number of private and government or municipal corporation-run schools, in the urban areas. However, in the rural areas, education is imparted largely by government-run schools. In addition, the diplomatic missions in New Delhi and Mumbai run schools that are affiliated to the education systems of the respective countries for the children of embassy officials and foreign expatriates. Renowned schools, colleges and professional education institutes are mostly located in the metropolitan and other large cities. There is stiff competition for admission into such institutes, as the quality of education imparted is high. Some institutions, such as the Indian Institutes of Technology and the Indian Institutes of Management are reputed worldwide.

The literacy rate in the country has been steadily rising, as people are increasingly realizing the importance of education. As per the 2001 Census, the overall literacy rate was 64.8 per cent, with a literacy rate of 75.3 per cent for males and 53.7 per cent for females. The corresponding figures as per the 1991 Census were 52.2 per cent, 64.1 per cent and 39.3 per cent, respectively. The nation is fully committed to providing Education for All by 2010, the priority areas being free and compulsory education of children till the age of 14 years, education of girl children to reduce gender inequality, education of children with special needs, and education of children belonging to the weaker sections of society and minorities. The

government is also focusing on bringing about consistent improvement in the quality of education through teacher education and training programmes. The National Literacy Mission aims at imparting functional literacy to illiterates with the goal of attaining a sustainable threshold literacy level of 75 per cent by 2007.

Indian Society

Indian society is multifaceted on account of its cultural and religious diversity. Social conduct is shaped by a variety of factors - religious and cultural mores, socio-economic status, location of residence (rural / urban), etc. Gender distinctions are pronounced, especially in the rural areas. The behavioural pattern of men and women can be quite different, and prescribed gender roles shape the actions of both sexes as they move in the family and the world outside their homes. With increasing global integration and exposure, Indian society is undergoing a pronounced change, impacted by the customs and life-styles of the Western society.

Cost of Living

India offers the advantage of a low cost of living, relative to American and European countries. The cost of living varies by type of location (urban / rural), size of location (small / large / metro), etc. The standard of living is comfortable in urban areas, with the availability of well-developed residential areas equipped with all utilities.

Recreation

India offers a wide repertoire of avenues for recreation and entertainment. Metropolitan and large cities have several five-star hotels, clubs, pubs and restaurants, discotheques, cinema theatres, art galleries, and theatres for music and dance and drama performances that cater to the recreational needs of tourists and residents alike. Hotels and clubs offer facilities for a wide range of sports including bowling, squash, tennis, snooker and swimming. In addition, most large cities also have golf courses.

For living-room entertainment, the print and electronic media offer many options. India has a highly developed print media that comes out with numerous books and magazines to suit diverse tastes. Television and radio offer a variety of entertainment fare. The advent of cable television has brought several international television channels, such as BBC, CNN, CNBC, Discovery, National Geographic, HBO, AXN and ESPN, into the Indian living room. With the privatization of radio, several large cities now have private FM music channels and the satellite radio organization Worldspace too is present in the country.

Indian cuisine is known and loved the world over for its rich and spicy taste. Most large cities have restaurants that offer cuisine from various parts of the country. Besides, there are also restaurants that specialize in French, Italian, Greek, Mexican, Thai, Japanese, Chinese and Lebanese cuisine. In addition several multinational fast-food chains such as McDonald's, Subway, Domino's Pizza and Pizza Hut are present in the country.

Shopping

India is a veritable paradise for shoppers. Everything from consumables to consumer durables can be bought off the shelf. Leading global players in nearly every consumer product segment are present in the market - Coca Cola, Pepsi, Kellogg's, P&G, Unilever, Colgate Palmolive, Gillette, Garnier, L'Oreal, Sony, Panasonic, LG, Samsung, Rolex, Mont Blanc, Armani, Louis Vuitton, Mercedes Benz, etc. Some of them such as Coca Cola, Pepsi, Unilever, P&G and Colgate have become household names.

Indian textiles, leather products, jewellery, handicrafts and artifacts, etc. are much sought after by foreign shoppers.

Travel

Most parts of the country are well connected by air, rail and road transport. For domestic air travel, there are a number of regular airlines - Indian Airlines, Jet Airways, Air Sahara and Kingfisher Airlines as well as budget airlines for cheap air travel - Air Deccan, Spice Jet and Paramount Airways. Besides, a few private operators also offer chartered flight services. International air connections are available from Ahmedabad, Amritsar, Bangalore, Chennai, Dabolim, Guwahati, Hyderabad, Kochi, Kolkata, Kozhikode, Mumbai, Nagpur, New Delhi, Srinagar and Thiruvananthapuram. Nearly every major international airline operates flights to and from the country. The country also has an extensive rail and road transport network. Railway services are offered by the government-owned Indian Railways. Bus services (regular, deluxe and luxury) over shorter distances are provided by government agencies and private operators. Numerous car rental agencies offer cars for hire and public taxis are available in some cities.

Tourism

Tourism is in a high-growth phase in the country. In 2004-05, foreign tourist arrivals numbered some 3.6 million and the country earned over US\$ 5 billion from foreign tourist spending. Foreign tourists comprise business and leisure travellers, and with growing foreign investment interest in India, the business travel segment is expected to witness rapid growth. Domestic tourists have also grown considerably in number, as the concept of a holiday per year has increasingly caught on, especially among the middle class.

India has numerous breathtaking tourist locales in its hill stations, beaches, wildlife sanctuaries, heritage resorts and places of religious significance. The single most famous tourist attraction is the Taj Mahal (at Agra near New Delhi), one of the seven wonders of the world. Some locations (in the northern states of Uttaranchal and Himachal Pradesh) also offer adventure sports such as white-water rafting, kayaking, etc. Besides the Indian Tourism Development Corporation which is run by the central government, each state has its own tourism development corporation. Indian addition to promoting tourism in the state and acting as information centres for tourists, these agencies also operate hotels at various tourist locales in the state.

The country has a good quality tourism infrastructure. Most of the tourist locales have lodging facilities ranging from luxury hotels to budget hotels to cheap, no-frills lodges. Well-known domestic hospitality brands, such as the Taj group, the Oberoi group and the ITC Welcomgroup, as well as international hospitality brands, including Accor, Days Inn, Choice Hotels International, Sheraton, Best Western, Hyatt, Marriott, Hilton, Holiday Inn and Le Meridian, operate in the country.

Time Zone

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

Business Hours

Normal business hours are from 9:00 am to 6:00 pm, Monday through Friday. Some commercial establishments also work on Saturdays. Banking hours are usually from 9:00 am to 3:00 pm although some banks have branches open till 8:00 pm. Shops are usually open till 9:00 pm six days a week. Sunday is the weekly holiday, although this can vary from place to place for various commercial establishments.

Public Holidays

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

Useful Addresses and Telephone Numbers

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

A. Government Structure and Economic Climate

A.1 Government Structure

Government

As enshrined in its Constitution, India is a sovereign, socialist, secular, democratic republic. It comprises 29 states and six union territories. It follows a federal form of government. Each state is administered by a state government, while the central government is in charge of the overall administration of the country. The union territories are administered by representatives nominated by the central government. To define the legislative powers of the central and state governments, three lists have been created - the central list, the state list and the concurrent list. The central and the state lists contain items where the central government and the state government respectively have legislative authority. The concurrent list contains items where the central government can legislate in consultation with the state governments.

India follows a parliamentary form of government. Even though the president is the Head of the Republic, the real powers are vested in the Prime Minister, who is the elected representative of the people. The government has three distinct branches - the legislature, the executive and the judiciary. While the executive is drawn from, and is responsible to the legislature, the judiciary is independent of the other two branches.

The Legislature

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

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

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

The Executive

The leader of the majority party in the Lok Sabha usually becomes the Prime Minister of the country. The prime minister and the Council of Ministers, collectively called the Union Cabinet, are vested with the responsibility of running the day-to-day affairs of the central government. The Union Cabinet is responsible

for its functioning to the Lok Sabha. The past few governments in the country have been coalition governments, with no single political party securing absolute majority in the Lok Sabha.

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

The Judiciary

India has an independent judicial system. The Supreme Court is the apex judicial authority, below it are the High Courts which head the judicial system in each state. Under each High Court there is a hierarchy of subordinate courts (district level and lower).

Political Parties

India has numerous political parties, including national, regional and local parties. The major national parties are the Congress (I), the Bhartiya Janata Party (BJP), the Communist Party of India (CPI), the Communist Party of India - Marxist (CPM) and the Janata Dal (JD). India has a tradition of having strong opposition parties, and the leader of the opposition party in the Parliament is accorded statutory recognition.

A.2 Financial System

India's financial system has kept pace with the growing needs of its corporate and retail borrowers. Interest rates are market-determined, and have shown a downward trend over the last few years.

Reserve Bank of India

The Reserve Bank of India is the central bank of the country. Established in 1935, RBI's role is four-fold:

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

RBI, through its policies, directives and guidelines, has been placing increasing emphasis on the monitoring of and provisioning for non-performing assets, capital adequacy and risk management. It is fully committed to the implementation of the Basle II norms in the Indian banking industry.

Types of Institutions

The banking system in India comprises scheduled commercial banks, urban and state cooperative banks and regional rural banks. Scheduled commercial banks, in turn, can be categorized into public sector banks, private sector banks and foreign banks. Besides banks, there is another segment of players in the Indian financial system, known as ('NBFI').

Public Sector Banks

This segment comprises 28 banks, including the State Bank of India and its seven subsidiary banks. It is the dominant segment in the banking industry. As at end-March 2005, it accounted for 79 per cent of the total deposits, 78 per cent of the total loans, 79 per cent of the total assets, and 88 per cent of the total number of branches of the scheduled commercial banks. The central government is the majority shareholder, holding more than 51 per cent equity stake in all the public sector banks, although its shareholding has decreased over the years on account of public offerings of shares and return of equity capital to the government by these banks.

Private Sector Banks

As at end-March 2005, this segment comprised 29 banks, including nine new private sector banks and 20 old private sector banks. The new private sector banks are growing rapidly in size, with an aggressive focus on the retail customer segment and substantial investments in state-of-the-art technology. As at end-March 2005, the private sector banks segment accounted for 17 per cent of the total deposits, 19 per cent of the total loans, 18 per cent of the total assets, and 11 per cent of the total number of branches of the scheduled commercial banks. The last couple of years have witnessed some mergers and acquisitions in this segment, and this trend is expected to gain in strength in the years to come. The RBI has however, placed restrictions on shareholding in private sector banks. As per extant regulations, no shareholder can hold more than 5 per cent shareholding in a private sector bank.

Foreign Banks

As at end-September 2005, this segment comprised 31 banks with 245 branches. Most of the leading international banks have a presence in India, though restricted to the metropolitan and large cities. In terms of size, this is the smallest segment in the banking industry, accounting for 5 per cent of the total deposits, 6 per cent of the total loans and 6 per cent of the total assets of the industry. A foreign bank can operate in the country either as a branch of the parent or as a wholly-owned subsidiary of the parent. Currently, there are several restrictions on foreign banks with respect to the expansion of branch network, location of new branches, acquisition of shareholding in Indian banks, etc. However, recently, RBI has come out with a road map for deregulation of foreign banks, such that from 2009 onwards, a foreign bank would be on par with an Indian bank, and can freely compete with other Indian banks, carry out mergers and acquisitions, etc.

Cooperative Banks and Regional Rural Banks

Cooperative banks cater to the credit needs of specific communities or groups of people in a region and operate in both urban and rural areas. They have been established under the respective State Co-operative Societies Acts, and are administered by the state authorities, although their banking activities come within the purview of the RBI. Regional rural banks were established under an act of the Parliament with a view to improving credit delivery in rural areas. They have been sponsored by the central government, state governments and various public sector banks in the ratio of 50:15:35 (of equity capital). In order to improve the operational viability of these banks and to enable them to take advantage of the economies of scale (through reduced transactions costs, etc.), the government has recently kicked off a process of consolidation among these banks. This process would also strengthen the weaker banks.

Non-Banking Financial Institutions

Unlike banks, whose core services comprise payment and liquidity-related services, non-banking financial institutions tend to offer enhanced equity and risk-based products. They play a crucial role in broadening access to financial services and enhancing competition and diversification of the financial sector. They are increasingly being recognized as complementary to the banking system, and capable of absorbing shocks and spreading risks at times of financial distress. The NBFIs segment comprises all-India financial institutions, state-level Financial Institutions, NBFCs and primary dealers. The first two are government-owned and focus on long-term development financing; NBFCs are mostly private sector entities that provide niche financial services and the primary dealers play an important role in the primary and secondary government securities market.

A.3 Type of Economy

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

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

General Economic Trends

Key Economic Indicators

GDP at factor cost (current prices): Rs 28,305 billion (2004-05)

Real GDP growth: 6.9 per cent (2004-05)

Inflation rate (measured by change in wholesale price index): 6.4 per cent (average during 2004-05)

Foreign exchange reserves (excluding gold and SDRs): US\$ 131 billion (December 30, 2005)

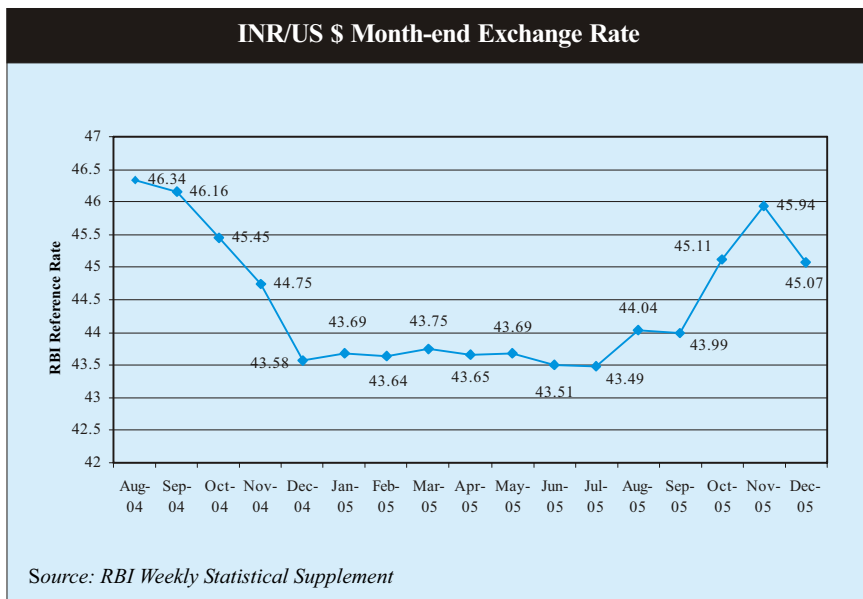
Bank rate: 6 per cent (end-December 2005)

After growing by a record 8.5 per cent in 2003-04, the economy kept up the growth tempo in 2004-05, with real GDP growing by 6.9 per cent year on year. With the agriculture sector growing by only 1.1 per cent year on year, the industry and services sectors were the principal drivers of economic growth during the year. While the services sector grew by 8.9 per cent year on year, the industry sector experienced accelerated growth at 7.7 per cent year on year, vis-à-vis 6.6 per cent during the previous year, on the back of a strong and sustained industrial recovery. This is also borne out by the accelerated growth in industrial production over the last few years. The Index of Industrial Production (IIP) grew by 8.4 per cent on an average during 2004-05, as against 7.0 per cent, 5.8 per cent and 2.6 per cent during 2003-04, 2002-03 and 2001-02 respectively.

The performance of the economy is expected to be even better in the current 2005-06. Real GDP growth in the first half of the year (April-September) was 8.1 per cent year on year compared to 7.1 per cent in the corresponding period last year. As per the latest estimates of the Centre for Monitoring Indian Indian Economy, real GDP growth for the full year is forecast to be 7.6 per cent year on year, with the Agriculture, Industry and Services sectors expected to grow by 3.0 per cent, 8.1 per cent and 9.2 per cent respectively.

Robust economic growth has been accompanied by continued macroeconomic stability with respect to other parameters such as foreign exchange reserves, exchange rates, inflation and interest rates. The country's foreign currency reserves, excluding gold and SDRs, swelled from US\$ 51 billion at end-March 2002 to US\$ 131 billion on December 30, 2005. The principal factors responsible for this reserve accretion are the country's burgeoning services exports and strong capital inflows comprising FDI and foreign portfolio investments by FIIs.

The Indian rupee has appreciated significantly against the US dollar over the past few years. The rupee-dollar exchange rate which stood at 48.80 at the end of the 2001-02 declined to 43.75 at the end of 2004-05. After remaining around 43.50 levels in the first half of the current financial year, the rupee has lost a little ground in the second half and is currently ruling at 45.07 to a US dollar (as on December 30, 2005).



Appendix 2 provides a table of the exchange rates of the Indian Rupee vis-à-vis selected major currencies as on December 30, 2005.

Inflation, measured on a weekly basis by the wholesale price index, ruled higher at 6.4 per cent on an average during 2004-05, as against 5.4 per cent in 2003-04, primarily on account of increase in fuel, power and lubricant prices resulting due to surge in international crude prices. In the first half of the current financial, inflation eased to an average of 4.6 per cent.

With the central government and the RBI maintaining a 'soft interest rate' stance, interest rates have shown a steady decline over the years. The maximum prime lending rate (PLR) dropped from 12 per cent in 2001-02 to 10.75 per cent in 2004-05. Thereafter, the PLR has remained unchanged in the first half of the current financial. However, with stiff competition prevailing for good quality assets, deals have been clinched at sub-PLR rates. Recently, with RBI hiking the repo rates to rein in inflation, banks are considering hiking the lending rates. In fact, there have already been a couple of hikes in the housing loan segment.

The Market

Consumer Market

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

In the urban areas, the so-called 'middle class population' has undergone some key socio-economic changes - increasing emphasis on higher and professional education, transition from joint families to nuclear families, increasing number of nuclear families with working women, rising disposable incomes, and exposure to western lifestyles and customs. These factors have generated a growing demand for a variety of quality products and services such as convenience foods, branded clothing, automobiles, toys, home appliances, electronic goods, restaurants, travel, communication and entertainment. The availability of cheap consumer finance has served to fuel this boom in consumerism.

In the rural areas, which are home to about 72 per cent of the country's population, the electronic media has played a great role in enabling consumer product companies create awareness about their branded products, ranging from personal and household products to durables like home appliances, bicycles and two-wheeler vehicles. This has caused a shift in consumption from unbranded and traditional products to branded alternatives. Besides, the composition of the consumption basket has also changed, with the share of food items decreasing in favour of non-food products. Another factor, which has been instrumental in increasing the penetration of branded products in the rural areas, is the extensive sales and distribution network of consumer product companies. An estimated one million market intermediaries, including wholesalers, stockists, transporters and retailers, are involved in the distribution of a variety of consumer goods to nearly 3,800 towns and cities and over half a million villages. While the urban areas have a range of retail outlets from small mom-and-pop stores to large supermarkets, the villages are catered to by small shops.

Industrial Market

The industrial market is an equally large and diverse market comprising a wide range of products for industrial consumption. While the majority of requirements are met domestically, some products are imported. A significant quantum of production in certain industries is also exported. Recognizing India's cost advantages and technical expertise in manufacturing, several MNCs have begun to use their manufacturing base here to outsource their regional or global product requirements. Industrial products can broadly be categorized as basic goods, intermediate goods and capital goods. During the last three years (2001-02 to 2004-05), industrial production (measured by IIP) grew at an average of 7.1 per cent per annum, stimulating rapid growth in the industrial market for capital goods like plant and machinery, instrumentation, and basic and intermediate goods like chemicals, plastics, components, etc. During this period, the capital goods production grew at an average of 12.7 per cent per annum, while the basic and intermediate goods production grew at an average of 5.3 per cent per annum and 5.5 per cent per annum respectively. During the first half of the current financial year (April-September, 2005), IIP grew at an average of 8.8 per cent. The production in the capital goods, basic goods and intermediate goods sectors grew at an average of 13.8 per cent, 6.3 per cent and 3.3 per cent respectively.

Currency

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

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

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

A.4 Leading Industries

India has built up a diverse industrial sector, which is currently one of the largest in the developing world. The major industries are automobiles and auto ancillaries, iron and steel, aluminum, textiles and garments, pharmaceuticals, chemicals and petrochemicals, oil and gas and other hydrocarbons, electricity, telecommunications, IT and BPO services, healthcare and biotechnology. The country is fast emerging as a leading sourcing base for global players in auto and auto ancillaries, pharmaceuticals, IT and BPO services, research and development services and engineering services.

Since the commencement of the economic reforms in 1991, successive governments have implemented strong measures to liberalize the business environment and boost industrial growth. The elimination of licensing requirements for all but six industries has ushered in an era of competition and imparted dynamism to the industry. Substantial reduction in import tariffs on raw materials and intermediate products, coupled with rationalization of excise duties, have eased access to inputs and reduced costs. Forward-looking export-import policies have enhanced the competitiveness of the country's exports, and created an environment conducive to rapid growth in exports. In order to enable industry to imbibe state-of-the-art technology and global best practices, the government has been welcoming FDI and foreign collaborations; FDI limits in almost all industries have been progressively liberalized and approval procedures simplified. An illustrative list of sectors in which FDI up to 100 per cent is allowed under automatic route is available at Appendix 3. Lastly, the central government and several state governments are in the process of investing significantly in sprucing up the country's infrastructure roads, seaports, airports, electricity and

telecommunications to enable the country realize its growth potential. An illustrative list of infrastructure and services sectors in which FDI up to 100 per cent is allowed under automatic route is available at Appendix 4 and Appendix 5 respectively.

Energy, Chemicals and Utilities

Oil and Natural Gas

Overview

India is the fifth largest consumer of primary energy in the world. Over the years, the country's primary energy consumption has grown at a rate that is one of the highest in the world and is expected to double in the next two decades.

The total production of crude oil and natural gas in the country during 2004-2005 was 33.98 million tonne and 31.77 billion cubic metre respectively, which represents a growth of 1.8 per cent and 0.5 per cent respectively over the previous year.

Crude oil import requirement is expected to reach 190 million tonne per annum by 2011-12. It is estimated that investments of US\$ 100-150 billion would be required over the next 10-15 years to cater to the projected demand.

The requirement of additional refining capacity is pegged at 40 million tonne per annum by the year 2010 to meet the domestic demand for petroleum products. Further, extensive oil and gas distribution infrastructure such as cross-country pipelines, port terminals, and strategic reserves also need to be developed. The first liquefied natural gas (LNG) receiving terminal at Dahej became operational in 2004 and the country got its second LNG terminal with the commissioning of the Hazira terminal of Shell-Total during April 2005. Plans to import gas through gas pipelines have also made witnessed progress in the recent times. The Iran-Pakistan-India pipeline particularly has witnessed significant development.

The industry, under the overall charge of the Ministry of Petroleum and Natural Gas, is poised for faster growth in the near future. This has been highlighted in the India Hydrocarbon Vision 2025 report prepared by an expert group set up by the government. As per the report, the demand for oil and gas is projected to grow around 368 million tonne and 200 billion cubic metre respectively by the year 2025.

In view of the rising energy demand, steps are required to increase investment in the upstream oil and gas sector and to formulate an appropriate strategy to firm up LNG supplies and gas imports through pipelines to bridge the demand supply gap for natural gas.

On the supply side, the scenario seems encouraging, with several significant oil and gas discoveries in the country by companies such as Reliance-Niko Resource, ONGC, GSPC and Cairn.

Regulatory Framework

Under the New Exploration Licensing Policy (NELP), the government has completely revamped its policy of awarding blocks for exploration and production, and has come out with attractive terms for private investors. The government has also delivered on its commitment to speed up the process of awarding blocks and signing contracts. In all, in the five rounds of bidding under NELP so far, 110 blocks have been awarded and contracts signed, in contrast to a mere 22 contracts during the 10 year period preceding implementation of NELP. The government is expected to launch the next round of bidding for the award of exploration blocks under NELP VI during January 2006. It is envisaged that in the medium term instead of rounds of bidding, there would be open availability of exploration acreages all round the year.

Salient Features of NELP

The investment package proposed under NELP is rated as comparable with the best in the world in terms of the following:

- International pricing of oil for new discoveries for private and state-owned companies.
- Royalty payments to be computed on ad valorem basis, along with concession on royalty due for exploration in deep waters.
- Freedom for marketing crude oil and gas in the domestic market.
- Duty concessions on import of capital goods available at par for private as well as national oil companies.
- Cess levied under the Oil Industry Development Act, 1974 to be abolished for the new exploration blocks.

Power

Overview

The Indian power sector is undergoing a major restructuring and reform exercise. Since 1991, when the government of India announced its new power policy, the thrust has been on encouraging private development of generation projects as compared to capacity additions in the state and central sectors prior to the new policy. In the area of distribution of electricity, the focus has been on corporatization and, implicitly, privatization. Even in the area of transmission, the current policies of the government envisage ownership of the transmission infrastructure by the private sector. The sector has witnessed consolidation of several existing legislations through the Electricity Act, 2003, which mandates unbundling of vertically integrated State Electricity Boards (SEBs), independent sector regulation, non-discriminatory open access to networks, and features several other progressive provisions.

The regulatory framework has also undergone a major change. Major changes in the legal and policy framework have established independent regulatory commissions at the central and state levels. Most states have established Electricity Regulatory Commissions and others are following suit. Thus, the central and state governments are progressively moving from the integrated role of policy-maker, owner, regulator and operator to being policy makers and partial owners.

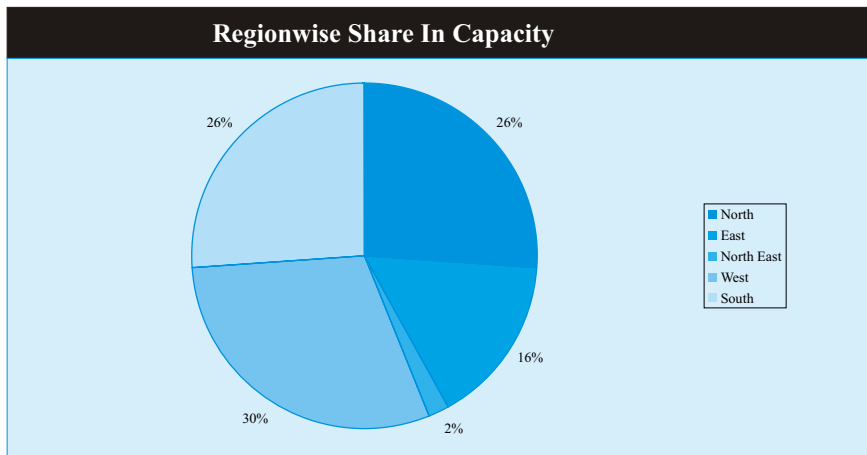
The impetus for these changes has come on account of the poor finances of the state governments and the inability to fund the burgeoning subsidy requirements on account of inadequate tariffs and commercial losses. Given the rapid growth of the economy and the need for electricity, state finances are also inadequate to meet the investment requirements. A more permissive and enabling framework is expected to attract higher levels of investments in the sector.

Industry Structure

While most of the industry is under public sector ownership, the private sector's participation is increasing in generation and distribution, and recently, in transmission too. The key private sector players in the power industry are Tata Power, Reliance Energy, RPG group, Essar group, and GMR group. The key players in power generation and their capacities are provided in the following below.

Name	Ownership	Capacity (megawatt)
NTPC	Government	21,435
DVC	Government	2,769
BBMB	Government	2,755
NPC	Government	2,720
NLC	Government	2,490
Tata Power	Private	2,300
NHPC	Government	2,275
NEEPCO	Government	1,130
RPG (CESC)	Private	1,065
Reliance Energy	Private	933
GMR Energy	Private	800
CLP Gujarat	Private	655
GIPCL	Government	562
Essar Power	Private	515

India's electricity market is divided into five regions and 29 states with each region and each state being served by a regional electricity board. The following chart depicts the share of each region in the total power capacity.



Source: Ministry of Power

As mentioned earlier, the power industry is regulated at both the central and state levels. The government at the central level is essentially responsible for setting India's energy policy, regulating interstate power activities and regulating the operations of government-owned utilities.

Governments at the state level establish state power policies, oversee operations of the SEBs and utilities and regulate interstate power activities.

Regulatory Framework

The principal legislations regulating the electricity sector in India till 2003 were the Indian Electricity Act, 1910; Electricity (Supply) Act, 1948; Electricity Regulatory Commissions Act, 1998; Electricity Laws (Amendment) Act, 1998 and the legislations enacted by the state governments, in particular the Reforms Acts. The newly enacted Electricity Act, 2003 has replaced the first three acts mentioned above. Based on the above, the following institutional framework has been chalked out.

Key Sector Players

Central Electricity Authority. The Central Electricity Authority is responsible for developing a sound, adequate and uniform policy and formulating short-term and prospective programmes for power development in relation to the control and utilization of the national power resources.

State Electricity Board. Constituted by the state governments, SEBs have the broad function of generating, transmitting and distributing electricity in coordination with generation companies, the government and any relevant agency. Several states have restructured and unbundled their SEBs into separate generation, transmission and distribution companies. Others are expected to undertake the same shortly.

Central and State Electricity Regulatory Commissions. The main functions of these commissions are to regulate the tariff of generating companies, regulate interstate/intrastate transmission, aid and advise the central government/state government in the formulation of tariff policy and frame guidelines related to the electricity tariff.

Power Grid Corporation of India. Power Grid Corporation of India is responsible for evacuating power from central generating stations, interstate transmission lines, formation of the national grid and operation of regional load dispatch centres.

Other government agencies include the NTPC, NHPC and the NPC that are responsible for thermal, hydel and nuclear power generation, respectively.

Salient features of the Electricity Act, 2003

As mentioned, the Electricity Act, 2003 has consolidated existing laws and brought about significant changes in the industry structure and the underlying commercial and regulatory arrangements. Some of the key changes include the following:

- Delicensing of generation.
- Mandatory open-access provisions for transmission and distribution networks for generators, including captives, subject to the availability of adequate transmission capacity and according to a schedule determined by the regulator.
- Power trading introduced in object clause of the law.
- Generators or traders provided with open access will need to pay a surcharge that is required to be reduced progressively. However, captive generation, including group captives or collective captives, will not attract a surcharge on open access.
- Competition has been encouraged even in network functions and parallel networks have been allowed explicitly.
- Appellate mechanism introduced through separate tribunal.
- National Electricity Policy and Tariff Policy envisaged to harmonize operations of the sector.

The new law intends to bring about an element of standardization in power sector operations in India through new features like the National Electricity Policy and Tariff Policy, National Load Dispatch Centre, the Appellate Tribunal and features related to open access and power trading.

With the introduction of this law, the government has put into motion its initiatives to liberalize generation, transmission and distribution. It also seeks to eliminate the key causes of the crisis of the SEBs relating to subsidies and poor metering. The government has already formulated a National Electricity Policy that aims to provide quality electricity to all citizens by 2011-12. The government is likely to finalize a tariff policy shortly.

The government has also instituted an Accelerated Power Development and Reforms Programme, which aims at upgradation of the sub-transmission and distribution system in the country and improving the commercial viability of SEBs. During 2003-04, funds amounting to about US\$ 0.62 billion were released to states as project assistance and incentives. A crisis resolution group has been set up in the MoP. The government has also attempted to upgrade regulatory infrastructure and improve federal and state coordination.

The National Electricity Policy was notified in February 2005. Following this the union government has also notified the Guidelines for Competitive Bidding and the Tariff Policy as required by the Electricity Act, 2003.

Power Industry: Key Statistics

- A total of 6,361 megawatt of capacity was added during 2004-05. This included 3949 megawatt of new conventional generation, 470 megawatt added through uprating or modernization of old capacity and 1942 megawatt from renewable sources (including hydro; less than 25 megawatt). Capacity addition has been continuing at a fast pace. The total installed generation capacity in the country as on October 31, 2005 stood at 123,463 megawatt. The region-wise and modewise installed capacity in various ownership categories is provided in the following table.

Ownership		Mode wise Breakup			Grand
Sector	Hydro	Thermal	Renewable	Nuclear	Total
State	25,053	41,898	3,496	-	70,447
Private	910	9,535	2,663	-	13,107
Central	6,172	30,426	-	3,310	39,908
Total	32,135	81,859	6,158	3,310	123,463

Generation installed capacity as on October 31, 2005 (in megawatt)

A capacity addition of 41,110 megawatt has been targeted during the Tenth Plan (2002-2007). While this is unlikely to be met, capacity addition of the order of 35,000 megawatt is currently expected during this period.

- Total electricity generation during 2004-05 was 587 billion kilowatt hour; an increase of 5.2 per cent over the previous year. The plant load factor of generating stations improved to 74.8 per cent vis-à-vis the previous year's figure of 72.7 per cent and the targeted figure of 72 per cent. On an overall basis, the power supply position was similar in 2003-04 and 2004-05. Energy shortage and peak shortage during the year was 7.3 per cent (previous year 7.1 per cent) and 11.7 per cent (previous year 11.2 per cent) respectively.

- At the end of 2004-05, nine states had enacted their State Electricity Reforms Acts. 13 SEBs had been unbundled / corporatized and others are expected to do so shortly; distribution had been privatized in two states and 24 states had constituted their state electricity regulatory commissions.
- There is renewed thrust on rural electrification. The present targets involve an ambitious plan to reach electricity to all villages in rural India by 2007 and thereafter make available electricity to all households on demand by 2011-12. The union government is providing a large quantum of funding support for rural electrification through the Rajiv Gandhi Grameen Vidyutikaran Yojana. The programme aims to strengthen the rural electricity distribution networks, reach electricity to unelectrified villages and improve governance in the rural electricity distribution.

Mining

Overview

With its abundance of natural resources, India produces four fuel, eleven metallic, fifty-two non-metallic and twenty-two minor minerals a total of 89 mineral products.

The total value of mineral production (excluding atomic minerals) was approximately Rs 739.45 billion (US\$ 16.43 billion) in 2004-05, of which the value of fuel minerals was around Rs 572.56 billion (US\$ 12.72 billion) or 77 per cent. The metallic production is accounted for by iron-ore, copper-ore, chromate, zinc concentrates, gold, manganese ore, bauxite and lead concentrates.

Amongst the non-metallic minerals, more than 90 per cent of the aggregate value is shared by limestone, magnesite, dolomite, barytes, kaolin, gypsum, apatite and phosphorite, steatite and fluorite.

India is the world's largest producer of mica blocks and mica splittings. With the recent spurt in world demand for chromite, India has stepped up its production to attain the third position amongst the chromite producers of the world.

Regulatory Framework

The Department of Mines, Ministry of Mines and Minerals, under the centre government, regulates and promotes the mining sector, other than coal, lignite, petroleum and natural gas and atomic minerals. The latter minerals come under the purview of independent government departments.

In the federal structure laid down by the Constitution of India, the 29 state governments are the owners of the minerals in their respective territorial jurisdictions. In offshore areas, exclusive economic zone and continental shelf, the rights are vested in the government at the centre.

Law and mineral rights empower the central and the state governments to receive payment of royalty from the lessee or mine owner for extraction and consumption

of minerals. The rates of royalty for various minerals, other than minor minerals, are specified by the central government through a notification. The royalty rates for minor minerals are specified by the concerned state government.

State-owned and privately-owned land, are both available for exploration and mining, except in certain areas, which the government may reserve through a notification. Since the surface rights of the land may vest in either the government or an individual, the access over the land is subject to the consent of the owner of the surface rights.

The following types of mineral concessions are granted as per the Mines and Minerals (Development and Regulation) Act.

- Reconnaissance permit
- Prospecting license
- Mining lease

Key features of Reconnaissance Permit, Prospecting License and Mining Lease are tabulated below:

Mineral concessions	Purpose/ Activities	Maximum area in a state *	Initial grant	Renewal
Reconnaissance permit	Prospecting of a mineral through regional, aerial, geographical or geo-chemical surveys and geological mapping	10,000 square kilometres (single permit 5,000 square kilometres)	3 years	Not Applicable
Prospecting license	Search and explore area for minerals and to remove limited quantities of substances for testing	25 square kilometres	3 years	2 years
Mining lease	Development and production of minerals discovered by prospecting or explorations operations	10 square kilometres	20-30 years	Blocks of 20 years

**The above ceilings on area for different concessions apply to the whole group (i.e. a company and its affiliate entities) and not to a singly entity.*

FDI is allowed in the mining sector and most proposals for FDI in the mining sector are eligible for investment without obtaining the government's permission, provided the prescribed ceilings are adhered to. The permissible ceilings on FDI in the mining sectors are provided in the following table:

Activities	Ceiling on foreign equity (per cent)
Exploration and mining of precious stones and diamonds	74
Exploration and mining of gold, silver and all other non fuel and non atomic minerals	100
Metallurgy and processing	100
Setting up operating power projects as well as coal and lignite mines for captive consumption and coal processing plants subject to certain prescribed conditions (Please refer note below)	50*
Exploration or mining of coal for captive consumption	50**

Note: Since, Coal is a nationalized mineral, no private/ foreign direct investment is permitted for mining activities of Coal in India, except for the activities mentioned in the table above.

**100 per cent FDI is allowed, however only 50 per cent is permitted under the automatic route.*

*** 74 per cent FDI is allowed, however only 50 per cent is permitted under the automatic route.*

Existing companies, who may not be in the mining sector but who have an expansion programme in the mining sector, and existing companies in the mining sector, are also eligible for automatic approval for induction of FDI if they propose to increase the equity base in line with the increase in the equity level, and bring in remittance in foreign currency for the purpose.

In a significant relaxation of the general policy, the automatic route for FDI and/ or technical collaboration is available to those who had any previous joint venture or technology transfer agreement. Further, as an additional relaxation from general policy, automatic route for FDI in the mining sector is also allowed to those who have an existing joint venture in India and who want to set up their 100 per cent owned subsidiaries in India. The investors in such cases will have to file a declaration with the RBI that they have no existing joint venture in the same area and/ or the mineral concerned.

Technology, Communications and Entertainment

Information Technology

Overview

The IT industry in India can be segregated into various segments comprising software services, ITES including the BPO sector and the hardware sector (consisting of manufacture and trading of computers and computer peripherals).

The IT industry in India has witnessed a five-fold growth since 2000 and has also recorded a CAGR of 28 per cent during 2000-05. This has occasioned an increased contribution of the IT industry to the national output, a growth from 1.2 per cent in 1997-98 to an estimated growth of 4.1 per cent in 2004-05.

According to National Association of Software and Service Companies (NASSCOM) findings, the overall Indian IT industry has grown by 32 per cent in 2004-05 registering revenues of US\$ 22 billion as against US\$ 16.7 billion during the preceding year. From an employment generation perspective, the total number of IT and ITES professionals employed in India has grown from 284,000 in 1999-2000 to over 1 million in 2004-05, growing by over 200,000 in the last year alone.

The list of multinationals operating from India includes IBM, Microsoft, Novell, Computer Associates, Oracle, AT&T, Fujitsu, Motorola, EDS, SAP, Computer Vision, Digital, Hewlett Packard, Texas Instruments, Intel, Analog Devices, Cadence Design, etc.

Key Highlights

- Of the Fortune 500 companies, about 220 such companies belonging to countries like the US, UK, Germany, France, Japan, Netherlands, South Korea, Switzerland, Canada and Sweden amongst others have established their presence in India.
- The total value of outsourcing to India (US\$ 17.2 billion in 2004-05) is estimated to be 44 per cent of the worldwide total.
- The growth in software service export has been sustained during the current financial year. In 2005-06, the Indian software and service exports industry is expected to register a strong growth of 30-32 per cent.
- Frost & Sullivan estimates the global market size for embedded software development alone to be worth US\$ 31 billion by 2004-05. The Indian market size for embedded software development is expected to reach US\$ 1.1 billion by 2005-06. It is pertinent to note that the embedded software development market represents 8-9 per cent of the overall Indian software export pie and is growing at a continuous pace.

Software services

The Indian software services industry comprises of a diverse group of companies ranging from start ups to billion-dollar global companies. The growth rate across these diverse groups of companies is varied.

This industry continues to be the dominating factor in the overall growth of the Indian economy. In 2004-05, Indian software services exports clocked revenues of US\$ 17.2 billion, registering a robust growth of 34.5 per cent over the previous year. The domestic market has also witnessed a growth in software and services revenue, up from US\$ 2.8 billion in 2002-03 to US\$ 4.3 billion in 2004-05.

The industry is vibrant with MNCs ramping up their offshore delivery capabilities in India. This has resulted in the clear shift in the delivery model to a global delivery model.

Looking into the future, the share of IT software and services in the national output is expected to reach 7 per cent of GDP in 2007-08, from the present level of approximately 4 per cent of GDP during 2004-05. Additionally, it is projected that India would build a US\$ 54 billion IT Software services export industry by 2007-08.

IT Enabled Services

India has become one of the most favoured destinations for sourcing ITES. The existence of a large, English-speaking, technically-qualified manpower, coupled with competitive billing, and high productivity gains has helped the nation emerge as a key ITES outsourcing hub.

Owing to rapid expansion of global outsourcing, the Indian BPO sector has emerged as a clear winner in the ITES industry. This BPO segment, in particular, has grown at a CAGR of 56.4 per cent during the five-year period ended 2004-05. Admirably, captive ramped-up capacities continue to dominate the BPO segment with 70 per cent share.

Within the BPO market, some of the significant growth areas that emerged during 2004-05 were engineering design, F&A outsourcing, voice customer support, research outsourcing, customer analysis, market analysis and equity research.

As per the McKinsey report, it is projected that by 2007-08, India will build a US\$ 21 - US\$ 24 billion BPO industry, given its strong value proposition. This growth will, however, depend on how the industry counters the anti-outsourcing threat and maintains its quality and cost advantages.

Hardware

India has the potential to become a large manufacturing facility owing to the abundance of technical skills. The country is now emerging as a design hub of the world.

The Indian IT hardware industry, a sector dominated by MNCs and the unorganized sector, is expected to generate revenues of US\$ 6 billion in 2004-05 thereby registering an approximate growth of 25 per cent over the previous year. However, the share of hardware revenues to the total revenues of the IT industry has declined from 28.6 per cent in 1999-2000 to a projected contribution of 21.3 per cent in 2004-05. This has primarily been due to declining prices and the inability of locally

manufactured products to compete with imports (on account of an inverted duty structure for related products). Nonetheless, hardware export continues to be a high potential segment with growth expected in the areas of components and design, embedded systems and wireless / telecom systems.

The Indian IT hardware market is projected to grow rapidly. This sector is expected to achieve a CAGR of 15.7 per cent and is expected to reach US\$ 62 billion by 2010-11. The prime drivers in achieving such augmentation will be the Internet, education, e-governance, banking and the ITES/software industry growth.

India - What lies ahead?

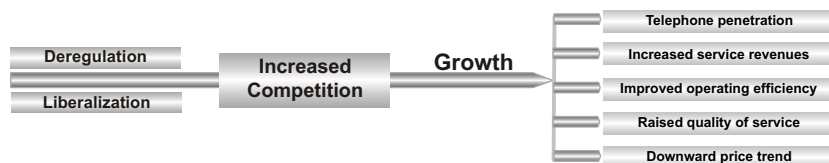
- The IT industry is poised to provide direct employment to more than 2.2 million people (and nearly twice the number by way of indirect employment) by 2008-09.
- Increased focus on research and development services which currently account for more than 15 per cent of the total IT exports.
- NASSCOM expects the export revenues of the Indian IT software and services industry to touch US\$ 15 billion in 2005-06, registering a growth of 25 per cent over 2004-05. The export revenues of the ITES sector, on the other hand are expected to grow by approximately 40 per cent to reach US\$ 7.3 billion in 2005-06.
- Domestic IT spending in India is also at an inflexion point, thereby opening a window of opportunities for growth in the next 2-3 years.
- While India continues to lead in segments it already operates in, vendors are now also gaining ground in newer services such as packaged software implementation, systems integration, network infrastructure and IT consulting.
- The Indian government is working on providing a beneficial fiscal framework for exporters, through the creation of SEZs. This development has captured the interest of several electronics manufacturing companies keen to establish facilities in India.

Telecommunications

Overview

The Indian telecom industry has been witnessing explosive growth rates since 1997. India is next only to China in telecommunications growth in the Asia-Pacific region. The beginning of internet and mobile telephony coupled with the coming into existence of the TRAI provided the foundation for this growth. Through its New Telecom Policy enacted in 1999, the government reduced license fees for operators and introduced more competition, which along with a reduction in import tariffs on equipment, slashed consumer prices and expanded the wireless telephony market. The government then introduced the Unified License Scheme whereby service providers can offer both wireline and wireless telephony and other telecom services with a single license. With the FDI limit now hiked to 74 per cent, investments of over US\$ 900 million are expected in this sector.

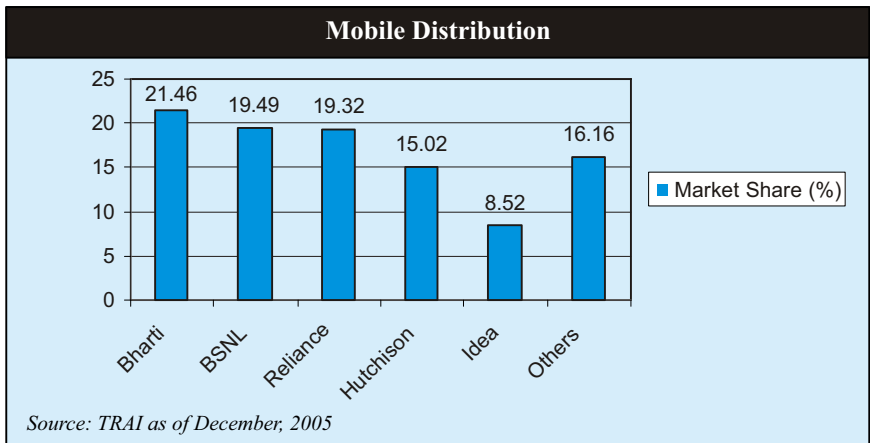
The last couple of years can be characterized as years of consolidation, growth and achievement for the Indian telecom sector. These years saw an infrastructure built-up with all major operators investing in building next-generation converged telecom networks capable of delivering high-tech services.



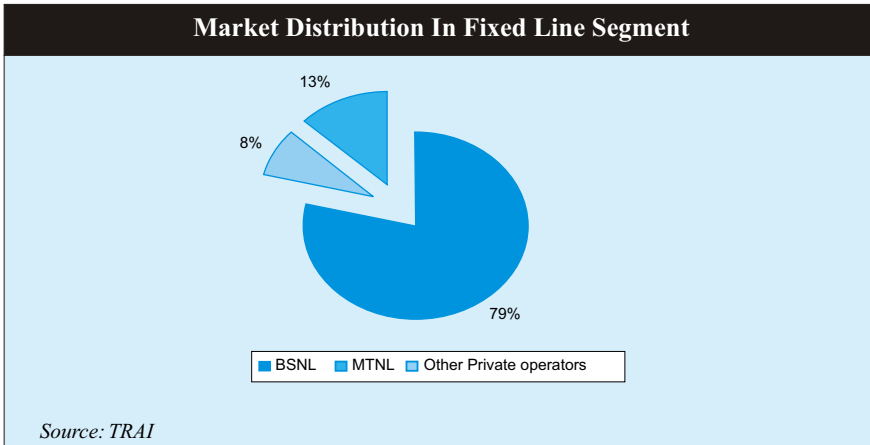
Recently, there has been spate of acquisitions with bigger players snapping up smaller players in an attempt to become larger and stronger. The buyouts accelerated after the government introduced unlimited competition in mobile segment by bringing the unified access licensing regime. This has resulted in increased competition in all segments, which in turn has resulted in lower prices and greater choice for consumers.

The total number of telephone connections in India has touched 124.85 million as at December 2005. Mobile leads the subscriber numbers with 75.92 million subscribers as against the fixed lines subscriber base of 48.93 million. In the mobile segment, Bharti Televentures is the market leader with a subscriber base of 16.30 million (Market share: 21.46 per cent) followed by BSNL with a subscriber base of 14.80 million (Market Share: 19.49 per cent) as at December, 2005.

The total telecom subscriber base is expected to cross 212 million by the end of 2008-09, at a CAGR of 22.7 per cent. The teledensity has also gone up from 2 per cent in 1999 to over 11 per cent currently, and is set to cross 20 per cent in the next five years. With the government stressing on increasing the rural teledensity, the revenue from telecoms is expected to almost triple to US\$ 23-25 billion by 2009 from US\$ 9 billion in 2002.



The fixed line telephony showed a stagnant growth rate of 7.68 per cent. The segment, however, continues to be dominated by BSNL and MTNL, the state-owned enterprises.



The astonishing pace of growth in the country's mobile subscriber base has stirred up a great deal of interest among global handset manufacturers with foreign majors like Nokia announcing plans to manufacture mobile handsets in India.

All this coupled with a strong growth in the GDP augurs well for the Indian telecom sector. It is expected that India will have total telecom subscribers of approximately 250 million by 2007-08, to result in a teledensity of approximately 20, which would more than double of the current level.

Regulatory Framework

- Up to 74 per cent FDI is permitted for telecom service companies (such as Basic, Cellular, Unified Access Services, National/International Long Distance, V-SAT and Global Mobile Communication Services) subject to inter alia following key conditions:
 - The 74 per cent FDI would include inter alia, proportionate investment in Indian promoters and investment companies, including holding companies.
 - Key management positions such chief executive officer, chief financial officer, chief technology officer etc. would necessarily have to be held by Indian residents.
 - No remote access (of the equipment of Indian telecom companies) to be allowed to any manufacturer or agency outside India except in the circumstances of catastrophic software failure.

FDI in internet service providers (ISPs) with gateways is limited to 74 per cent. However, FDI up to 100 per cent is permitted for ISPs without gateways.

Unlimited competition is permitted in most telecom services with the exception of cellular services wherein four cellular operators are permitted in each telecom circle in India.

Recently, to promote competition in National/International Distance Services, the government has liberalized certain licensing conditions. Pursuant to the changes, annual revenue share of National/International Long Distance Service Providers has been reduced from 15 per cent to 6 per cent of the gross revenues. Further, roll obligations and one-time entry fees for National/International Long Distance Service Providers have also been relaxed.

- FDI of 100 per cent is permitted for telecom equipment/handset manufacturing activities.

The institutional framework in Indian telecommunications sector includes various government departments and agencies.

Department of Telecommunications (DoT). DoT, under the Ministry of Communications, is the administrative department for monitoring the telecommunications sector. Its functions include policy formulation and overall administrative control.

Telecom Regulatory Authority of India. TRAI has been empowered to provide recommendations on various aspects related to the functioning of the telecom service providers and to discharge certain regulatory functions. The

recommendations of TRAI are required to be sought by the government on the need and timing of the introduction of new service providers and the terms and conditions of the license. The consultation with TRAI has been made mandatory and time bound. TRAI has been working on the complex problem of obtaining a sound framework for competition between multiple technologies and vendors.

Telecom Dispute Settlement and Appellate Tribunal (TDSAT). TDSAT has been empowered to adjudicate on disputes between the licensor and the licensee; between two or more service providers and between a service provider and a group of customers. It shall also act as the appellate authority in respect of any directions, decisions and orders of TRAI. It envisages a time-bound decision on appeals. Any appeal thereafter shall lie directly with the Supreme Court of India.

Entertainment

Overview

The Indian entertainment industry has out-performed the Indian economy and is one of the fastest growing sectors in India. The current size of the industry as a whole is estimated at Rs 200 billion (US\$ 4.5 billion) (2004) and is expected to grow to Rs 450 billion (US\$ 10 billion) by 2009. Currently, there are about 35 companies in the industry that are listed on the Indian stock exchanges.

The Indian entertainment industry can broadly be categorized into films, television, television software, music, radio and live entertainment and event management.

Films. The immense popularity of films as a source of entertainment and the vast cultural diversity of the Indian population has been instrumental in making India the largest producer of films in the world. The Indian film industry has produced more than 67,000 films in more than 30 different languages and dialects ever since the introduction of the 'talkies' in 1931.

This segment is poised to grow at an impressive rate in the future, primarily due to the expansion in the exhibition infrastructure and the development of multiplexes, availability of finance from institutional sources, exports of film and animation software, etc. In 2004, the total revenue of the Indian film industry was estimated at Rs 56.5 billion (US\$ 1.25 billion). It is expected to cross Rs 129.26 billion (US\$ 2.87 billion) by 2009.

The growth in revenue has improved due to an increase in the average investment and revenue realization per film rather than an increase in the number of films produced. The popularity of Indian films in the overseas markets has soared. Also, several countries such as Canada and France have signed co-production agreements with India. Digital technology is finding increasing use in film-making and the multiplex revolution is gaining strength. Film completion guarantee is another concept that has been introduced recently. The concepts of insurance and institutional financing of films have taken off. Till a few years back, the film-making business was largely in the hands of partnership and proprietary firms, but corporatization is slowly and steadily taking place now.

Television. There has been rapid growth in television penetration and the number of television channels with the entry of private television channels in the early 1990s. Currently, television reaches 59.5 per cent of the total population.

There are over 119 million television households in the country, with most households receiving over 100 Indian and foreign television channels.

With increased competition and the vagaries of ad spend in the economy, private broadcasters are looking at developing subscription revenues as a prominent revenue stream to combat the increasing pressure on the ad revenues.

From a near zero base in the early 1990s, the number of cable television households have grown at a scorching pace to the current estimate of 50 million. Today, India is the third largest country after the USA and China in terms of the number of cable viewers.

The distribution segment of the cable television industry is largely controlled by a few multi-system operators who account for almost 40 per cent of the total market by delivering through the local cable operators, who provide the last mile access.

As regards direct-to-home television, the year 2004 saw the launch of Doordarshan's DD Direct Plus and Zee Television's Dish TV. Apart from these, other key players like the Star-Tata venture, Sun TV etc. are expected to enter this segment shortly.

Television Software. Television software has been witnessing growth since 1985 when the national channel Doordarshan decided to go for commissioned and sponsored programmes. The subsequent meteoric rise in the number of private channels, especially regional channels, resulted in a burgeoning demand for television content.

Several television software companies were set up and programme genres such as news, current affairs, soap operas, religious programmes and game shows were established. Initially, the quality of content did not get due importance. However, today's competitive clamour among channels to retain audiences and the rising expectations of the viewers is making the channels demand quality programmes from the production houses. Production houses specialized in specific genres are investing in state-of-the-art technology and infrastructure to improve production quality and expand operations.

Music. The Indian music industry is characterized by a dominance of Hindi film music, capital intensiveness and generation preferences. The current industry size is estimated to be Rs 6.7 billion (US\$ 0.14 billion) in terms of revenue with a future growth potential of Rs 7.77 billion (US\$ 0.17 billion) by 2009. This industry is currently undergoing a phase of gradual reinvention with increased focus on the development of the non-Hindi film music segment, market and product expansion and organized music retailing.

Radio. The radio industry in India can be segmented into medium wave, short wave and frequency module based on the frequency of the stations. In its entirety, radio broadcasting reaches to 99 per cent of the Indian population and is also the most cost-effective mass medium.

Despite advancement in television broadcasting, radio continues to be an important and in some places, the sole source of entertainment. Recently, the radio segment has witnessed a jump in listenership with the launch of new FM radio stations in the metros pursuant to the privatization of FM radio. Radio currently accounts for approximately 2 per cent of the total ad spend and this share is expected to grow further. The revenue of radio services is expected to rise to Rs 6.46 billion (US\$ 0.14 billion) by 2009.

Live Entertainment and Event Management. Event management in India, which was born somewhere in the mid-1980s, has grown into a highly professional and tech-savvy industry over the years. Broadly, events can be classified as corporate events and live entertainment events.

Corporate events are commissioned by corporates for specific purposes such as a dealers' conference, or for visits of personnel from corporate headquarters. Corporate events account for the lion's share of the total number of events managed in the country.

Live entertainment events are film-based, music-based or sports-based functions such as stage shows or concerts by international or Indian artists.

According to industry sources, the current industry size is Rs 7 billion (US\$ 0.15 billion) and is expected to cross Rs 16 billion (US\$ 0.35 billion) by 2009.

Regulatory Framework

The entertainment industry in India is primarily under the charge of the Ministry of Information and Broadcasting, which is the apex body for the formulation and administration of the laws, rules and regulations relating to information, broadcasting, the press and films.

Recently, TRAI was appointed as the regulator for Broadcasting and Cable Services in India. During the year 2004, TRAI issued the 'Inter-connect' regulations, which inter alia provide for 'must carry' and 'must provide' regulations. Further, in the year 2005, TRAI issued the second phase policy for Privatization of Radio Broadcasting Services to attract private agencies to supplement and complement the efforts of All India Radio.

The Central Board of Film Certification screens films along the guidelines issued under the Cinematograph Act, 1952 before certifying a film for public exhibition.

Prasar Bharati (Broadcasting Corporation of India) Act, 1990 regulates the functioning of Doordarshan and All India Radio.

Various regulations affecting the industry such as cinema exhibition rules, entertainment tax regulations, etc. are state subjects and almost all states have enacted laws on the same.

Financial Services

India's financial services sector is in the process of rapid transformation. Reforms are continuing as part of the overall structural reforms aimed at improving the productivity and efficiency of the economy. The financial services industry can be broadly divided into banking, capital markets (asset management/mutual funds and portfolio investors), insurance companies and non-banking financial intermediaries/institutions.

Banking

Banking today has assumed a technology-intensive and customer-friendly face with focus on the ease and speed of operations. The sector is set to witness the emergence of financial supermarkets in the form of universal banks providing a suite of services from retail to corporate banking and industrial lending to investment banking.

The government, through the MoF, is responsible for the policies of the financial system, and also plays an important role in the domestic banking system through its ownership and control of the 28 PSBs.

Prior to the reforms in 1991, India's banking system was almost entirely owned by the government, except for about 22 private sector banks and foreign banks. The financial reforms of 1991 led to the banking system's movement from a totally administered sector into a more market-driven system.

The reforms included progressive tightening of prudential norms for asset quality and capital adequacy (benchmarking international norms), deregulating interest rates, liberalizing the entry norms for new intermediaries and developing new institutions.

The entry of the new private sector banks has brought about increased competition, though PSBs still continue to dominate the banking system. This also resulted in a significant improvement in the level of technology employed by banks and in their customer service standards.

The Banking Regulation Act, 1949 provides the legal and institutional framework for the banking industry in India. RBI is entrusted with the responsibility of regulating and supervising the banking system in India and is governed by the RBI Act, 1934.

RBI also regulates non-banking finance companies and key financial institutions, and jointly supervises the urban cooperative banks along with the respective state authorities. It acts as the banker to the government and manages the latter's internal

debt programme. RBI is also the 'last resort' lender to banks and financial institutions, and is responsible for the management of currency and payment systems, foreign exchange and the conduct of monetary and credit policies.

In February 2005, RBI announced a road map for the presence of foreign banks in India. During the first phase between March 2005 and March 2009, foreign banks are permitted to set up wholly-owned subsidiaries in India. During the second phase, from April 2009, RBI proposes to accord full national treatment to wholly-owned subsidiaries of foreign banks, dilution of stake in wholly-owned subsidiaries and mergers and acquisitions of any private sector bank in India. RBI also announced norms for the ownership of foreign banks in Indian private sector banks.

Capital Markets

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

Securities Regulatory Authority. The SEBI was established as a statutory body in 1992 to regulate and promote the development of the Indian securities market and to protect the interests of small retail investors. SEBI regulates the functioning of the Indian capital markets and issues detailed guidelines concerning capital markets, disclosures by public companies and investor protection.

SEBI also formulates regulations to govern various intermediaries such as brokers, portfolio managers, merchant bankers, etc. as well as regulates the mutual fund industry, portfolio investments by FIIs and venture capital investments.

Mutual Funds. With the entry of private sector funds in 1993, a new era started in the Indian asset management industry, giving the Indian retail/corporate investors a wider choice of fund families. Overall assets under management grew from Rs 1396.2 billion at end-March 2004 to Rs 1495.54 billion at end-March 2005. As at end-September 2005, they had further increased to Rs 2016.69 billion. The 2004-05 saw a record number of 97 schemes being launched in one year. Traditionally, the Unit Trust of India was the dominant player in the industry. However, over the years, private sector funds have grown steadily, and now they comprise the largest segment in the industry. There were a total number of 38 mutual funds as at end of September 2005. The sector is simultaneously witnessing consolidations and expansion.

Foreign Institutional Investors. India has, of late, generated a high level of interest among FIIs on account of its deep and liquid stock market and the relatively high returns generated by it. This has resulted in a marked increase in the number of FIIs operating in India and the total foreign portfolio investment. The number of FIIs registered with SEBI increased from 540 at end-March 2004 to 685 at end-March 2005, and 793 at end-September 2005. The total investment of FIIs in debt and equity increased dramatically from US\$ 25.75 billion at end-March 2004 to US\$ 35.93 billion at end-March 2005, and US\$ 40.35 billion at end-September 2005. While the portfolio investments of FIIs have traditionally been skewed in

favour of equity, recently the markets have also witnessed inflows into debt securities and derivatives. Significant inflows are further expected with FIIs being permitted to invest in Security Receipts issued by Asset Reconstruction Companies.

Insurance Companies

The insurance industry in India was traditionally a domain of the government-owned insurance behemoths such as the Life Insurance Corporation in the life insurance segment, and the General Insurance Corporation and its four subsidiaries and the Export Credit and Guarantee Corporation in the non-life insurance segment. In August 2000, the insurance sector was opened up to private participation and since then, 13 new life insurance and eight new general insurance companies have entered the market as joint ventures with major global insurance companies. The IRDA, which was established under an act of the Parliament, regulates the insurance and reinsurance business in India.

During 2004-05, life insurance companies underwrote a first year premium of Rs 253.4 billion, representing a 35.75 per cent growth over the previous year. Further, 26.2 million policies were underwritten during the year. In non-life insurance, the total gross premium income during 2004-05 was Rs 180.95 billion, a 13 per cent increase over the previous year. Life Insurance Corporation dominates the life insurance sector with a life insurance fund of over Rs 2,000 billion (US\$ 45.59 billion) and a market share of 78.07 per cent during 2004-05. The performance of the private sector players has been robust, and their market share in the premium has increased to 22 per cent in 2004-05 compared with 13 per cent in 2003-04. In non-life insurance, the share of private insurers has increased to 20 per cent in 2004-05 compared with 14 per cent in 2003-04.

Non-Banking Financial Institutions

NBFCs. NBFCs provide loans and hire-purchase finance, mostly for retail assets. NBFCs are required to be registered with RBI, which has extensive supervisory and regulatory powers over them. The total assets of NBFCs (excluding residuary NBFCs) amounted to Rs 377 billion (US\$ 8.7 billion) in March 2003.

Housing Finance Companies (HFCs). As the name suggests, the primary objective of these companies is to extend finance to the public for housing purposes. The sector was earlier dominated by Housing Development Financial Corporation (HDFC), which had a 66 per cent share in 1998. However, large banks have rapidly gained market share in the last two years reducing HDFC's share to an estimated 42 per cent in 2002. There are a total of 45 registered HFCs (of which 23 can accept public deposits) with the National Housing Bank. Total assets of all registered HFCs (having an asset base of more than Rs 100 million) amounted to Rs 430.53 billion (US\$ 10 billion) as at March 2003.

Credit Rating Agencies. Credit rating companies in India rate a wide range of debt securities including quasi-government and municipal securities; corporate debt, including bonds and commercial paper; and asset-backed and other structured finance securities. They also rate mutual funds on their performance and the state

governments on their power sector reforms. CRISIL is the country's leading rating agency, and others are ICRA, CARE, Fitch and Duff & Phelps. Moody's and Standard and Poor, the leading global rating agencies are strategic investors in ICRA and CRISIL respectively.

Venture capital funds. Though venture capital funds have been active in India, their visibility has increased over the last year or so with several large funds looking actively at investments in India. Venture Capital Funds (VCFs) and private equity investors invested an estimated US\$ 1.1 billion in India in 66 India-based companies in 2004. At end-March 2005, there were 50 VCFs and 14 Foreign Venture Capital Investors (FVCIs) registered in India. Their number has increased during the first six months of 2005, bringing the total number to 62 VCFs and 30 FVCIs registered in India. The SEBI regulates the registration and operations of VCFs in India through the SEBI (Venture Capital Funds) Regulations, 1996 which apply to domestic VCFs; and SEBI (Foreign Venture Capital Investor) Regulation, 2000 which apply to FVCIs.

Other Aspects of the Financial Services Industry

Key Stock Exchanges. India has 22 recognized stock exchanges, which operate under government-approved rules, bylaws and regulations. These exchanges constitute an organized market for securities issued by the central and state governments, public sector companies and public limited companies. India has modernized the operations of its stock exchanges through the introduction of screen-based trading.

The Stock Exchange, Mumbai (BSE) (earlier known as Bombay Stock Exchange) was hitherto India's premier stock exchange. However, the National Stock Exchange (NSE), which commenced operations in 1994, and which provides nationwide trading facilities to investors through an established nationwide information-technology network, now executes a higher proportion of the trades transacted on the stock exchanges. In addition, NSE is also the primary exchange for debt securities.

SEBI has initiated the process of demutualization (segregating the ownership, management and trading rights) of stock exchanges for ensuring better functioning of stock exchanges and introducing transparency in their operations. The process has been completed for BSE, which has now started working as a company.

Listing Requirements. Public limited companies are not statutorily required to list their shares on a recognized stock exchange. However, companies must be listed on a stock exchange if their shares and debentures are offered to the public for subscription. For initial public offerings, companies must abide by the stock exchanges' requirements to have their shares admitted, and if a company is not admitted to the exchange, it must refund the amounts received from subscribers. Consequently, companies should apply to one or more recognized stock exchanges for a listing before issuing a prospectus.

Investor Protection. In addition to the SEBI regulations on investor protection, the Companies Act, 1956 and the Securities Contracts (Regulation) Act, 1956 also contain provisions for protecting the interests of investors. Under the SEBI regulations, insider trading is punishable in certain specified circumstances. SEBI is streamlining the guidelines governing takeovers, public issues and disclosure norms to introduce increased transparency in the capital markets.

Aggrieved investors may seek redressal by writing to SEBI and informing the concerned stock exchanges. They may also file complaints with the district forum, state commission or national commission established under the Consumer Protection Act, 1996.

Retail

India is on the cusp of a retail revolution. The country's retail market, currently estimated at around US\$ 330 billion, is expected to grow to US\$ 550 billion by 2008. Most of this growth is expected to come from modern or organized retailing.

The retail industry is the second largest employer in the country after agriculture, and is possibly the biggest untapped market for the organized corporate sector. There are some 20 million players in the industry employing more than 40 million people. Most of these are mom-and-pop neighborhood stores run by individual proprietors. Organized or modern retailing is only a decade-old concept, and the top ten organized retailers account for a minuscule 2 per cent of the total market. However, all this is set to change. Modern retailing is poised to enter a boom phase and the top players are expected to capture up to 10 per cent of the total market in the next five years.

The retail revolution is being fuelled by the demographic changes sweeping the country. The country is becoming younger, with nearly a quarter of its one billion-plus population in the age group of 20-34 years. The purchasing power of the consumers is increasing, with per-capita GDP expected to grow at about 4 per cent per annum, and by 2010, 49 per cent of the households are expected to move into the middle-to-high income categories. Literacy rates are going up and there is an increasing emphasis on education, especially advanced education. Travel and exposure to electronic media are broadening the outlook of the young people. All these demographic trends are driving a change in the lifestyles and buying habits of consumers. Consumers are now looking for attributes such as a better shopping experience, presence of associated facilities, wide choice of products, better product quality and value, convenient payment mechanisms and better customer service.

Currently, the modern retailing segment comprises outlets of different formats department stores, supermarkets, discount stores and speciality stores. While supermarkets are the most popular format today, huge discount stores or hypermarkets are gaining in prominence and are expected to become the dominant format with time. The large-scale development of shopping malls in the urban areas

is expected to aid this trend. The leading players are investing in sprucing up store ambience and facilities, information technology, logistics and administration and customer relationship management in order to enhance the shopping experience, improve operating efficiencies and retain customers. There are a few challenges as well – relatively lesser attraction of retail jobs for potential employees, a less than robust infrastructure, high cost of real estate and lack of homogeneity in the Indian market.

The enticing retail growth story has made several big Indian business houses as well as global retail players draw up plans to enter the industry. The foreign companies that already have a presence in the country are: Metro, Marks and Spencer, Benetton, McDonald's, Domino's, Dairy Farm International, Mango and TGIF. Except for Benetton and Dairy Farm International, the others operate through the franchise model or operate only in the wholesale segment in view of the prevailing restrictions on FDI in retailing. Global retail giants, such as Wal-Mart, Tesco and Carrefour are eagerly eyeing the Indian market, waiting for the government to relax these restrictions. Once that happens, considerable foreign investment is expected flow in, accelerating the pace of growth in the industry.

Health Sciences

The health sciences industry comprises the following segments:

- Drugs and pharmaceuticals
- Biotechnology
- Healthcare
- Information management companies
- Pure research and development companies
- Contract research organizations
- Medical equipment suppliers

Drugs and Pharmaceuticals

According to a McKinsey and Co report, the Indian pharmaceutical industry accounted for 8 per cent of the global market in terms of volume and around 1 per cent in terms of value in the year 2004. Globally, it ranked fourth in terms of volume and thirteenth in terms of value. The Indian pharmaceutical sector is expected to attain a size of US\$ 11.6 billion by 2009 (*Source: Ibid, WPM Outlook, January 2005*).

The excellent export performance of the Indian pharmaceutical companies has substantially boosted their sales revenues. India's pharmaceutical exports were approximately US\$ 3.17 billion (*Source: Cygnus Business Consulting and Research Apr-Jun 2005*) and formulations constituted above 50 per cent of exports. The exports have grown at a CAGR of 26 per cent during the last five years while the Pharmaceutical industry has witnessed a growth of 7 per cent in 2004.

India being a signatory to the GATT is committed to honour global product patents 2005 onwards. India took a significant step towards becoming a global player in pharmaceuticals by making the patents (Amendment) ordinance 2004 a law on March 23, 2005. If the product patent regime is strictly followed, it is likely that multinational pharmaceutical companies might introduce their latest products into the Indian market.

Indian pharmaceutical companies are well-positioned to exploit the US\$ 80 billion global generics market created by several blockbuster drugs going off patent in the next five years. Indian players have already set up subsidiaries and sealed alliances in foreign regulated markets such as the Europe to enhance their distribution network. In addition, Indian companies have upped the ante in terms of acquisitions to gain complementary capabilities. One such deal was Matrix acquiring the Belgian firm Docpharma for a value of US\$ 263 million. Further, to acquire access to foreign markets and leading technologies, Wockhardt acquired Germany's Espharma GmbH in May 2004. Leading Indian companies are also investing increasing amounts of resources on new drug discovery and new drug delivery systems. The domestic pharmaceutical market is expected to grow at a CAGR of 9.7 per cent over the next five years owing to an increase in population, higher purchasing power, pruning of the number of drugs under price control, and the introduction of new drugs by MNCs.

The Indian pharmaceutical industry consists of both multinationals as well as domestic players. MNCs are primarily present in the formulations segment and have a negligible presence in the bulk drugs segment. In India, MNCs like Glaxo Smithkline, Pfizer, Novartis and Merck have created a strong brand identity for their products through high marketing expenditure coupled with global strengths/products.

As such, Indian players have a higher focus on bulk drugs with an active presence in formulations. Some of the key strengths of the Indian players include the following:

- High levels of integration and operating efficiencies.
- Reverse engineering and low-cost structures.
- World-scale manufacturing facilities.
- Shift from 'generic' drugs to high-growth segments.

Major Indian pharmaceutical companies include Cipla, Ranbaxy, Nicholas Piramal, Sun Pharma, Dr Reddy's, Wockhardt, Torrent Pharma and Lupin.

The Department of Chemicals and Petrochemicals, Ministry of Chemicals and Fertilizers is the nodal regulatory agency for the drugs and pharmaceutical industry. The government has also set up an independent regulatory body, the National Pharmaceutical Pricing Authority for fixing/revising the prices of drugs and pharmaceuticals. There are active associations of pharmaceutical manufacturers in

the country such as the Indian Drug Manufacturers Association, Indian Pharmaceuticals Alliance and the Organization of Pharmaceutical Producers of India.

The primary strengths of Indian companies are a large pool of highly qualified and experienced scientists and excellent manufacturing facilities as recognized by the Food and Drug Administration, US and other international counterparts. With an increasing number of bulk drugs going off patent and given the capability of Indian scientists in the process technology, the share of Indian pharmaceutical products in the world market is expected to rise further. Global pharmaceutical companies are increasingly regarding India as a manufacturing base.

India is also an attractive market for contract research organizations, on account of its cost-effective capabilities.

Biotechnology

The Indian biotech industry comprises the following sectors: bio-pharmaceuticals, agricultural biotech (including seeds), industrial biotech, bioinformatics and bio-services.

India has been practising conventional biotechnology for several decades. During the last five years, activity in modern biotechnology such as genetic engineering, immunological techniques, cell culture methods and hybridoma technology has intensified. Although many institutions have been set up across the world for genetic disorders and diagnostics, India has joined a select club by taking some major initiatives in genomic sequencing, pharmacogenomics, gene annotation and proteomics.

As per Ernst and Young's Global Biotechnology Report, 2005, the biotechnology market size is US\$ 54 billion, of which the USA accounts for US\$ 35.85 billion. The Indian market constitutes only 2 per cent of the global market. Further, the industry has attracted an investment of US\$ 140 million in 2003-04 and around US\$ 220 million in 2004-05.

The Indian biotechnology industry has registered a 36.55 per cent growth to cross US\$ 1 billion as against the US\$ 700 million in 2003-04. The bulk (75 per cent) of the biotech sector's revenue in 2004-05 came from the bio-pharmaceuticals segment. This segment consists of products such as vaccines, therapeutics, diagnostics and statins. Considering only the pure play biotechnology companies (excluding CROs, CMOs, medical device companies etc.), around 96 enterprises have been identified which constitute the Indian Biotechnology market. Considering a broader definition of biotechnology followed by the BioSpectrum-ABLE survey, which was conducted in 2005, the number of companies in the biotechnology sector have increased to 280 from about 150 in 2003-04. The biotech business in India has the potential to generate annual revenues of US\$ 5 billion and a million skilled jobs by 2010.

The skilled resource pool in the biotech sector consists of more than 15,000 scientists, 500,000 graduates from the 300 life sciences colleges, 12,000 doctorate scholars in chemistry and 115,000 postgraduates in sciences (*Source: Excerpt from a press release by Ranbaxy Labs*). The sector attracted an investment of US\$ 137 million during 2003-04. Investment has increased by 26 per cent and manpower has grown by nearly 42 per cent over 2002-03. In contrast, the clinical research field requires 20,000 research professionals and 4,000 investigators by 2010 if India is to secure a significant chunk of the global outsourcing pie. (*Source: Centerwatch*)

In 2004-05, the government through the Department of Biotechnology invested over US\$ 260 million towards research and development in national laboratories and centres of excellence. The investment was utilized for developing skilled manpower, creating a research and development infrastructure and providing extramural research and development support to public-funded institutions. The government has also increased the budgetary allocation for biotechnology to US\$ 1.2 billion as part of the Tenth Five Year Plan. Recently, a US\$ 40 million National Institute of Biologicals has been set up in New Delhi to carry out research, manufacturing and clinical studies. The Dynam Venture East Group and Andhra Pradesh Industrial Development Corporation (APIDC) recently established a joint venture (APIDC-VCL) to create India's first national VCF for biotechnology. In 2004, it provided about US\$ 17.7 million in funding to biotech firms.

Several states such as Maharashtra, Andhra Pradesh, Tamil Nadu, Karnataka, Delhi and Kerala have taken initiatives to encourage entrepreneurs to set up biotech industries. Some of the key initiatives include announcement of separate biotech policies, setting up of biotech parks and setting up of expert task forces for guidance on policy issues. India is taking steps to rationalize its policies in conformity with the provisions of the WTO.

The Department of Biotechnology is the nodal agency for policy, promotion of research and development, international cooperation and manufacturing activities. The other government agencies involved in biotechnology research and development are the Indian Council of Medical Research, the Indian Council of Agricultural Research, the Council of Scientific and Industrial Research and the Department of Science and Technology. The technology development board has also played a pivotal role in promoting many start-ups in the biotechnology sector such as Bharath Biotech, ABL Biotech, Shantha Biotech, Venkateshwara Bioproducts Limited, to name a few.

India is a signatory to the WTO and the country is taking steps to enact its provisions in letter and spirit. More regulatory dictums within the framework of international commitments of India to WTO and a Convention on Biological Diversity are in the offing. These include enactment of the Plant Varieties and Farmers' Rights Bill and creation of the Plant Quarantine Authority of India. The Plant Varieties and Farmers' Rights Bill will seek to protect currently unprotected plant varieties that are novel, distinct, uniform and stable for a period of 15 years from the date of registration; in respect of trees and vines, the period is 18 years. The Biological

Diversity Bill has been framed with the intention of protecting India's rich biodiversity and associated knowledge against their use by foreign individuals and organizations without sharing the benefits that arise out of such use. Indian Patent laws were significantly amended in 1999 as part of India's commitments to WTO.

India is expected to emerge as a large consumer of biotech products in the coming years. Over the next five years, biotechnology can offer opportunities for fresh investment of Rs 7 to 8 billion (US\$ 0.15 to 0.17 billion). This investment, if realized, can result in an additional turnover of Rs 9 to 10 billion (US\$ 0.19 to 0.21 billion) during the next five to seven years. This could contribute towards an increase in domestic production, import substitution, and the introduction of new products in the global market.

Consumption of Biotech Products in India			
	1999	2005*	(in Rs million) 2010*
Human and animal healthcare	32,240 (37.5)	35,320(37.6)	93,540 (40.0)
Agriculture	25,670 (29.8)	28,880 (30.7)	78,720 (33.7)
Industrial products	27,090 (31.5)	28,500 (30.3)	53,590 (22.9)
Other biotech Products	1,040 (0.02)	1,300 (1.4)	7,940 (3.4)
Total	86,040 (100)	94,000 (100)	233,790 (100)
In million US\$	1,789	2,186	4,270
<p><i>* projected figures</i> <i>Note: Figures in brackets indicate contributions in per cent of the total</i> <i>Source: CII</i></p>			

Sector	Revenues in USD Million (2004-05)	Market Share (%)
BioPharma	813.34	75.24
BioServices	96.81	8.96
Bio Agri	75.17	6.95
BoiIndustrial	72.89	6.74
BioInformatics	22.77	2.11
Total Industry Size	1080.98	100

Source: Biospectrum, June 2005
Biotechnology: Core Competence in India

- Capacity in bioprocess engineering;
- Skills in gene manipulation of microbes and animal cells;
- Capacity in downstream processing and isolation methods;
- Skills in extraction and isolation of plants and animals products;
- Competence in recombinant deoxyribose nucleic acid (DNA) technology of plants and animals;
- Excellence in traditional and molecular marker-assisted breeding of plants and animals; and
- Infrastructure in fabricating bioreactors and processing equipment.

Agricultural biotechnology promises to be an important business prospect. There are sizeable opportunities for foreign bioscience companies seeking research and business alliances with Indian companies. India offers a huge market for agri-biotech products as the country's economy is substantially dependent on agriculture.

Demand for biotech products in healthcare is also expected to grow significantly. Diagnostics are being increasingly consumed in more than 11,500 hospitals and 14,000 diagnostic laboratories in the country. The current market size is an estimated US\$ 200 million, of which around 50 per cent is accounted for by imports. In the 2004-05, the vaccines market grew at 28.88 per cent, and accounted for 35 per cent of the total biotech segment, with sales of US\$ 380.26 million.

Many Indian companies have introduced products of original research through technology transfer from research and development institutions of India in the field of vaccines, diagnostics and reagents. Some others have teamed up with foreign companies for sourcing technologies and are experimenting with new products produced by foreign technologies with a view to introduce them into the Indian market within the framework of Indian laws.

India is expected to gain leadership in bioinformatics owing to its large resource pool of molecular biologists, statisticians and software programmers. The global bioinformatics market is around US\$ 2 billion, which is expected to grow to US\$ 60 billion by 2005. According to experts, India is well-placed to garner a 5 per cent share of this global market. Currently, the market size of the Indian bioinformatics sector is US\$ 22.7 million and is growing at a rate of 25 per cent. 72 per cent of the total sales is generated by exports. This sector corners only 2.1 per cent of the Indian biotech industry. Bioinformatics contributed about 3.6 per cent of the total biotech exports from the country. (Source: *Biospectrum*, June 2005)

There is an increasing trend to outsource low-cost research and development functions by MNCs. This represents a tremendous opportunity for Indian companies to carry out contract research for overseas companies. The current global spend on outsourced research and development is an estimated US\$ 7 billion, which is expected to grow at 30 per cent per annum over the next five years. Typically, opportunities exist in gene sequencing work, Complementary Deoxyribonucleic Acid (cDNA) library preparation, genetic research, new crop varieties and early stage drug development.

A venture capital funding requirement of Rs 3,000 million (US\$ 65.20 million) has been estimated for this segment. Financial institutions such as the Small Industries Development Bank of India and ICICI Bank have committed about 35 per cent each.

Some of the active players in biotechnology in India include Cipla, Dr Reddy's Laboratories, Eli Lilly-Ranbaxy, Monsanto India Limited, SPIC, Zydus-Cadila, Scheering India Limited, Morepen Labs, Biocon, Torrent Biotech and Wockhardt Biotech. About 70 VCFs are operating in India which have about US\$ 5.6 billion in assets under management. Some agencies have dedicated biotechnology funds, while others have identified biotechnology as one of their priority areas of investment. Together they amount to almost US\$ 1.1 billion PPP by the end of 2003. These firms are located in four major clusters- Bangalore, Mumbai and Pune, Hyderabad and Chennai.

Healthcare

The healthcare industry includes medical care providers-physicians, specialist clinics, nursing homes, hospitals, medical diagnostic centres, and pathology laboratories. The global healthcare industry is estimated at US\$ 2.8 trillion while the size of India's healthcare industry is currently estimated at Rs 1500 billion (US\$ 34 billion) (Source: *Cygnus Business Consulting*, June 2005), which is roughly 5.5 per cent of the country's GDP. The private healthcare segment is by far the dominant segment with a size of Rs 860 billion (US\$ 15.73 billion). Public health spending accounts for only Rs 170 billion (US\$ 3.87 billion), which is a mere 0.9 per cent of the GDP. The tertiary care market is estimated at US\$ 3 billion and is currently 10 per cent of the total spends. Out-patient spending accounts for 61 per cent of the private healthcare segment and in-patient spending accounts for the remaining 39 per cent. The healthcare industry is growing at about 13 per cent

annually and is expected to grow at 15 per cent over the next four to five years. There are nearly 300 million strong middle class population is driving the demand for quality healthcare. Some of the leading listed players in this sector are Apollo Hospitals, Indraprastha Medicals, Bayer Medicals and Kovai Medicals.

Trends

The industry has grown in size and sophistication over the last decade with several corporate groups in the private sector setting up large multi-speciality and super-speciality hospitals in the large cities. While the basic health indicators in the country have improved substantially since independence, performance of the industry in terms of coverage, purchasing and delivery is poor vis-à-vis other developing nations like Brazil, Thailand and Korea. India has only 0.7 beds per 1000 people (*Source: Epsicom Business Intelligence World Pharma Fact Book - 2005*) in contrast to around 4.3 beds per 1000 in other countries. Corporate hospitals have created a large demand for the latest equipment. Infact many of these hospitals are partnering with their counterparts in the developed world to provide patient consultancy and medical education. Medical tourism is the latest buzzword of the Indian Healthcare industry. Telemedicine has enabled treating of patients residing in rural India. Another significant trend is the acquisition of technological solutions by the corporate hospitals to reduce operational costs.

The demand for healthcare is expected to see explosive growth with a rise in lifestyle diseases such as cardiovascular disorders and cancer. According to a recent study, the total healthcare spending is expected to reach Rs 2,000 billion (US\$ 43.47 billion) by 2012, and its contribution to the GDP would be around 8.5 per cent. Private healthcare would continue to dominate with a size of Rs 1,560 billion (US\$ 33.91 billion) and if health insurance gains wider acceptability, this could go up by an additional Rs 390 billion (US\$ 8.47 billion). Expenditure on public health could also double if the government increases its expenditure to the target level of 2 per cent of the GDP. In-patient spending is expected to increase its share in private healthcare expenditure to 47 per cent while the share of out-patient spending would decline. This industry growth would require a supporting investment of Rs 1,000 billion (US\$ 21.73 billion), 80 per cent of which would have to come from the private sector.

According to the National Health Policy, 2002, an increased fund allocation for the industry is envisaged in the next few years. Government spending is expected to go up to 2 per cent of the GDP by 2005 and 6 per cent of the GDP by 2010. Of the increased spending, 55 per cent would be devoted to primary healthcare, 35 per cent to secondary, and the remaining 10 per cent to tertiary medical and health facilities. The policy also includes a code of ethics for healthcare providers, and the setting up of a Medical Grants Commission to improve the standards of medical education in the country.

The Union Ministry of Health and Family Welfare is instrumental and responsible for the implementation of various programmes of national importance like family welfare, prevention and control of major diseases, etc. which form the main plank of

the development efforts. Apart from these, the Ministry also assists the states in preventing and controlling the spread of outbreaks and epidemics through technical assistance.

The Ministry comprises the following departments, each of which is headed by a Secretary to the government of India: (i) Department of Health, (ii) Department of Family and Welfare and (iii) Department of Indian Systems of Medicine and Homeopathy.

The Directorate General of Health Services (DGHS), a repository of technical knowledge, is an attached office of this Ministry. DGHS also renders technical advice on all medical and public health matters and in the implementation of various health schemes. Further, in order to implement policies and programmes of the Ministry in an effective manner, three subordinate offices are located at various places in the country which function directly under the Ministry. The Ministry is also administratively concerned with 29 autonomous / statutory bodies. There are also three public sector undertakings under the administrative control of the Ministry.

There is a huge opportunity for global healthcare companies, entrepreneurs and investors in the area of healthcare in India. As mentioned, the demand for healthcare is expected to be more than double in the next decade, and to meet this demand, an investment of Rs 1,000 billion (US\$ 21.73 billion) would be needed, mostly from the private sector, in the form of public-private partnerships or purely private ventures. A World Health Organization report states that India needs to add 80,000 hospital beds each year to meet the demand of its growing population.

As per IRDA, the Indian healthcare industry has the potential to show the same exponential growth that the software and pharmaceutical industries have shown in the past decade. Further, as per IRDA, only 10 per cent of the market potential has been tapped till date and market studies indicate a 35 per cent growth in the coming years.

Another facet of the healthcare industry is the 'preferred provider organization', which offers medical services to its clients. It manages almost all the healthcare needs of the customers except for the insurance cover. However, upon the deregulation of the insurance sector, it is estimated that there will be a spurt in activities to set up the preferred provider organization and health maintenance organizations.

Backed by its new state-of-the-art medical facilities, a pool of highly skilled and experienced doctors and lower costs, the country has also begun to offer specialist healthcare services to people from other developing countries and even some developed countries such as the USA. Thus, the industry is poised to grow fast and emerge as a key industry in the country.

Information Management Companies

Information management companies are information-driven organizations that provide non-technical support to organizations in the healthcare industry. Typically, their services include providing customer companies with information on the efficacy of the marketing initiatives undertaken, efficacy of the medical facility, administration, deliveries, etc. Currently, MNCs such as IMH and Battaerd Mansley have a presence in the information management segment in India. As the healthcare industry grows, one can expect tremendous demand for such niche services.

Pure Research and Development Companies

Capital investment in research and development by Indian health sciences companies lags way behind the world levels; the average research and development spend being about 2 per cent of the sales. Given India's commitment to honour global product patents from the year 2005, the need for novel drug discoveries is poised to increase at a phenomenal rate. Further, the incapability of the players in the pharmaceutical industry to fund research and development could make them turn to pure research and development companies. Pure research and development companies typically carry out long-term research and development focusing on preliminary research and development of new molecules and the out-licensing of such molecules.

Contract Research Organizations

Contract research organizations are typically engaged in conducting research outsourced by companies in the pharmaceutical sector, such as new drug testing (clinical trials), bioequivalence studies biometrics (data management) and site and project management.

These organizations offer tremendous promise in the health sciences sector and have seen phenomenal growth in India; the industry is growing at 100 per cent a year on year. Currently, revenues generated by the industry amount to Rs 3.5 billion (US\$ 0.08 billion).

Medical Equipment Suppliers

Medical equipment products include cardiology and X-ray machines, cardiovascular equipment, nuclear medicine devices, critical care IT, equipment radiation therapy machines, etc. Traditionally, MNCs sold medical equipments directly to high-end institutions. However, now the medical equipment suppliers segment includes traders and manufacturers with current trends indicating that indigenous players are growing in stature as traders and manufacturers. Industry experts expect the Rs 150 million (US\$ 3.42 million) medical equipment manufacturing segment to grow at 20 per cent per annum. Major players (MNC and Indian) include Philips, Boston Scientific Group, GE Medical, L&T, Wipro, Roche, etc.

As on November 30, 2005, in the Golden Quadrilateral component, nearly 5,100 kilometres of highways had been completed, while the remaining portion was under implementation. In the North-South East-West Corridor component, about 800 kilometres of highways had been completed, while another 2,500 kilometres was under implementation. Contracts for the remaining portion are yet to be awarded. In the Port Connectivity component, about 100 kilometres of highways connecting the major ports had been completed, while 250 kilometres was under implementation. Of the 800 kilometres of other national highways, nearly 300 kilometres had been completed and 250 kilometres was under implementation, while contracts for 250 kilometres were yet to be awarded.

In 2005, the government kicked off Phase III of the NHDP in which about 10,500 kilometres of national highways are proposed to be upgraded to four-lane dual carriageways. These stretches of national highways are subject to high volumes of traffic. They connect state capitals with the NHDP Phases I and II or provide connectivity to places of economic, commercial and tourist importance. This is planned to be implemented in two phases Phase IIIA and B. Phase IIIA comprises about 4,000 kilometres of highways, of which roughly 900 kilometres in under implementation and contracts for the remaining portion are yet to be awarded. Phase IIIB comprises about 6,500 kilometres of highways, all of which is yet to be awarded.

In addition to the above projects, the government is considering two more initiatives, called NHDP Phase IV and NHDP NE. Under NHDP Phase IV, with a view to providing balanced and equitable distribution of improved highways throughout the country, the government proposes to upgrade 23,000 kilometres of single lane highways to two-lane highways with paved shoulders and strengthen 18,000 kilometres of the existing two-lane highways with paved shoulders. Under NHDP NE, the government is considering accelerated development of roads in the north-eastern region, which will provide connectivity to all the state capitals and district headquarters, critical for economic development of the region.

Besides national highways, substantial action is taking place on the state highways front too. Several states are in the process of strengthening and upgrading their state highway network in order to improve connectivity within the state. These include Gujarat, Bihar, Karnataka, Tamil Nadu, Mizoram, Uttar Pradesh, Uttaranchal, Chhattisgarh, Madhya Pradesh and West Bengal.

The NHDP is being funded through various mechanisms budgetary allocation from the government (from the collection of a cess on the sale of petrol and diesel in the country), loan assistance from multilateral funding agencies such as the World Bank, the Asian Development Bank and the Japanese Bank for International Cooperation, and private sector participation.

Keeping in view the huge quantum of resources required and the need for managerial efficiency in the maintenance and administration of highways, the government has been actively encouraging private investment in highway projects.

FDI up to 100 per cent is permitted under the automatic route in road construction and maintenance. Besides laying down comprehensive policy guidelines for private sector participation, the government is also providing several incentives such as tax exemptions and duty-free import of road building equipment and machinery. Private participation is being sought through one of the following three structures:

- **Build Operate and Transfer (BOT) Toll-based.** In this structure, the private party constructs the stretch of highway and maintains it for a specified concession period, which can range up to 30 years. During this period, the party collects toll charges from the users of the road and earns returns on its investment. At the end of the concession period, the road is transferred to the NHAI. In the NHDP Phases I and II, a total of 30 projects worth about Rs 45 billion have been taken up under this model. Of these 21 projects had been completed and nine were under implementation. Besides, in NHDP Phase III, 15 projects have been awarded through the BOT route and another 97 projects are yet to be awarded.
- **BOT Annuity-based.** This structure is used for projects where the risk associated with the toll revenue is high on account of uncertainty in traffic, etc. The private party constructs a stretch of the highway and maintains it. In return, NHAI pays an annuity to the party during the term of the concession period. The project is awarded to the bidder who bids the lowest annuity amount. Eight projects, worth about Rs 24 billion, have been awarded on an annuity basis.
- **Special Purpose Vehicle (SPV):** In this structure, NHAI forms an SPV for implementing and managing the project. While NHAI provides some financial support in the form of equity / debt, the rest of the funds come from ports / financial institutions / beneficiary organizations. SPV is the concessionaire and collects toll from users during the concession period. NHAI has used this structure mainly for the port connectivity projects and a few others. In all, eleven projects worth about Rs 21 billion have been awarded through the SPV route.

The government has formulated Model Concession Agreements for all the above structures.

Ports

India is presently ranked 17th in the maritime nations of the world. About 95 per cent by volume and 70 per cent by value of the country's trade is carried on through maritime transport. The country is endowed with a long coastline of 7,517 kilometres (spread on the western and eastern shelves of the mainland and also along the islands) which contain 12 major ports and 187 minor and intermediate ports. The major ports are Chennai, Ennore, Haldia, Paradip, Kandla, Kochi, Kolkata, Marmagao, Mumbai, New Mangalore, Tuticorin and Visakhapatnam.

The major ports together handled about 75 per cent (383.6 million tonnes) of the total maritime cargo of the country in 2004-05 (518.3 million tonnes). The total

traffic and container traffic handled by these ports increased by 11.3 per cent and 7.2 per cent respectively to 383.6 million tonnes and 54.7 million tonnes respectively in 2004-05. Further, overall capacity utilization of these ports jumped from 88.5 per cent in 2003-04 to 96.5 per cent in 2004-05, as total capacity increased by a mere 2 per cent during the above period. The non-major ports also witnessed growth in traffic, from 118.9 million tonnes in 2003-04 to 134.6 million tonnes in 2004-05.

In 2005-06, during the period April-October 2005, cargo movement at almost all the major ports posted healthy growth. Traffic during the period was 234.7 million tonnes, representing 11.6 per cent growth over the corresponding period in 2004-05. Container traffic, accounting for 15.1 per cent of total cargo traffic, witnessed a 12.4 per cent growth over the corresponding period in the previous year.

Considering the long-term growth potential in maritime trade, the government has formulated a draft maritime policy for sprucing up the country's maritime infrastructure and creating an enabling framework to facilitate public and private investments, promote competition and enhance efficiencies. Integrated development of facilities at the major ports will be carried out in accordance with their individual master plans, which the ports are in the process of preparing. FDI up to 100 per cent under the automatic route is permitted in the construction and maintenance of ports and harbours, and in projects providing support services to water transport, such as the operation and maintenance of piers and loading and discharging of vehicles. The government has formulated guidelines for private/foreign investment in ports. Already, private/foreign players are operating container at several ports - P&O Ports at the Jawaharlal Nehru port and Chennai port, Port of Singapore Authority at the Tuticorin port, United Liner Agencies and Dubai Ports International at the Vishakhapatnam port and the Maersk-Concor consortium at the Jawaharlal Nehru port. However, the government is keen to foster competition and to ensure that no monopolies are created. Hence, there are some restrictions on incumbent private operators bidding for more projects at the same port.

The Department of Shipping, under the Ministry of Shipping, Road Transport and Highways, has the primary responsibility of the development and management of the country's maritime infrastructure. The administration of minor ports is the responsibility of the respective state governments though. Each major port is governed by a Port Trust, which is responsible for the administration, control and management of the port. With the entry of private sector players into port operations, the power to fix and revise tariffs has been entrusted to an independent authority called the Tariff Authority for Major Ports. The tariff fixed by the authority is only a ceiling; the port and the private operators are free to charge less than the notified tariff. The principal legislations governing the Indian ports are The Indian Ports Act, 1908 and The Major Ports Trusts Act, 1963.

Civil Aviation

India is one of the fastest growing civil aviation markets in the world. In 2004-05, the total number of passengers flown was 59.3 million, which represents an impressive 21.7 per cent growth over the previous year. While the domestic

passenger segment grew by 24.4 per cent to 39.9 million, the international passenger segment grew by 16.5 per cent to 19.4 million. Growth has continued to be robust in 2005-06, with the domestic passenger segment, the international passenger segment and the total passengers flown growing by 21.4 per cent, 14.5 per cent and 19.2 per cent respectively, to 26.5 million, 12 million and 38.5 million respectively during the period April-October 2005.

Freight traffic too has shown strong growth. In 2004-05, the total cargo transported was 1.28 million tonnes, which represents a 19.8 per cent growth over the previous year. While domestic cargo grew by 21.6 per cent to 457,000 tonnes, international cargo grew by 18.8 per cent to 824,000 tonnes. Growth has continued to be robust in 2005-06, with the domestic cargo segment, the international cargo segment and the total cargo transported growing by 6.3 per cent, 12.2 per cent and 10.1 per cent respectively, to 279,000 tonnes, 529,000 tonnes and 808,000 tonnes respectively during the period April-October 2005.

The country has 126 airports in all, comprising 14 international airports, 8 custom airports, 24 domestic airports, 26 civil enclaves at defence airfields and 54 other small airports. International airports, which are open to operations by foreign airlines, are present at Ahmedabad, Amritsar, Bangalore, Chennai, Dabolim, Guwahati, Hyderabad, Kochi, Kolkata, Mumbai, Nagpur, New Delhi, Srinagar and Thiruvananthapuram. International flights are operated by the national flag carriers from Coimbatore, Gaya, Jaipur, Kozhikode, Tiruchirapalli and Varanasi. Besides, tourist charters also touch Agra, Coimbatore, Jaipur, Lucknow and Patna airports. The international airports account for the major chunk of passenger and freight traffic. In 2004-05, they had an 87 per cent share of the total passenger traffic and 96 per cent share of the total freight traffic. In 2005-06, during the period April-October 2005, their shares of the passenger traffic and freight traffic were 88 per cent and 96 per cent respectively.

The international airport at Kochi is the only private sector airport in the country as of date. It is managed by Cochin International Airport Limited. The other airports are managed by the Airports Authority of India (AAI). Two more green-field airports in the private sector are being set up at Bangalore and Hyderabad, for which the concession agreements have been signed with the government. The government has also embarked on a massive programme for modernization of the existing airport infrastructure in the country. As part of this programme, it proposes to lease out the airports at New Delhi and Mumbai to two separate joint venture companies, in which private sector players would hold 74 per cent equity stake (FDI allowed up to 49 per cent). The joint venture companies would modernize the airports to world-class levels and operate them. Several consortia, each comprising Indian and foreign entities, including foreign airports, have submitted bids and the evaluation process is presently underway. Additionally, facilities at the airports at Chennai and Kolkata are also in the process of being upgraded by AAI. Further, AAI has also developed a plan for the city-side development of 25 other non-metro airports. In the first phase, 10 airports have been taken up and a global financial advisor and financial consultant have been appointed.

Air transport services in India were opened up to the private sector in 1994, and several private players entered the business. However, in the next few years, many of them became unviable and shut down operations. Till 2004-05, there were only five scheduled airline operators Air India, Indian Airlines and Alliance Air, which are state-owned carriers, and Jet Airways and Sahara Airlines, which are private operators. While Air India operated only on international routes, Indian Airlines operated on domestic routes and a few international routes, and the others operated only on domestic routes. Some hectic activity was seen in the air transport business in 2004-05, with the government implementing some pathbreaking measures. The government permitted private airlines with more than five years of operational experience to fly on international routes (except to the Middle East region). As a result, Jet Airways and Sahara Airlines also operate international flights now. The government also negotiated with the developed nations to substantially increase the seat capacity on international routes. As a result, numerous foreign airlines have started operating more flights to more destinations in India and vice versa. The government has also approved the plans of Air India and Indian Airlines to substantially modernize their fleet by purchasing new aircraft. The most significant development, however, was the entry of low cost carriers or no-frills airlines, as they are also called. Air Deccan, the pioneer of this concept in India, has successfully driven down the price points in air travel and attracted passengers from the middle-income group. Encouraged by the success of Air Deccan, several other private players have also entered this segment. While the market is expected to demonstrate continued strong growth, it remains to be seen whether all these players will be able to enjoy sustained growth. As per extant regulations, FDI up to 49 per cent equity stake and NRI investment up to 100 per cent equity stake is permitted in an airline venture. However, no foreign airline, whether directly or indirectly, is allowed to hold shares in the airline company.

Real Estate

Real estate sector is currently at the forefront of the Indian government's agenda given its potential to propel economic growth significantly. The sector has assumed growing importance with the government recently opening its doors for foreign investment in the sector. Across all segments of real estate, be it residential, office space, hospitality or retail, there has been a significant increase in development activity.

As per FDI policy guidelines, introduced vide Press Note 2 (2005 series), FDI up to 100 per cent is permitted under the automatic route in township, housing, built-up infrastructure and the construction-development sector, subject to the fulfilment of prescribed conditions. The key conditions are:

- In the case of development of serviced housing plots, a minimum land area of 10 hectares to be developed and in case of construction-development projects, a minimum built-up area of 50,000 square metres to be developed.
- Minimum capitalization requirement of US\$ 10 million in the case of wholly-owned subsidiaries and US\$ 5 million for joint ventures with Indian partners,

with the funds to be brought in within a period of six months from commencement of business.

- Original investment cannot be repatriated before a period of three years from the completion of minimum capitalization. However, the investor may be permitted to exit earlier with prior approval of the Foreign Investment Promotion Board.

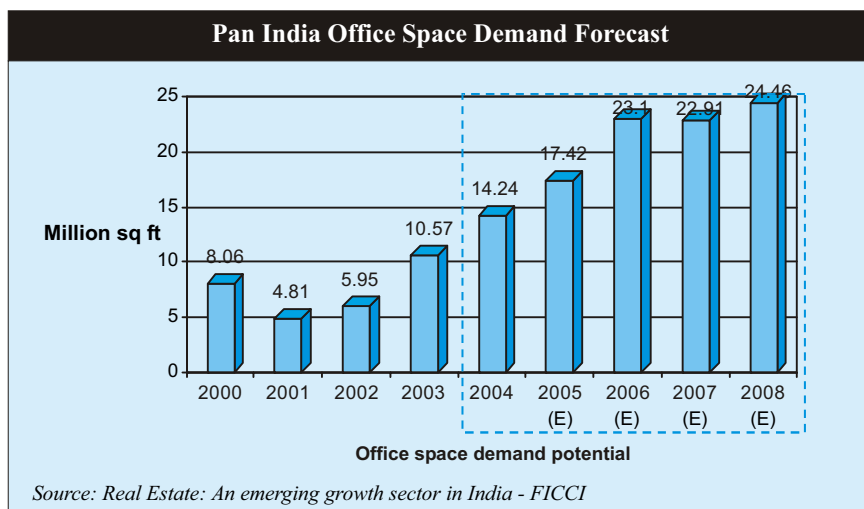
The real estate sector can broadly be categorized into residential, office space, hospitality and retail.

Residential. Residential sales account for more than 75 per cent of the total real estate market in value terms. Recently, there has been a spurt in activities in the residential space due to various factors that have led to an increase in the demand of residential property. Factors that have fuelled the growth in residential property are rapid urbanization, change in demographic composition, increase in disposable income, easy access to institutional funds, etc. In spite of the spurt in the residential development activities, the residential segment still has a long way to go. With demand outpacing supply, the current housing shortage is estimated to be 22.4 million units. Further, there is scope for over 400 township projects of a population of 0.5 million each over the next five years spread over 30-35 cities.

In view of the above, the government of India has also legislated tax incentives for the segment. A 100 per cent corporate tax exemption is provided for profits earned of qualifying projects. The projects, approved by March 31, 2007, should be developed on a minimum plot area of 1 acre with residential units having a maximum built-up area of 1000/ 1500 square feet depending upon the city of development, within four years from the financial year in which the housing project is approved by the local authorities.

Office space. The office space segment which includes commercial office space, industrial/ IT parks has seen significant action. With India becoming a preferred destination for ITES and BPO services, the service sector looking upward and the economy growing at a significant pace, there has been a sharp increase in the demand for office space.

The office space requirement in the eight major cities, considered to be commercial centres of India, has seen a phenomenal increase from 3.5 million square feet in 1998 to 16 million square feet in 2004. The cumulative demand for office space from 2005-2008 is expected to be 85 million square feet i.e. a CAGR of 14.5 per cent in the next three years.



Earlier, the trend of office space was that it was mainly dominated by the Central Business Districts (CBDs) of Mumbai and Delhi. Although the two cities still continue to dominate the segment, there has been a change in the trend for office space. Given the constraints of CBDs and the economic viability of the suburbs, there has been a shift in the focus from CBDs to the suburbs, and cities such as Bangalore, Gurgaon, Hyderabad, Chennai, Pune and Kolkata have also witnessed a steady rise in the demand for office space.

While demand for commercial office space in cities is on the upswing, industrial/IT parks and the SEZs have been the key drivers for this segment. It is believed that industrial/IT parks have a potential of absorbing 43 million square feet over 2005-2008. There is a 10 year 100 per cent tax holiday for undertakings deriving profit from developing, operating and maintaining industrial parks. The tax holiday is however available only to industrial/IT parks developed before March 31, 2006 and subject to it being notified by the central government.

Hospitality. Given the surge in the overall economy and with India emerging as a popular tourist destination there has been a sharp rise in both business and tourism related travel. The year 2004 saw record tourist arrivals of 3 million. Additionally, the first five months of 2005 saw a 20 per cent increase in foreign tourist arrivals in comparison to the same period last year. It is expected that by 2020, India will be a leading tourist destination in South Asia with more than 8 million tourist arrivals. In the short and medium term it is expected that the demand would exceed the supply leading to an increase in the average room rates.

Supply demand gap in premium hotels segment (average of 10 cities)					
	Room availability	Room demand	Increase in room supply	Occupancy rate (per cent)	Average room rate (Rs)
1999-2000	16,378	10,138	-	62	-
2000-2001	17,656	10,671	1,278	60	4,220
2001-2002	18,976	9,448	1,320	50	4,094
2002-2003	22,247	13,001	3,271	658	3,835
2003-2004	23,010	15,472	763	67	4,046
2004-2005	24,246	17,518	1,236	72	4,332
2005-2006 (P)	24,620	19,130	374	78	5,250
2006-2007 (P)	25,773	20,797	1,153	81	5,936
2007-2008 (P)	27,703	22,822	1,930	82	6,772

Note: The data pertains to the cities of P - Projections Source: CRIS INFAC Mumbai, Delhi, Chennai, Kolkata, Bangalore, Hyderabad, Pune, Goa, Jaipur and Agra

According to industry estimates the demand for hospitality-focused real estate during 2005-2009 is projected to be 30-35 million square feet with an estimated capital investment of US\$ 8-9 billion.

Another part of the hospitality segment which is currently in its infancy in India is serviced residences. Industry experts expect service apartments to grow rapidly in the near future. All these factors have fuelled the growth of the hospitality segment with existing hotels increasing their capacity and international hotels and service apartment chains establishing their operations in India.

While there are no corporate tax holiday benefits for profits derived from newly established hotels, hotels that started functioning during the period April 1, 1997 to March 31, 2001 can avail a corporate tax holiday of 50/ 30 per cent of their profits for a period of 10 years from their commencement, depending on their location. However, income by way of dividends, interest or long-term capital gains of an infrastructure capital fund/ company from an eligible hotel project are tax exempt in the hands of the investors subject to specific conditions.

Retail. The Indian retail industry is the second largest untapped market after China. In fact, India was ranked the second most attractive retail destination by AT Kearney in one of its recent reports. The total domestic retail market is currently estimated to be over US\$ 330 billion and is growing at a rate of 4-6 per cent in real terms. Although the size of the retail sector is substantial, the sector is dominated by small independent players with the organized sector accounting for just 2 per cent of the market (i.e. US\$ 4 billion). Organized retail has however, benefited from increased consumption expenditure as well as with a shift in preference for organized channels. It is estimated that the organized retailing segment will grow four-fold to US\$ 15 billion by 2010.

Keeping in mind that the organized retail industry is space intensive, the real estate requirements for the same are expected to rise. Currently, there is 12.8 million square feet of operational mall space in India. It is estimated that by 2007 there would be as many as 343 malls built in India with a mall area of over 87.7 million square feet. It is expected that the coming two years itself would see more than 46 million square feet of space for malls and multiplexes be added on. Of this, 32 million square feet of space is estimated to be absorbed by the Tier - I cities of Mumbai, NCR, Chennai, Kolkata and Bangalore. Further, as many as 45 malls with 9.5 million square feet of space are coming up in Tier - II cities like Jaipur, Chandigarh, Ludhiana, Nagpur, Surat, Kochi, Ahmedabad and Baroda. The growth of the retail sector in Tier -II cities is not restricted to malls. While most of the initial multiplex projects started in major metros, of late there has been a sharp rise in the multiplexes being established in non-metro urban centres. The primary cities witnessing a growth in multiplexes include Pune, Baroda, Indore, Ahmedabad and Jaipur.

There are no corporate tax holiday benefits for the retail space segment of real estate. However, multiplex theatres constructed during the period April 1, 2002 to March 31, 2005 (other than in Chennai, Delhi, Mumbai and Kolkata) can avail a 50 per cent tax holiday for a period five years.

B. Investment Climate and Foreign Trade

B.1 Foreign Investment Framework

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

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

Industrial Policy

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

The system of obtaining government approvals has been progressively liberalized over the 1990s, commencing with the watershed changes in the industrial policy announced on July 24, 1991, which substantially abolished industrial licensing, announced measures for facilitating foreign investment and technology transfers and opened up most areas which were earlier reserved for the public sector.

Industrial Licensing

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

- Industries reserved for the public sector
- Five industries of strategic, social or environmental concern
- Manufacture of items reserved for the small-scale-sector by non-small-scale industrial units or units in which foreign equity is more than 24 per cent.

All other industries are exempt from licensing, subject to certain locational restrictions in metropolitan areas. In the event, the locational restrictions are not adhered to, the unit is required to obtain an industrial license.

Industrial licensing is compulsory for investing in the following five industries of strategic, social or environmental importance:

- Distillation and brewing of alcoholic drinks
- Cigars and cigarettes of tobacco and manufactured tobacco substitutes
- Electronic aerospace and defence equipment

- Industrial explosives including detonating fuses, safety fuses, gunpowder, nitrocellulose and matches
- Hazardous chemicals

Foreign Investment Policy

India's economic policies are designed to attract significant capital inflows into India on a sustained basis and to encourage technology collaborations between the Indian and the foreign entities. Policy initiatives taken over the last few years have resulted in inflows of foreign investment in diverse sectors of the economy.

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

B.2 Economic Policies and Incentives for Foreign Investment

Features of the foreign investment policies and incentives

- No government approval required for FDI in virtually all the sectors/activities, except for a small negative list notified by the government.
- The government has notified 'Sector Specific Guidelines for FDI' wherein investments up to specified sectoral caps are covered under the automatic route, with a few exceptions.
- The FIPB considers proposals for foreign participation that do not qualify for automatic approval.
- Decisions on all foreign investment proposals are usually taken within 30 days of application.
- Free repatriation of capital investment and profits thereon is permitted, provided the original investment was made in convertible foreign exchange.
- Use of foreign brand names/trademarks for the sale of goods in India is permitted.
- Indian capital markets are open to FIIs.
- Indian companies are permitted to raise funds from international capital markets.
- Special investment and tax incentives are given for exports and sectors such as power, electronics, software and food processing.
- 'Single window' clearance facilities and 'investor escort services' have been provided in various states to simplify the approval process for new ventures.

Foreign Direct Investment

In pursuance of the government's commitment for early implementation of the second phase of economic reforms and with a view to give further impetus to the Indian industry the government of India permits FDI on an automatic basis, except with respect to a small negative list.

Negative List

All industries/activities would qualify for FDI on an automatic basis, except the following:

- Investment in companies where activities require an industrial license.
- Proposals involving a foreign collaborator who has an existing venture/tie-up in India in the same field (except in the IT and mining sector), and investments made by international financial institutions such as the Asian Development Bank, International Finance Corporation, Commonwealth Development Corporation and Deutsche Entwicklungs Gesellschaft.
- Proposals relating to the acquisition of existing shares in an Indian company by a foreign investor in the case of financial sector and the cases where SEBI takeover code is attracted.
- Proposals falling outside notified sectoral policy/caps.

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

Proposals for foreign investment, which are not covered under the automatic approval route, are considered for approval, by the government of India. Composite proposals, i.e. proposals seeking other industrial approvals such as industrial license, technical collaborations, etc. along with approval for foreign investment, are given a composite clearance by the government of India.

Foreign Investment Promotion Board

FIPB is a specially empowered board chaired by the Secretary, MoF, set up specifically for expediting the approval process for foreign investment proposals.

There are no prescribed application forms for applying to FIPB, except in the case of purely technical collaborations. Proposals for FDI may be sent to the FIPB Unit, Department of Economic Affairs, MoF or through any of India's diplomatic missions abroad. The government has started a mailbox facility for accepting FDI proposals through the internet and providing an acknowledgement number for the same, with the condition that a hard copy should be received in original before the proposal is considered by the government.

FIPB has the flexibility to examine all proposals in totality, free from predetermined parameters or procedures. Its approach is liberal for all sectors and all types of

proposals. While applications are subject to stages of negotiations, it is important for the investors to convince FIPB on the benefits to the Indian economy from the project. Some of the other parameters that the FIPB considers while evaluating proposals are the levels of investment proposed, the technology to be inducted, the export potential or the import substitution factors and the employment potential.

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

Foreign Investment Implementation Authority

The government has set up Foreign Investment Implementation Authority (FIIA) in the Ministry of Industry, pursuant to the announcement in the Union Budget Speech for 1999-2000. FIIA facilitates quick translation of FDI approvals and implementations and provides a proactive one-stop aftercare service to foreign investors by helping them obtain the necessary approvals, sort out operational problems and meet various government agencies to find solutions to problems and maximize opportunities through a partnership approach.

FIIA in accordance with its mandate assumes the following role:

- Understands and addresses concerns of investors.
- Understands and addresses concerns of approving authorities.
- Initiates multi-agency consultations.
- Refers matters not resolved at the FIIA level to higher levels on a quarterly basis, including cases of project slippages on account of implementation bottlenecks.

FIIA has the following functions:

- Expedites various approvals/permissions.
- Fosters partnership between investors and concerned government agencies.
- Resolves differences in perceptions.
- Enhances overall credibility.
- Reviews policy framework.
- Liaises with the Ministry of External Affairs for keeping India's diplomatic missions abroad informed about the translation of FDI approvals into actual investment and implementation.

The following are the modalities of the functioning of FIIA:

- FIIA has set up a Fast Track Committee (FTC) to review and monitor mega projects.
- FIIA has initiated inter-ministerial consultations to make appropriate

recommendations to the competent authority, i.e. ministry/department concerned at the central or the state government levels, as the case may be, on issues requiring policy intervention.

- FIIA acts as a single-point interface between the investor and government agencies including administrative ministries/state governments/pollution control board/ Director General of Foreign Trade /regulatory authorities/tax authorities/Company Law Board.
- FIIA meets regularly to review cases involving investments of Rs 1 billion or more, considers references received from FTC and monitors the functioning of the various FTCs. It also entertains complaints regarding implementation bottlenecks from FDI approval holders, regardless of the quantum of investment.
- FIIA makes recommendations from time to time on any issue relating to the speedy implementation of FDI projects and also provides transparency in government functioning with respect to FDI projects.

Foreign Technology Agreements

Foreign technology collaborations that are eligible for approval are:

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

The RBI accords automatic approval to foreign technology agreements in all industries, within the following prescribed monetary limits:

- Lumpsum payments up to US\$ 2 million.
- Royalty payments up to 5 per cent of domestic sales and 8 per cent of exports without any restriction on the duration of royalty payments. The aforesaid royalty limits are net of Indian taxes and are computed in accordance with standard conditions.
- Royalty payment for the use of brand name/trademark of the foreign collaborator is allowed under the automatic route up to 1 per cent of domestic sales and 2 per cent of exports, where there is no technology transfer agreement.
- Royalty payment for various services in respect of hotel and tourism industry vary from 3 per cent of the capital cost for technical and consultancy services, 3 per cent of turnover for marketing support fees, to 10 per cent of the gross operating profits for management fees. These limits apply to hotels with at least 500 rooms.

Foreign Portfolio Investment

Besides direct investment in India, non-residents can also make portfolio investments. FIIs are allowed to invest in the primary and secondary capital markets in India under the portfolio investment scheme.

The term FII is defined as an institution established or incorporated outside India for making investment in Indian securities and also includes a sub-account of an FII. FIIs must register themselves with the SEBI and comply with the exchange control regulations of RBI.

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

Investment Limits. The investment limits as laid down in the FII Guidelines and the RBI Regulations are as follows -

- An FII and each of its sub-accounts can individually invest up to 10 per cent of the paid-up share capital of an Indian company. However, an FII together with all its sub-accounts cannot hold more than 10 per cent of the paid-up capital of an Indian company. A lower limit of 5 per cent applies to foreign corporations and foreign individuals as sub-accounts.
- FIIs can cumulatively hold up to 24 per cent of the paid-up share capital of a company, but they may increase their holding up to the applicable sectoral limits on the various sectors with the approval of the board of the investee Indian company. The shareholders of the investee Indian company must also pass a special resolution to approve such an increase. The foreign investment under portfolio investment scheme is in addition to the amounts invested as FDI in the Indian company.
- Unless a FII is registered as a debt fund, the total investment in equity and equity-related instruments should not be less than 70 per cent of the aggregate of all its investments. An FII registered as a debt fund can invest the entire amount in debt securities.

The above investment restrictions do not include investments made by an FII through offshore funds, GDRs, ADRs or Euro-convertible Bonds.

FIIs are allowed to tender their shares in the case of an open offer following a takeover bid by an acquirer. They are also permitted to take forward cover on their equity and debt exposures to hedge against currency fluctuations. However, they are not allowed to short sell and can only engage in delivery-based trading.

Registration Eligibility. FII Guidelines require FIIs to meet certain qualifying conditions for registration. For example, they are required to have a good track record and be professionally competent. They must be registered with the appropriate foreign regulatory authority, and satisfy the 'fit and proper' requirements. SEBI also examines whether the grant of registration is in the interest of the development of the Indian securities market.

Registration of Sub-accounts. Besides entities that are eligible as FIIs, other foreign investors are also eligible for registration as sub-accounts. The sub-accounts may be (i) collective investment funds and institutions, (ii) proprietary funds or (iii) foreign corporations and individuals. The FII through whom an application is made for sub-account registration must be authorised to manage the investments on behalf of the sub-account. A fund or portfolio, which is already registered as a sub-account of an FII or as an FII, is not permitted to be registered as a sub-account of another FII.

ADRs / GDRs / FCCBs

Qualifying Indian companies are allowed to raise equity capital overseas through the issue of ADRs/GDRs/FCCBs. To qualify, the company must have a track record of good performance (financial or otherwise) for a minimum of three years. Where an issue of ADRs, GDRs or FCCBs by a company is likely to increase the permissible investment limits of FDI under the automatic route, or where such an investment is made in the form of a project that requires government approval, the company must seek approval from FIPB.

Preference Shares

Another way to invest in India is through the issue of preference shares. Foreign investment through convertible preference shares is treated as FDI. These investments may be made through the automatic route or the government route. The salient points for the issue of preference shares are as follows:

- Foreign investments through preference shares are considered as part of the share capital.
- Preference shares may be issued with or without a conversion option. If they are issued with a conversion option, they are treated as foreign equity and the FDI investment limits are applicable. If, however, such an option is not available then they are excluded from the FDI limits.
- Duration for conversion should not exceed the maximum time limit prescribed in the Companies Act, 1956, i.e. 20 years.
- Dividend rate should not exceed the limit prescribed by the MoF (3 per cent above prime lending rate of the State Bank of India).
- Issue of preference shares should conform to the guidelines prescribed by SEBI and RBI and must also meet other statutory requirements.

Investment by Non-resident Indians

NRIs can also invest on a non-repatriable basis in the shares or convertible debentures of an Indian company, either through public issue or private placement without any limit. These investments do not require FIPB approval. NRIs cannot invest in companies that are engaged in carrying on certain financial services activities or engaged in agricultural/plantation activities. While the capital is non-repatriable, the dividends and interest income can be remitted as current account transactions.

NRIs can invest in housing and real estate development and hold 100 per cent equity in civil aviation.

Investment in Export Trading Companies

Trading is permitted under the automatic route with an FDI of up to 51 per cent provided it is primarily export activities, and the undertaking is an export house/trading house/super trading house/star trading house.

In addition to the automatic route, 100 per cent FDI is permitted under the government route for various kinds of specified trading activities. Essentially, the government restricts retail trading operations by an Indian company which has foreign equity holding.

Foreign Exchange Controls

Foreign Exchange Policy

India's journey on the exchange control front is a well-travelled one. Since 1991, the country's foreign exchange reserves have surged from US\$ 2 billion to approximately US\$ 131 billion in December 2005. This achievement has been well-supported by the increasingly liberalized exchange control policy of the government.

FEMA virtually provides for full convertibility on capital and current account transactions for non-residents, while it subjects residents to non-convertibility on capital account transactions only.

The key changes under FEMA relate to the removal of rigid and stringent controls over transactions with non-residents. Under the FERA regime, a majority of these transactions required prior sanction from RBI. With the introduction of FEMA, the objective of the government has shifted from the conservation of foreign exchange to promoting an orderly development and maintenance of the foreign exchange market in India.

Current Account Transactions. The rupee is fully convertible for trade and current account purposes. Except for certain specified restrictions, foreign currency may be freely purchased for trade and current account purposes. In general, such purchases must be made at the market rate.

Some of the transactions for which a drawal of foreign exchange requires prior approval of RBI are:

- Release of exchange exceeding US\$ 10,000 or its equivalent in one calendar year, for one or more private visits to any country (except Nepal and Bhutan).
- Release of foreign exchange, exceeding US\$ 25,000 to a person, irrespective of the period of stay, for the purpose of business travel, to attend a conference or specialized training, maintenance expenses of a patient going abroad for medical treatment or check-up or for accompanying as attendant to a patient going abroad for medical treatment/check-up.
- Remittances exceeding US\$ 1 million for architectural/consultancy services procured from abroad subject to submission of satisfactory document.

- Remittances for the purchase of trademark/franchise in India.
- Remittance exceeding US\$ 100,000 by an Indian entity by way of reimbursement of pre-incorporation expenses.

Capital Account Transactions. These transactions are not permitted unless they are specifically allowed and the prescribed conditions are satisfied.

Transactions that are specifically allowed include the following:

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

The Indian foreign exchange market is developing fast, with banks offering a variety of instruments to companies to hedge foreign exchange risks. The level of activity in the Indian foreign exchange market is expected to increase once the rupee becomes fully convertible on the capital account.

The provisions in respect to the repatriation of foreign exchange for select purposes have been summarized below.

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

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

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

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

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

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

External Commercial Borrowings (ECBs)

Debts raised in foreign currency fall within the purview of the definition of ECBs, and are regulated by MoF and RBI. The guidelines issued by MoF/ RBI have prescribed various schemes through the use of which corporates and institutions may raise ECBs.

ECBs include commercial bank loans, buyer's credit, supplier's credit, securitized instruments such as Floating Rate Notes and Fixed Rate Bonds, etc., credit from official export credit agencies and commercial borrowings from the private sector window of multilateral financial institutions.

As per the revised ECB guidelines issued by MoF/RBI, ECB can be accessed under two routes, viz., automatic route and approval route.

Automatic Route

ECBs up to US\$ 500 million have been put under the automatic route subject to the compliance of the ECB policy. ECB can be availed by corporates registered under the Companies Act except for financial intermediaries (such as banks, financial institutions, housing finance companies and NBFCs). It has to be availed from an internationally recognized source, export credit agencies, suppliers of equipment, foreign collaborators and foreign equity holders. For a foreign equity holder to be eligible as a recognized lender under the automatic route would require minimum holding of equity in the borrower's company as under:

- ECB up to US\$ 5 million minimum equity of 25 per cent held directly by the lender,
- ECB more than US\$ 5 million minimum equity of 25 per cent held directly by the lender and debt-equity ratio not exceeding 4:1 (i.e. the proposed ECB not exceeding four times the direct foreign equity holding).

ECB can be availed by corporates only in the real sector - industrial sector including small and medium enterprises and the infrastructural sector. ECB proceeds, under no circumstances, can be used for on-lending, investment in capital market,

working capital and real estate. The ECB availed has to be parked abroad unless actually required.

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

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

Prepayment of ECB up to US\$ 200 million is allowed without prior approval of RBI, however, the stipulated minimum average maturity period as applicable for the loan has to be complied with.

Approval Route

An empowered committee of RBI decides all cases falling outside the purview of the automatic route in the new ECB policy.

B.3 Economic Laws and Regulations

Economic laws and regulations include the Indian Contract Act, 1872, intellectual property rights protection, labour laws, anti-trust regulations, consumer protection act, arbitration and company law (see section C.1)

Key Economic Laws

- Indian Contract Act, 1872
- Copyright Act, 1957
- Trademarks Act, 1999
- Geographical Indications of Goods Act, 1999
- Indian Patents Act, 1970
- Designs Act, 2000
- Industrial Disputes Act, 1947
- Maternity Benefit Act, 1961
- Payment of Bonus Act, 1965
- Payment of Gratuity Act, 1972
- Workmen's Compensation Act, 1923
- Industrial Employment (Standing Orders) Act, 1946
- Minimum Wages Act, 1948
- Payment of Wages Act, 1936

Key Economic Laws

- The Factories Act, 1948
- Employees Provident Fund and Miscellaneous Provisions Act, 1952
- Monopolies and Restrictive Trade Practices Act, 1969
- Competition Act, 2002
- Consumer Protection Act
- The Negotiable Instruments Act, 1881
- The Sale of Goods Act, 1930
- Arbitration and Conciliation Act, 1996

Indian Contract Act, 1872 (ICA)

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

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

ICA includes the following general principles of contract:

- Formation of a contract.
- Competence of contracting parties.
- Validity of a contract.
- Performance of contracts vis-a-vis liability/obligation of contracting parties.
- Breach of contract and damages.
- In order to form a contract, there should be a proposal and acceptance of the proposal.
- A contract is valid and enforceable by or against a contracting party only if such party consents and is legally competent to contract, i.e. is a natural or artificial person, of sound mind and is not a minor.
- A contract may be written, oral or implicit by conduct.
- A contract should have some lawful, real and valuable but not necessarily adequate consideration and should be for a lawful object.
- The consideration may flow either from the contracting parties to each other, or from a third party.
- There is a privity of contract, i.e. contracts are not enforceable by or against a third party. However, contracts executed for the benefit of a third party may be enforceable by such third party.

- A breach of contract may give rise to two remedies-damages or specific performance. Damages may be either liquidated or unliquidated. However, penalties and exemplary damages are not enforceable. Specific performance may be sought in certain cases of breach under the Specific Relief Act, 1963.
- Agreements in restraint of inter alia legal proceedings, trade, and marriage, wagering contracts are void contracts and are not enforceable.
- ICA also provides for the rights and obligations governing the parties in relation to the contract of indemnity, guarantee and bailment.
- ICA lays down the general principles governing the law of agency including the agent-principal relationship, rights and liability of agent inter se principal and third party, revocation/termination of agency, etc.

Intellectual Property Rights Protection

The term 'intellectual property', in the international legal parlance covers patents, industrial designs, copyrights, trademarks, know-how and confidential information. The laws relating to intellectual property in India are still in the process of transition and are being harmonized with the corresponding laws in developed countries.

With the objective of containing piracy in India and promoting the use of legal software, import of software for authorized duplication is allowed at reduced customs duty.

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

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

Copyrights

A copyright is an intangible, incorporeal right granted by the statute to the author or originator of a work whereby he obtains, sole and exclusive privilege of reproducing the work for a limited period, which depends on the nature of the work sought to be copyrighted.

India's copyright law, laid down in the Indian Copyright Act, 1957 as amended by Copyright (Amendment) Act, 1999, fully reflects the Berne Convention on Copyrights, to which India is a party. Additionally, India is party to the Geneva Convention for the Protection of Rights of Producers of Phonograms and to the

Universal Copyright Convention. India is also an active member of the World Intellectual Property Organization (WIPO), Geneva.

Main features of the Copyright Act

- Provide defined categories of works in which copyright subsists and the scope of the right conferred on the author under the Act.
- Provide for compulsory licensing of copyright in certain cases.
- Encourage registration of copyright by making institution of proceedings regarding infringement of copyright subject to the registration of copyright.
- Creation of a copyright office and copyright board to facilitate the registration of copyright and to settle disputes arising under the Act.
- Separate copyright for the cinematographic film apart from its various components namely, story, music, etc.
- International copyrights relation based on international treaties to be regulated by specific orders made by the central government.

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

As per the Act, copyright in work vests in the author named in the Register of Copyrights maintained by the copyright office. It may be noted that the registration of work is neither necessary nor a condition precedent to sue for damages for passing-off of copyright.

The copyright law in India has been amended from time to time to keep pace with the changing requirements. The amendments made to the copyright law have ushered in comprehensive changes and brought it in line with the new developments in satellite broadcasting, computer software and digital technology. Computer programmes and computer databases are classified as 'literary work' and are protected by the copyright law. The law has also made provisions to protect the performer's rights as envisaged in the Rome Convention.

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

Trademarks

A 'trademark' may consist of a word or invented word, signature, device, letter, numeral, brand, heading, label, name written in a particular style, the shape of goods other than those for which a mark is proposed, or any combination thereof or a combination of colours and so forth capable of distinguishing the goods or services of one undertaking from those of others.

To provide for the registration and protection of trademarks and for the prevention of the use of fraudulent trademarks, the Trade and Merchandise Marks Act was passed in 1958. Keeping in view the changes in the trade and commercial practices, globalization of trade, need for simplifying and harmonizing the trademarks registration systems, etc. Comprehensive review of the Trade and Merchandise Marks Act, 1958 was made and a Bill to repeal and replace the 1958 Act was passed by the parliament in 1999.

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

The Trademarks Act, 1999 was passed by the Parliament in 1999 and the Trademarks Rules, 2002 were notified on February 26, 2002. The Trademarks Act, 1999 provides for the registration of trademarks for services and goods, including collective marks, and for the assignment and transmission of trademarks. There is provision for an appellate board for speedy disposal of appeals, rectification of applications and simplification of procedures for the registration of the registered user and for enlarging the scope of the permitted use of trademarks and prohibition on the use of someone else's trademarks as part of corporate names or names of business concerns. The Act also provides for the incorporation of other provisions like amendment in the definition of 'marks', provision for filing of single application for registration in more than one class, a 10 year period for the registration and renewal of trademarks and for making the trademarks offence cognisable.

The Trademarks Act, 1999 came into force on September 15, 2003. On the same date, the Intellectual Property Appellate Board was set up in Chennai. The said act is compatible with the TRIPS agreement.

A project to upgrade infrastructural facilities with technical assistance from WIPO is currently under implementation to augment the existing capacity and provide a user-friendly system.

Geographical Indications of Goods

The Geographical Indications of Goods (Registration and Protection) Act, 1999 (GI Act) was passed by the Parliament in December 1999 and the Geographical Indications of Goods (Registration and Protection) Rules, 2002 were notified on March 8, 2002. The legislation was brought into force on September 15, 2003 as notified by the government of India.

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

The term 'geographical indication' in relation to goods, means an indication which identifies such goods as agricultural goods, natural goods or manufactured goods as originating or manufactured in the territory of the country, or a region or locality in that territory, where a given quality, reputation or other characteristics of such goods is essentially attributable to its geographical origin.

The GI Act prohibits the registration of such geographical indications (i) which are likely to deceive or cause confusion, (ii) which would be contrary to any law for the time being in force, (iii) which comprise or contain scandalous or obscene matter, (iv) which comprise or contain any matter likely to hurt the religious feelings of any class or section of citizens in India, (v) which would otherwise be disentitled to protection in a court, (vi) which are determined to be generic names or indications of goods and are, therefore, not, or have ceased to be protected in the country of origin, or which have fallen into disuse in that country, (vii) which, although literally true as to the territory, region or locality in which the goods originate, falsely represent to the persons that the goods originate in another territory, region or locality.

To receive applications for geographical indications of goods as provided in the Geographical Indications Act, 1998, the government of India has set up a Geographical Indications Registry at Chennai.

Patents

The Indian Patents Act, 1970 provides for the grant, revocation, registration, license, assignment and infringement of patents in India. A patent is a monopoly right granted to a person for the invention of a new and useful article, improvement of an existing article or formulation of a new process for making an article. The following are the essential ingredients of a patent.

- Novelty
- Inventiveness
- Industrial application

Any infringement of a patent is punishable under the terms of this Act. A patent is 'infringed' by any person who, without the grant of a license by the owner of the patent, undertakes anything, which, as per the provisions of the Act, only the owner of the patent is entitled to undertake.

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

The Indian Patents Act is administered through the head office located at Kolkata and branch offices located at New Delhi, Chennai and Mumbai. In order to improve the administrative infrastructure, the government has initiated modernization of the patent offices in association with WIPO.

The main components of this project are computerization of operations, networking of offices, improvement in infrastructure, recruitment of additional workforce, redesigning of the patenting procedure and simplification of the procedures. Several activities have already been undertaken and completed and the remaining are underway.

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

Industrial Designs

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

The term design means the shape, configuration, pattern, ornamentation or composition of lines or colours applied to any article in any form. It does not include any mode or principle of construction, or any thing which is in substance a mere mechanical device and does not include any trademark.

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

The terms of protection and obligations imposed upon the owner of design are:

- Any person claiming to be the author of a new and original design not previously published in any country, and which is not contrary to public order, can file an application for the registration of the design under the Designs Act.
- On registration, the author of the design is assured of exclusive rights to sell, distribute, manufacture and import such design and such registered articles to which the design is applied for a period of 10 years from the date of registration.
- The Designs Act provides for penalty for the infringement of the design.

As per the provisions of the Act, the owner of any international design can file an application in the prescribed form and apply for the registration of the same design in India, provided such an application is filed within six months of filing the original application in the other country.

The right conferred by the registration of a design is called 'copyright'. This appears to be a misnomer, as it has no resemblance to the copyright under the Copyright Act, and is more akin to the right given under the Patents Act.

Copyright in an industrial design or product is governed by the Designs Act, 2000. If a design is registered under this Act, it does not qualify for protection under the Copyright Act though it may be an original artistic work.

In the event of a design which is capable of registration under the Designs Act, but is not so registered, copyright will subsist in the Copyright Act, 1957, but it will cease to exist as soon as any article to which the design has been applied, has been reproduced more than 50 times through an industrial process by the owner of the copyright. Therefore, designs, which are not registerable under the Designs Act, get protection under the Copyright Act provided they are original artistic works.

Labour Laws

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

The government continuously reviews various labour laws to keep them in line with the changing circumstances. These laws address various issues such as the resolution of industrial disputes, working conditions, labour compensation and insurance.

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

Industrial Disputes Act, 1947 (IDA)

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

The definition of 'workman' under IDA does not include a person who, employed in a supervisory capacity, draws wages exceeding Rs 1,600 per month or is employed in a managerial or administrative capacity.

IDA applies to any 'industrial establishment or undertaking', which means an establishment or undertaking in which an industry is carried on. The term 'industry' in this regard is defined as 'any business, trade, undertaking, manufacture or calling of employers, and includes any calling, service, employment, handicraft, or industrial occupation or avocation of workmen.'

IDA lays down the following conditions to be complied with before the termination/retrenchment or lay off of a workman who has been in continuous service for not less than a year under an employer:

- The workman has been given one month's notice in writing indicating the reasons for retrenchment and the period of notice has expired, or the workman has been paid, in lieu of such notice, wages for the period of the notice.
- The workman has been paid, at the time of retrenchment, compensation which shall be equivalent to 15 days' average pay for each completed year of continuous service or any part thereof in excess of six months.
- Notice, in the prescribed manner, is served on the appropriate government.

IDA also lays down compliance requirements in case of a lock-out, closure and sale of the unit.

As per IDA, a person who indulges in any unfair labour practices is punishable with imprisonment up to six months and/or a fine up to Rs 1,000.

Maternity Benefit Act, 1961 (MBA)

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

MBA applies to factories, mines and plantations including any such establishment belonging to the government, shops or establishments and to other establishments in which people are employed for the exhibition of equestrian, acrobatic and other performances.

MBA does not apply to any factory or other establishment to which the Employees State Insurance Act, 1948 (ESI Act) is applicable. However, where the factory/establishment is governed under the ESI Act and the woman employee is not qualified to claim maternity benefit under the ESI Act, then such a woman employee is entitled to claim maternity benefit under this Act.

The following categories of women are covered under MBA:

- Pregnant women.
- Women taking leave for the delivery of a child.
- Women taking leave due to miscarriage.
- Women who have fallen ill because of pregnancy, delivery, premature birth of a child, miscarriage, medical termination of pregnancy or tubectomy operation.

Every woman employee, whether employed directly or through a contractor, who has actually worked in an establishment for a period of at least 80 days during the 12 months immediately preceding the date of her expected delivery, is entitled to receive maternity benefits under the Act. The employer is thus required to pay maternity benefits and/or medical bonus and allow maternity leave and nursing breaks to women employees, in accordance with the provisions of the Act. In addition, employers should not knowingly engage pregnant women in duties/tasks

in contravention of the Act, and not dismiss or discharge a pregnant woman employee during the period of the maternity leave.

MBA prescribes monetary penalties (up to Rs 500) as well as imprisonment (up to 3 months) for the contravention of its provisions by the employer.

Payment of Bonus Act, 1965 (PBA)

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

PBA is applicable to factories and establishments employing 20 or more persons on any day during an accounting year. The government has been empowered to extend its provisions to any other establishment employing 10 or more employees.

PBA is applicable to persons, other than apprentices, employed on a salary or wage not exceeding Rs 3,500 per month, in any industry, to do any skilled or unskilled, manual, supervisory, managerial, administrative, technical or clerical work for hire or for reward, whether the terms of employment are express or implied.

The minimum bonus which an employer is required to pay even if he suffers losses during the accounting year or there is no allocable surplus is 8.33 per cent of the salary or wages during the accounting year, or Rs 100 in the case of employees above 15 years of age and Rs 60 in case of employees below 15 years of age, at the beginning of the accounting year, whichever is higher.

If in an accounting year, the allocable surplus, calculated after taking into account the amount 'set on' or the amount 'set off' exceeds the minimum bonus, the employer in lieu of such minimum bonus, is liable to pay bonus in proportion to the salary or wages earned by the employee in that accounting year, subject to a maximum of 20 per cent of such salary or wages.

The bonus should be paid in cash within eight months from the close of the accounting year or within one month from the date of enforcement of the award or coming into operation of a settlement following an industrial dispute regarding payment of bonus. However, if there is sufficient cause, extension may be applied for.

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

For the contravention of the provisions of the PBA or rules, or on failure to comply with the directions or requisitions made under PBA, the penalty is imprisonment up to six months or fine up to Rs 1,000, or both.

Payment of Gratuity Act, 1972 (PGA)

PGA provides for a scheme for the payment of gratuity to all employees engaged in factories, mines, oilfields, plantations, ports, railway companies, shops and other establishments employing 10 or more employees on any day in the preceding 12 months.

PGA is applicable to all employees employed on wages to do any skilled, semi-skilled, or unskilled, manual, supervisory, technical or clerical work, whether the terms of such employment are express or implied, and whether or not such a person is employed in a managerial or administrative capacity. It defines the term 'employee' to mean a person other than an apprentice, who is employed on wages in any capacity.

Gratuity is payable to an employee on his retirement/resignation, superannuation, termination on account of death or disablement due to accident or disease or retirement. Normally, gratuity is payable only after an employee completes five years of continuous service. In the case of death and disablement, the condition of minimum five years' of service is not applicable.

PGA provides for compulsory payment of gratuity, to every employee, subject to a maximum of Rs 350,000, on the termination of his employment, after he has rendered continuous service for at least five years.

As per the provisions of PGA, gratuity is paid at the rate of 15 days salary of the employee for each completed year of service. In a seasonal industry, it is paid at the rate of seven days salary after each year of service.

Every employer must also procure the insurance of his gratuity liability with the Life Insurance Corporation or any other prescribed insurer.

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

Workmen's Compensation Act, 1923 (WCA)

The object of the WCA is to compensate an employee for any injury suffered during the course of his employment. WCA provides that compensation shall be paid to a workman in the case of his surviving an injury and to his dependants in the case of his death.

WCA is applicable to provide for the payment of compensation by certain classes of employers to their workmen (as defined under the WCA).

WCA applies to all workmen employed in factories, and in other establishments carrying out manufacturing activities. It also applies to all drivers and workmen employed by a company engaged in the transportation of goods. However, the WCA Act does not cover employees engaged in a clerical capacity.

WCA prescribes conditions under which compensation may be denied to an employee. It prescribes compensation to be paid at the following rates:

- For death resulting from the injury-50 per cent of the monthly wages of the deceased workman multiplied by the relevant factor or Rs 80,000, whichever is higher.
- For permanent total disablement resulting from the injury- 60 per cent of the monthly wages of the deceased workman multiplied by the relevant factor or Rs 90,000, whichever is higher.

Rs 4,000 per month is the maximum wage to be considered for computing compensation.

Industrial Employment (Standing Orders) Act, 1946 (IEA)

IEA requires employers in industrial establishments to provide for the conditions of employment for the employees.

IEA applies to establishments employing 100 or more workmen on any day of the preceding 12 months. However, the centre and state governments may extend the provisions of the IEA to any establishment employing less than 100 workmen. Therefore, now almost all establishments employing more than 50 workmen are covered by this Act.

IEA requires the employer to clearly define the conditions of employment to its workers by issuing standing orders/service rules relating to the matters set out in the schedule of the IEA. The standing orders are to be certified by the certifying officer appointed under the IEA.

The Industrial Employment (Standing Orders) Central Rules, 1946 provides for model standing orders, with respect to the classification of workmen, holidays, shifts, payment of wages, leaves, termination, etc. Model standing orders are temporarily applicable to an establishment that comes under the provisions of IEA and whose standing orders are not certified.

Minimum Wages Act, 1948 (MWA)

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

Under MWA both the state and the central government are 'appropriate governments' for fixation/revision of minimum rates of wages for the employments it covers. The central government is responsible for the fixation and revision of minimum wages for unskilled workers in scheduled employments.

Payment of Wages Act, 1936 (PWA)

The PWA seeks to regulate the payment of wages to certain classes of employees in an industry. It seeks to ensure that the wages payable to the employees covered under PWA are disbursed by the employers within the prescribed time limit, and that no deductions other than those authorized by law are made by the employers. It provides for the payment of wages to persons employed in any factory, persons employed (other than a factory) in any railway by the railway administration, either directly or through a sub-contractor or by a person fulfilling a contract with the railway administration and to persons employed in an industrial or other establishment.

Every person employed in the establishment and drawing wages less than Rs 1,600 per month is covered under the Act. The term 'wages' includes all remuneration, bonus or sums payable for the termination of service, but does not include inter alia house rent reimbursement, travel allowances, medical expenses, etc.

The state government is empowered to extend the applicability of PWA to any class of person(s) employed in any establishment or class of establishments.

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

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

Factories Act, 1948

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

The term 'factory' under this Act means any premises where:

- 10 or more workers carry on their work and the manufacturing process is carried on with the aid of power. or
- 20 or more workers carry on their work and the manufacturing process is carried on without the aid of power.

The term 'worker', 'manufacturing process' and 'power' are also defined under this Act.

With respect to health standards, every factory is required to maintain cleanliness, proper ventilation, temperature, lighting and other sanitation facilities on its premises. Further, with respect to safety measures, every factory should ensure the safety of its employees by keeping the machinery in good condition, protecting the employees from exposure to dangerous fumes and gases and installing necessary equipments to combat fire or any such contingent peril. With regards to the welfare measures, every factory is required to provide certain basic facilities to its employees such as canteens, shelters, rest rooms, lunch rooms, first aid appliances, crèches, etc.

The Act prohibits the employment of young children in factories who have not attained the age of 14 years. Further, with respect to children having attained the age of 14 years, the Act provides that they shall be allowed to work in a factory only after a grant of certificate of fitness in accordance with the provisions of the Act.

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

Employees Provident Fund and Miscellaneous Provisions Act, 1952 (EPFMPA)

The EPFMPA seeks to ensure the financial security of the employees in an establishment by providing for a system of compulsory savings. EPFMPA covers any establishment, which is a factory, engaged in any industry specified under EPFMPA in which 20 or more persons are employed, and any other establishment as notified by the government, from time to time and their employees in India. EPFMA provides that the employee's contribution shall at least be equal to the contribution payable by the employer in respect of him. However, the employee is entitled to contribute more than such minimum contribution, if he so desires.

A provident fund, as required to be established under EPFMPA, is a contributory fund created to secure the future of the employees after retirement.

Where the number of employees is less than 50, employees have to pay 10 per cent of their basic wages, dearness allowance and retaining allowance, (if any) into the fund. Should the number of employees be more than 50, the employees have to contribute 12 per cent of their basic wages, dearness allowance and retaining allowance, (if any). In the case of an employee's early death, his contribution along with appropriate interest is paid to the person nominated by him, subject to such deductions as authorized by the scheme or rules. Employees are also allowed to withdraw a part of their provident fund before retirement for certain specified purposes.

The government has prescribed various penalties at prescribed rates for any default, which the employer may make in connection with the payment of any contribution, arrears, accumulations, administrative charges, to the fund and/or has also prescribed imprisonment for a term, which may extend up to one year or a fine of Rs. 5000 or both.

Anti-Trust Regulations

Anti-trust laws are designed to preserve the free enterprise of the open market by making illegal certain private conspiracies and combinations formed to minimize competition. Most violations of anti-trust laws involve either price-fixing (entities conspiring to set fixed market prices/rates) or unfair allocation of customers or markets (entities agreeing to limit their units/areas of trade).

It is globally accepted that any forms of trusts and/or monopolies which lead to the concentration of wealth in the hands of a few are injurious to the public and individuals because such monopolies minimize, if not obliterate, normal market competition and yield undesirable price controls. These, in turn, cause the markets to stagnate and sap individual initiative. In line with global norms and to prevent monopolies from creating restraints on trade or commerce and reducing competition in India, the government of India has evolved an anti-trust regulatory framework that revolves principally around the following legislations:

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

These laws are designed to maintain economic liberty and to eliminate any unfair restraints on trade and competition. The following are the salient features of each of the above legislations.

Monopolies and Restrictive Trade Practices Act, 1969 (MRTP Act)

The Competition Act received the assent of the President on January 13, 2003 and was published in the Gazette on January 14, 2003. The Act intends to repeal the MRTP Act. However, as of date, except for certain provisions relating to the formation and establishment of the CCI and selection of the chairman and members of CCI, which have come into effect from March 31, 2003, and June 19 and October 14, 2003, respectively, no substantive provision of the Act is in force and the same would come into force as and when notified by the central government. As of now, the MRTP Act is still in force.

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

- A restrictive trade practice refers to a trade practice which has the effect of preventing or restricting competition in any manner and which tends to bring about the manipulation of prices or affects the flow of supplies of goods and

services in the market so as to impose unjustified costs and restrictions on the consumers.

- An unfair trade practice refers to a trade practice, which for the purpose of promoting the sale or use of any goods or services adopts any unfair method or deceptive practice, including falsely representing the characteristics, performances, uses or benefits of a product in a manner that misleads the consumer/public.
- A monopolistic trade practice refers to a trade practice which has the effect of maintaining the prices of goods at unreasonable levels, or which prevents or limits competition or increases to an unreasonable extent the prices of goods or services.

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

Under the terms of the MRTP Act, the Commission has been conferred inter alia with the following powers:

- Right to investigate restrictive trade practices, which may be prejudicial to public interest.
- Direct an undertaking guilty of indulging in any restrictive, unfair or monopolistic trade practice from discontinuing the said practice.
- Pass a cease-and-desist order whereby an undertaking would be required to stop work forthwith and to abstain from carrying on any activity prohibited under the MRTP Act.
- Grant a temporary injunction, restraining an errant undertaking from continuing an alleged restrictive, unfair or monopolistic trade practice.
- Award compensation for loss suffered or injury sustained by any consumer on account of any restrictive trade practice, unfair trade practice and monopolistic trade practice.
- Direct parties to agreements containing restrictive clauses, to modify the same.

Further, under the provisions of the MRTP Act, in certain circumstances, a restrictive trade practice may not be considered to be prejudicial to public interest and accordingly it would be outside the purview of the powers of the Commission to pass any adverse order with respect to the arrangement entered into between the parties. These are commonly referred to as 'gateways'. Such gateways include inter alia:

- Where the restriction is necessary to protect the public against injury caused by consumption of the goods;
- Where the restriction does not directly or indirectly restrict or discourage competition to any material degree in the relevant trade or industry; and
- Where the removal of the restriction would deny the customers or consumers

of the goods, any benefit which they enjoy or are likely to enjoy by virtue of the restriction or any arrangements or operations resulting there from.

The aforesaid concept of 'gateways' is not available under the Competition Act.

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

Competition Act

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

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

The major provisions of the Competition Act relate to the following areas:

- *Prohibition of Anti-Competitive Agreements.* Horizontal agreements, i.e. agreements between enterprises engaged in similar businesses, are void ab initio, as these agreements would be presumed to have an appreciable adverse effect on competition in India. Vertical agreements, i.e. agreements between enterprises engaged in different stages of the production chain in different markets, would be void only if it causes or is likely to cause appreciable adverse effect on competition in India.
- *Prohibition of Abuse of Dominant Position.* A dominant position is defined in the Act to mean a position of strength, enjoyed by an enterprise, in the relevant market, in India, which enables such an enterprise to operate independent of the competitive forces prevailing in the relevant market or influences the competitors or consumers or the relevant market in its favour. The Act permits an enterprise to be in a dominant position. However, the Act seeks to check abuse of the dominant position by an enterprise. Section 4 of the Act lays down certain conditions, which if satisfied by an enterprise, would amount to the abuse of the dominant position by such an enterprise.
- *Regulation of Combinations.* Combinations may be of three types, (i) acquisition of one or more enterprises by another enterprise; (ii) acquisition of control over an enterprise by a person having control over another enterprise engaged in similar or identical or substitutable goods or services; or (iii) merger or amalgamation of enterprises. A combination will trigger the provisions of this Act, if the asset value and turnover exceeds certain limits as provided in the Act.

- *Establishment, Powers, Functions and Duties of CCI.* CCI, a quasi-judicial body, promotes and advocates competition and prevents practices having an adverse effect on competition. CCI is required to function as a regulator to give impetus to the quality of products and services, competition, faster mergers and acquisitions of companies, regulation of acquisitions and mergers falling within the threshold limits and allowing dominance and prevention of abuse of dominance. CCI has the power to examine whether any act of any enterprise/person would fall within the ambit of the anti-competitive practices under the criterion specifically provided in the various provisions of the Act.

CCI has been conferred with the powers to make inter alia the following kinds of orders:

- Declare an agreement, which contains a restrictive trade practice as void ab initio.
- Order division of dominant enterprises or grant interim relief or any compensation.
- Prohibit agreements regarding prices/quantities, tenders/bids or regarding market sharing by type, size of customer or in any other way.

Consumer Protection Act (CP Act)

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

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

The CP Act contains provisions for district, state and national consumer disputes redressal fora to adjudicate over claims, complaints and disputes, which result under the provisions of the CP Act. The District Consumer Disputes Redressal Forum has the power to entertain matters where the value of goods/services or compensation claimed, if any, does not exceed Rs 2 million. The State Consumer Disputes Redressal Forum has the power to entertain matters where the value of goods/services or compensation claimed, if any, exceeds Rs 2 million but does not exceed Rs 10 million. The National Consumer Disputes Redressal Forum has the power to entertain matters where the value of goods/services or compensation claimed, if any, exceeds Rs 10 million.

The aforesaid disputes redressal fora are conferred with the powers to pass, inter alia, the following kinds of orders:

- Remove the defect pointed out by an appropriate laboratory after carrying out required tests.

- Replace the goods with new goods of similar description which shall be free from defect.
- Return to the complainant the price or the charges/costs paid by the complainant.
- Pay any amount as compensation for loss or injury suffered by the consumer.
- Withdraw any hazardous goods from sale.
- Discontinue unfair or restrictive trade practices.

Negotiable Instruments Act, 1881 (NI Act)

Negotiable instruments are documents meant for making payments, the ownership of which can be transferred from one person to another many times before the final payment is made and is governed by the NI Act. The main object of the NI Act is to legalize the system by which instruments contemplated by it could pass from hand to hand by negotiations like any other goods.

The law relating to promissory notes, bills of exchange, cheques and other negotiable instruments is codified in India under the NI Act. It defines promissory note, bill of exchange, cheque, foreign instrument and negotiable instrument. As per the provisions of this Act, in India, every person capable of contracting, according to the law to which he is subject, may bind himself and be bound by making, drawing, accepting, endorsing, delivering and negotiating of a promissory note, bill of exchange or cheque and every person capable of binding himself or of being bound, may so bind himself or be bound by a duly authorized agent acting in his name. The Act provides for the liability of an agent, legal representative, drawer, drawee, maker and acceptor of a bill, endorser, holder in due course, suretyship, etc. As per the provisions laid down in the said Act, a negotiable instrument means a promissory note, bill of exchange or cheque payable either to order or to bearer and when a promissory note, bill of exchange or cheque is transferred to any person so as to constitute the person, the holder thereof of the instrument is to be negotiated. Detailed provisions have been made in the Act concerning presentment, payment, interest, discharge from liability, notice of dishonour, noting and protest, reasonable time for payment, acceptance and payment for honour and reference in case of need, compensation, special rules of evidence, providing for certain presumptions and estoppels, cross cheques, bills in sets, etc.

The NI Act was amended by the Banking, Public Financial Institutions and Negotiable Instruments Laws (Amendment Act), 1988 wherein a new Chapter of XVII was incorporated for penalties in the case of dishonour of cheques due to insufficiency of funds in the account of the drawer of the cheque. These provisions were incorporated with a view to encourage the culture of the use of cheques and to enhance the credibility of the instrument. Under this chapter dishonour of a cheque in certain cases is an offence. The punishment for the offence is imprisonment for a term which may extend to one year or with fine which may extend to twice the amount of the cheque or with both.

Sale of Goods Act, 1930

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

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

Thus, the following are the essentials of the contract of sale:

- It is a contract, i.e. all requirements of a 'contract' must be fulfilled.
- It is of 'goods'.
- Transfer of property is required.
- Contract is between buyer and seller.
- Sale should be for a 'price'.
- A part owner can sell his part to another part-owner
- Contract may be absolute or conditional.

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

The Sale of Goods Act requires that the goods transferred by the seller to the buyer must be ascertained and there should be an intention of the seller to pass such goods to the buyer.

The Act also deals with transferring the title in the goods by a person who is not the owner of the goods.

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

After goods are sold and property is transferred to the buyer and he refuses to pay for the same, the only remedy with seller is to approach the Court. The seller has no right to take forceful possession of goods from buyer, once property in goods is transferred to him. However, the Act gives some rights to the seller if his dues are

not paid and the goods are not transferred to the buyer. These rights are as follows:

- A lien on the goods for the price while he is in possession of them.
- The right to stop the goods in transit after he has dispatched them, in case of insolvency of the buyer.
- A right of resale.

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

Arbitration

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

The Arbitration and Conciliation Act, 1996 has been enacted to meet the following objectives:

- Comprehensively cover domestic arbitration, international commercial arbitration and enforcement of awards under the New York and Geneva Awards and Conciliation.
- Make provisions for an arbitral procedure, which is fair, efficient and capable of meeting the needs of the specific arbitration.
- Provide that the arbitral tribunal gives reasons for its arbitral award.
- Ensure that the arbitral tribunal remains within the limits of its jurisdiction.
- Minimize the role of the courts in the arbitral process.
- Permit the arbitral tribunal to use mediation, conciliation or other procedures during the arbitral proceedings to encourage settlement of disputes.
- Provide that every final arbitral award is enforced in the same manner as if it were a decree of the court.
- Provide the manner of settlement of the conciliation proceedings with respect to disputes arising out of legal relationships, whether contractual or not and other proceedings relating thereto.

- Provide that a settlement agreement reached by the parties as a result of conciliation proceedings will have the same status and effect as an arbitral award on agreed terms on the substance of the dispute rendered by an arbitral tribunal.
- Provide for the establishment of the new Arbitration Division within each High Court where awards can be challenged under the provisions of the existing Act.
- Determine the time limit for the disposal of proceedings (pending or future) which is an improvement over the UNCITRAL model.
- Resolve the conflicts among some judgements of the High Court under the Act.
- Provide for fast track arbitration following a special procedure.

The amendments also propose to apply the provisions pertaining to interim measures by the court to international arbitration outside India.

B.4 Special Investment Considerations

Special Economic Zones

Overview

The FTP provides for the setting up of SEZs in the country with a view to provide an internationally competitive and hassle-free environment for exports. Units may be set up in an SEZ for manufacture, trading, re-conditioning and repair or for services activity. Units in SEZs have to be net foreign exchange earners but are not subject to any predetermined value addition or minimum export performance requirements. Sales in the domestic tariff area for SEZ units shall be subject to positive foreign exchange earnings and on payment of the full customs duty and subject to the FTP in force.

The policy provides for the setting up of SEZs in the public, private, joint sector or by state governments. The central government has also converted some of the existing EPZs into SEZs such as the EPZs at Kandla and Surat (Gujarat), Santa Cruz (Maharashtra) and Cochin (Kerala). There are 11 functional SEZs in India which includes multi-product as well as product-specific SEZs. Some of the functional SEZs are SEEPZ (Maharashtra), Kandla SEZ (Gujarat), Noida EPZ (Uttar Pradesh, near Delhi).

There are more than 40 SEZs which have been approved by the government and are under various stages of establishment. Some of the SEZs approved for setting up are located at Dronagiri (Maharashtra); Kulpi (West Bengal); Paradeep (Orissa); Bhadohi, Kanpur and Greater Noida (Uttar Pradesh); Kakinada (Andhra Pradesh); Hassan (Karnataka); Positra, Dahej, Mundra, Vanj-Surat, Hazira-Surat, and Icchapur-Surat (Gujarat) on the basis of proposals received from the state governments. Some of these SEZs are in the initial stages of development while some are ready for operations.

Special Economic Zones Scheme

The SEZ scheme has the following salient features:

- A designated duty-free enclave and to be treated as foreign territory for trade operations and duties and tariffs.
- The activities permitted to be carried out in the SEZs are the manufacture of goods, services, production, processing, assembling, reconditioning, re-engineering, packaging, trading, etc.
- SEZ units to be positive net foreign exchange earners.
- Duty-free goods to be utilized within the approved period of five years.
- Export proceeds to be realized and repatriated within twelve months.
- Monitoring of the performance of SEZ units by a unit approval committee consisting of the Development Commissioner and the Customs Authority.

Incentives for Special Economic Zones Units

- Duty-free import of capital goods (including second-hand capital goods), raw materials, consumables and spares.
- Duty-free procurement of capital goods (including second-hand capital goods), raw materials and consumable spares from the domestic market.
- Exemption from the payment of central sales tax on interstate purchases from the domestic market.
- Exemption from service tax for services provided to a unit (including a unit under construction) of the SEZ.
- Manufacturing, trading or service activity allowed.
- Subject to achievement of positive net foreign exchange earnings, SEZ units permitted to free to sell production in the domestic tariff area (DTA) on payment of full customs duty, subject to the import policy in force.
- Certain supplies in the DTA such as supplies to other EOU/ STP/ EHTP/ BTP/ SEZ units, holders of special import licences, sale of ITA bound items etc. (payments for which is received in Indian rupees) would be counted towards achievement of positive net foreign exchange earnings.
- Full freedom for subcontracting.
- Subcontracting of part of production permitted abroad.
- No routine examination by the customs of export and import cargo.
- Facility to realize and repatriate exports proceeds within 12 months.
- Re-export imported goods found defective, goods imported from foreign suppliers on loan basis without Guaranteed Receipt waiver under intimation to the development commissioner.
- Facility to retain 100 per cent of the foreign exchange receipts in the export earners foreign currency account.

Incentives for Developers of Special Economic Zones

- Procure goods from the domestic tariff area without the payment of duty or import specified goods without the payment of customs duty as may be notified by the government for the development of SEZ.
- Full freedom in the allocation of developed plots to approved SEZ units on purely a commercial basis.
- Full authority to provide services like water, electricity, security, restaurants and recreation centres on commercial lines.
- Facility to develop a township within the SEZ with residential areas, markets, playgrounds, clubs and recreation centres.
- Exemption from service tax and central sales tax.
- No net foreign exchange earning requirement / export obligation imposed on the SEZ developers.

Institutional Framework

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

Recent Developments in SEZ

The Parliament of India has enacted the Special Economic Zone Act, 2005. The Act is a single self contained legislation governing the operations of SEZs. The Act is yet to be operationalized along with relevant rules. Once operationalized, the Act would replace the legislations and various rules and regulations presently governing the SEZ operations. Indirect tax incentives available under the new Act for SEZ developers as well as for units operating in SEZ are the same as those provided under the existing dispensation. The direct tax incentives are given in the corporate tax section.

100 per cent Export-Oriented Units

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

FDI in EOUs qualifies for the automatic approval route, subject to confirming with the existing guidelines for FDI.

The following incentives are available for EOUs:

- Exemption from customs duty on industrial inputs and capital goods including second-hand capital goods (without age limit).
- Local procurement of inputs and capital goods (including second-hand capital goods) exempted from the payment of excise duty.
- Credit of service tax paid on input services is available to the EOU

- Reimbursements of central sales tax paid on interstate purchases.
- Units need to be positive net foreign exchange earners.
- DTA sale of goods or rendering of services is permitted up to 50 per cent free on board value of exports / or 50 per cent of foreign exchange earned subject to fulfillment of other obligations of the scheme.
- Certain supplies to the domestic tariff area counted towards the fulfilment of positive net foreign exchange earner.

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

State-level incentives

Various incentives are offered by state governments to encourage investment and attract capital. These commonly take the form of investment and power tariff incentives and other financial benefits.

For better economic development, state governments have proactively come up with several incentives which include:

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

In addition to the above, the states in north-east India and the state of Jammu and Kashmir offer additional incentives. These incentives range from 50 per cent to 90 per cent transport subsidy, income tax exemption to new units, 100 per cent subsidy on the purchase of quality control equipment, units with a fixed capital investment of Rs 250 million (US\$ 5.4 million) or above treated as prestigious units entitled for a capital investment subsidy of Rs 6 million (US\$ 0.13 million) and interest subsidy from 3 per cent to 5 per cent on working capital loan.

For a detailed overview of state incentives in India please visit siadipp.nic.in/state/stateince.htm.

Investment Incentives

This involves the state financing a certain percentage of the fixed capital cost of a project. Various states have designated areas as 'A', 'B' and 'C' according to their level of development. The level of incentives provided by a state varies and is generally larger for investments made in backward areas.

Further, the terms and ceiling of the incentives vary across states, depending on the nature of industry that the state is trying to promote.

Power Tariff Incentives

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

The actual incentives given vary across states and from industry to industry and are also dependent upon the area in which the unit is set up. Some states specify a list of industries that do not qualify for some of these incentives.

Other incentives

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

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

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

Government-owned Industries and Privatization

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

The government now recognizes that most industries develop through the enterprise and initiative of private individuals and companies. Consequently, since 1991, the government has reversed its previous policies of nationalization. To accelerate economic growth and to enhance international competitiveness, the government is taking measures to deregulate trade and industry, dismantle bureaucratic controls, liberalize international trade, privatize the public sector, encourage entrepreneurial activity and technological development and introduce financial sector and trade reforms.

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

- Atomic energy
- Railway transport

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

Disinvestment and Privatization

Phase I. The policy on disinvestments has evolved over a period of time. The process started when the government formulated a policy to divest 20 per cent of the government equity in selected PSUs in favour of public sector institutional investors. The objective of the policy was to attain broad-based equity, improved management, enhanced availability of resources for these PSUs and also to yield resources for the exchequer.

In 1993, the Rangarajan Committee, which was formulated to study the disinvestment of shares, emphasized the need for substantial disinvestment. It stated that the percentage of equity to be divested could be up to 49 per cent for industries explicitly reserved for the public sector. It recommended that in exceptional cases, such as enterprises which had a dominant market share or where a separate identity had to be maintained for strategic reasons, the target public ownership level could be kept at 26 per cent.

Phase II. The second phase of disinvestments started in 1999 when the government decided to bring down its shareholding in PSUs to 26 per cent in most of the cases, thus facilitating ownership changes. It was, however, stated that the government would retain majority holdings in PSUs involving strategic considerations. The highlight of the government policy of 1999-2000 was the expression 'privatization' which was used for the first time. The government set a goal to strengthen strategic PSUs, privatize non-strategic PSUs through gradual disinvestment or strategic sale and devise viable rehabilitation strategies for weak units.

The government also established a new department for disinvestment on December 10, 1999 to establish a systematic policy approach to disinvestment and privatization and to give fresh impetus to this programme, which will increasingly emphasize the strategic sales of identified PSUs.

In the budget of 2000-01, for the first time the government stated that it was prepared to reduce its stake in the non-strategic PSUs to even below 26 per cent, if necessary, and that there would be increasing emphasis on strategic sales and that the entire proceeds from disinvestments/privatization would be deployed in the social sector, restructuring of PSUs and retirement of public debt. The government policy also emphasized the need to fully protect the interests of the workers.

The following table summarizes the divestment policy of the government over the years:

Period	Policy / Goal / Target
1991	The policy was to divest 20 per cent of the government equity in selected PSUs.
1993	The need for substantial disinvestments was emphasized. The government stated that the percentage of equity to be divested could be up to 49 per cent for industries explicitly reserved for the public sector.
1999	The government decided to bring down its shareholding in PSUs to 26 per cent in most cases. The government set a goal to strengthen strategic PSUs and privatize non-strategic PSUs through gradual disinvestment or strategic sale and devise viable rehabilitation strategies for weak units.
2000	The government stated that it was prepared to reduce its stake in non-strategic PSUs to even below 26 per cent. The government also established a new department for disinvestment.
2001	A target of Rs 120,000 million (US\$ 2474 million) from disinvestment was set for 2001-2002.
2002	The government set a target of Rs 120,000 million (US\$ 2533 million) on disinvestments receipts.
2003	The government set a target of Rs 145,000 million (US\$ 3,305 million) on disinvestments receipts.

Phase III. The third phase of disinvestment and privatization started in May 2004 with the introduction of the National Common Minimum Programme (NCMP). NCMP effectively contains the disinvestment and privatization policy of the

government. It seeks to reaffirm the commitment of the government to a strong and effective public sector with the revival of sick and loss-making PSUs. The objective of the policy is the revival of sick and loss-making PSUs and divestment of only the minority stake in the profit-making PSUs through capital markets retaining the control thereby changing its policy from the strategic sale of profit-making PSUs.

The government on January 27, 2005 constituted the 'National Investment Fund' wherein the realization from the sale of minority shareholding of the government in profitable PSUs would be channelized. The fund has been created with an objective of investment in social sector projects like education, health, etc. and capital investment in selected profitable PSUs that yield adequate returns.

In the budget of 2004-05 the government, consonance with the policy declared in NCMP, provided financial support to PSUs including the railways and emphasized the retention of government control over PSUs and the maintenance of their public character.

The actual disinvestment from 1991-92 till date, the methodologies adopted for such disinvestment and the extent of disinvestment in different PSUs has been elucidated in Appendix 6.

B.5 Regional and International Trade Agreements and Associations

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

B.6 Major Trading Partners and Leading Imports and Exports

Trading Partners

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

Foreign Trade Policy

The FTP announced by the government seeks to complete the process of India's integration with the global economy by the removal of quantitative restrictions, and seeks to provide fresh direction to exports by setting up agricultural export zones, providing special benefits to SEZs and providing various export incentive schemes.

The FTP is forward-looking and liberal and is the logical conclusion to India's commitments under the WTO agreement.

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

Imports

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

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

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

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

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

Exports

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

Foreign Trade - Key Statistics

Exports: US\$ 79.41 billion (2004-05)

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

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

Imports: US\$ 107.28 billion (2004-05)

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

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

Balance of Trade

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

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

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

Tariff Liberalization

The current trade policy is characterized by rationalized tariff levels and the removal of quantitative restrictions.

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

C. Companies

C.1 Forms of Enterprise

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

- Corporations
- Partnerships
- Sole proprietorships

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

Brief Description of Major Types of Corporate Forms

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

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

Private Corporations

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

- The right to transfer shares is restricted.
- The maximum number of its shareholders is limited to 50 (excluding past and present employees who are members).
- No offer can be made to the public to subscribe to its shares and debentures.
- No invitation or acceptance of deposits from persons other than members, directors or relatives is allowed.

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

Public Corporations

A public corporation is defined as one that is not a private corporation. A subsidiary of a public corporation is also treated as a public corporation. A public corporation is required to have a minimum paid-up capital of Rs 0.5 million (US\$ 10,850) with a minimum of seven members and of three directors.

In both public and private corporations, if the name of the Indian company contains the word 'India', the minimum authorized capital would be Rs 0.5 million (US\$ 10,850)

Foreign Corporations

Foreign corporations that are incorporated outside India but have a presence in India in the form of liaison offices, project offices, branch offices, etc. are also governed by the Companies Act, 1956, which contains special provisions for regulating such entities. Such companies have to register themselves with the registrar of companies, New Delhi within 30 days of establishing a place of business in India.

Structures Typically Used by Foreign Investors

Foreign corporations conducting business in India may operate in various forms. Common business structures employed by foreign investors in India are private limited companies (mostly wholly-owned subsidiaries of the foreign companies), liaison offices, branches offices and project offices. These business structures are discussed in the following paragraphs.

Subsidiary Companies

Foreign corporations can set up their subsidiary companies form of private companies in India. Setting up of a corporation in India requires compliance with the procedures of incorporation laid down under the Companies Act, 1956.

The subsidiary company, incorporated under the laws of India, is treated as a domestic company for tax purposes.

In comparison with the branch office and liaison office (discussed in the following paragraphs), a subsidiary company provides maximum flexibility for conducting business in India. However, the exit procedure norms of companies are more cumbersome as compared to other forms of business such as branch, liaison and project offices, which can be exited more conveniently. Following are some of the features of a subsidiary company:

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

Branches

Foreign corporations may open branch offices to conduct business in India. For opening a branch office in India, foreign corporations require a specific approval from RBI. Such approval prescribes the activities that a branch office may undertake in India. Consequently, a foreign corporation cannot undertake any activity in India that is not specifically permitted by RBI.

A branch office is also required to register itself with the registrar of companies and comply with certain procedural formalities prescribed under the Companies Act, 1956.

A branch office is permitted to undertake the following activities:

- Export/import of goods.
- Rendering professional or consultancy services.
- Carrying out research work, in which the parent company is engaged.
- Promoting technical or financial collaboration between Indian companies and the parent or overseas group company.
- Representing the parent company in India and acting as a buying/selling agent in India.
- Rendering services in IT and the development of software in India.
- Rendering technical support to the products supplied by parent/group companies.
- Undertaking activities of foreign airline/shipping company.
- Manufacturing by a branch located in a SEZ.

For income tax purposes, a branch office is treated as an extension of the foreign corporation in India and taxed at the rate applicable to foreign companies. Some key tax and regulatory aspects of a branch office are as follows:

- It is treated as a taxable business entity.
- Transactions between a branch and the foreign corporation are subject to Indian transfer pricing regulations.
- The branch office is permitted to acquire immovable property necessary or incidental to carrying on activities approved by RBI.
- Post-tax profits are fully repatriable to the foreign corporation.
- Surplus funds, post winding up of the branch office, can be repatriated to the foreign corporation subsequent to RBI approval.

A branch office provides the advantage of ease in operations and also provides for an uncomplicated closure.

However, since the operations are strictly regulated by exchange control guidelines, a branch office may not provide a foreign corporation with the most optimum structure for its expansion/diversification plans.

Liaison Offices

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

The setting up of a liaison office in India is also subject to the conditions outlined in the permission granted by RBI. The liaison office also requires registration with the registrar of companies.

A liaison office in India is permitted the following activities:

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

Further, RBI has specified certain conditions which are to be adhered to:

- No commission or fee or any other remuneration may be charged by the Indian liaison office of the foreign corporation.
- The liaison office cannot undertake any activity of a trading, commercial or industrial nature.
- All expenses of the liaison office should be met exclusively by remittances from abroad through normal banking channels.
- The liaison office should submit an auditors certificate annually to RBI.

Project Offices

A foreign corporation, which has secured a contract from an Indian company to execute a project in India, may establish a project office in India without obtaining prior permission from RBI. The exchange control norms also prescribe the following additional requirements:

- The project should be funded directly by inward remittance from abroad; or
- The project should be funded by a bilateral or multilateral international financing agency; or
- The project must be cleared by an appropriate authority; or
- The Indian company awarding the contract should have been granted a term loan by a public financial institution or a bank in India for the project.

However, the foreign corporation would be required to furnish a prescribed report to the concerned regional office of RBI under whose jurisdiction the project office is set up.

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

C.2 Mergers and Acquisitions

Over the years, restrictive provisions that regulated the expansions, mergers, amalgamations and takeovers of domestic companies have been removed to a large extent. However, certain regulations continue to govern the acquisition of substantial interest in a company.

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

The Takeover Code requires the acquirer to make a public offer to the remaining shareholders to obtain in aggregate, a minimum 20 per cent of the voting capital, at a prescribed minimum offer price.

Acquirers holding more than 15 per cent but less than 55 per cent of the voting capital may increase their holdings by 5 per cent in any 12 month period without triggering the requirement to make a public offer. Acquirer holding 55 per cent or more but less than 75 per cent of the voting capital can acquire any additional share or voting right only if he makes the public offer.

Reorganizations and Mergers

Reorganizations of a company by a compromise (shareholders', creditors' and others' sacrifice of their claims and entitlements to resurrect the company) or by an arrangement between the company and its creditors requires sanctioning by the jurisdictional High Court. The power to approve reorganization and mergers has recently been shifted from the High Courts to NCLT. However, the NCLT is still in the process of being formed. Further, all material facts, including the company's latest audited financial report and any pending investigations have to be properly disclosed before any scheme is sanctioned.

Buy-back of Shares

The Companies Act, 1956 permits a company to buy-back its share capital up to a ceiling of 10 per cent of the paid-up equity capital and free reserves provided the same is sanctioned in the company's board meeting. However, no such offer shall be made within 365 days from the date of the preceding offer of buy-back made under sanction from the company's board. A company may also buy-back 25 per cent of the company's paid-up capital and free reserves provided the buy-back is sanctioned by a special resolution.

However, a company buying back shares is not allowed to issue further shares of the same class or other specified securities for a period of six months following the buy-back. Such restriction is not applicable to securities issued by way of bonus issues or conversion of warrants, preference shares or debentures. The Companies Act, 1956 also prescribes certain conditions relating to reserves, debt equity ratios, etc. for a company to be eligible for undertaking a buy-back of shares.

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

Companies listed on a stock exchange in India are subject to the guidelines prescribed by SEBI with respect to the buy-back of shares.

Capital Reduction

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

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

Demerger

Demerger is a reorganization tool that is increasingly being employed by companies to segregate their core and non-core businesses.

Demerger involves the transfer of an identified business from one company to another. In consideration, the company, into which the business is spun off, issues shares to the shareholders of the selling company. Demerger is also a court-regulated process which requires sanction by the jurisdictional High Court. The power to approve demergers has recently been shifted from the High Courts to NCLT. However, NCLT is still in the process of being formed.

Slump Sale

Slump sale is another reorganization tool available to corporates. It involves the transfer of identified business from one company to another.

Unlike a demerger, slump sale is not a court-regulated process and can be achieved through a simple shareholders' resolution and legal agreement.

C.3 Taxes on Corporate Income and Gains

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

In the wake of economic reforms, the taxation system has undergone tremendous changes in the past eight to ten years. The tax rates have been rationalized and compare favourably with many other countries. Further, tax laws have also been simplified to ensure better compliance.

Administration

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

Further, the Central Board of Excise and Customs, under the MoF; deals with the tasks of the formulation of policy concerning levy and collection of customs, central excise duties and service tax; prevention of smuggling and administration of matters relating to customs, central excise and narcotics. It is the administrative authority for its subordinate organizations, including custom houses, central excise commissionerates and the Central Revenues Control Laboratory.

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

All corporations having Indian taxable incomes must register with their respective jurisdictional tax authorities. Corporate tax liability is required to be estimated and discharged by way of advance tax in four installments on June 15, September 15, December 15 and March 15 during the tax year beginning on April 1 and ending on March 31. The balance taxes, if any, must be paid on or before the date of filing the returns.

Corporations not adhering to the due date of the filing deadline are not permitted to carry forward their net operating losses/revise their returns. Also in a closely held corporation prior year business losses (excluding unabsorbed depreciation) would not be eligible for carry forward and set off against future income of the company, unless shares of the company carrying at least 51 per cent of the voting power are

beneficially held by the same persons on each of the following dates:

- Last day of the financial year; and
- Last day of the year or years in which the loss was incurred.

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

Penalties are leviable for failure to comply with the following requirements, wherever applicable:

- Applying for tax registration with the revenue authorities.
- Withholding tax at source from prescribed payments.
- Maintaining or retaining books of accounts or records.
- Disclosing the correct income or wealth.
- Having accounts audited from a tax perspective.
- Complying with notices issued by the revenue authorities in India.
- Depositing the taxes withheld at source into the government treasury.
- Furnishing a transfer pricing report.
- Adhering to the mode of acceptance and repayment of certain loans.

Reforms in Indian Taxation

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

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

Some of the significant rationalizations/changes effected in the direct tax policy include the following:

- Rates for the taxation of individuals have been substantially reduced. The maximum marginal rate which was as high as 97.5 per cent spread over eleven tax slabs with an exemption limit of Rs 5,000 in 1974, has been significantly rationalized to 33 per cent (including a surcharge of 10 per cent), spread over three slabs with an exemption limit of Rs 100,000 in 2005-06. The exemption limit will be Rs 135,000 in case of resident women below the age of 65 years at

any time during the financial year and Rs 185,000 in case of resident individuals of the age of 65 years or more at any time during the financial year. Surcharge of 10 per cent of the total tax liability is applicable where the total income exceeds Rs 1 million.

- Similarly, tax rates for the taxation of corporates have also been rationalized. Corporate tax rates for domestic companies have been reduced from 55 per cent in 1991 to 30 per cent for year ending March 31, 2006. Foreign companies, which were taxed at a rate of 65 per cent in 1991, are now taxed at 40 per cent.
- During recent years, a number of tax incentives have been introduced to promote exports, business reorganizations, and the development of infrastructure. These were introduced to facilitate improvement in India's balance of payments position and create new infrastructure to assist fresh capital and foreign enterprise.
- New tax levies have been introduced in the form of FBT and BCTT. FBT of 30 per cent is payable by the employers on the value of fringe benefits provided to employees. FBT has been introduced in India from the income year beginning April 1, 2005. Further, BCTT of 0.1 per cent is introduced on specified cash transactions in excess of Rs 10,000 on any single day entered into by any person with a scheduled bank. The tax has been charged from June 1, 2005 onwards

However, some of the reforms initiated in the early 1990s (such as incentives to specific sectors/activities, etc.), are today being considered inequitable and regressive. In view of this, in the recent past, the government has set up working groups to take a relook at the tax policy and recommend reforms.

The Kelkar Committee Task Force

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

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

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

- Introduction of the Goods and Services Tax Act (GST). The key features are as follows:
 - Tax to be levied on the 'sale' of goods and services.
 - All goods and services to be taxed except those covered under a negative list.
 - All exports to be zero rated.
 - Credits allowed of tax paid on intermediate goods.
 - Three-tier ad valorem rate structure of 6 per cent, 12 per cent and 20 per cent proposed.
 - GST proposed to be extended to immovable property transactions and financial service providers including banks, stock exchanges, etc.
- Introduction of State Goods and Services Tax legislation (SGST)
 - In line with the central GST, a comprehensive SGST legislation proposes to replace various central and state enactments, including existing local and central sales tax legislation, octroi, entry tax, stamp duties, tax on transportation of goods and passengers, electricity tax, telecom license fees based on revenue sharing, etc.
 - SGST proposes to levy the three ad valorem rates of 4 per cent, 8 per cent and 14 per cent in comparison to 6 per cent, 12 per cent and 20 per cent under GST, respectively.
- Customs duty
 - While recognizing the decline in customs rates over the recent years (from a peak basic rate of over 300 per cent in 1990-91 to 20 per cent in 2004-05), TFR has proposed to further reduce the customs duty to 5 per cent (for basic raw materials like coal, ores, etc.), 8 per cent (for intermediate goods) and 10 per cent for finished goods. However, a higher duty has been proposed for motor vehicles and consumer durables.
 - Proposal to eliminate all exemptions except those relating to life-saving goods, goods of security and strategic interest, goods for relief and charitable purposes and international obligations including contracts.

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

Corporate Income Tax

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

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

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

Rates of Corporate tax

Normal Rate

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

Corporates are subject to wealth tax at the rate of 1 per cent, if the net wealth exceeds Rs. 1.5 million.

Special Rates for Non-Resident Corporations

Royalty or Fees from Technical Services. Non-resident corporations are taxed in respect of royalties or fees for technical services earned from India in the following manner:

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

Notes:

- Royalties and fees for technical services earned in pursuance of agreements made after March 31, 2003 that are effectively connected with the foreign

corporation's permanent Indian establishment are taxed at the rate of 40 per cent (exclusive of surcharge and education cess) on a net income basis.

2. Royalties and fees for technical services (not effectively connected with the foreign corporation's Indian permanent establishment) that are not received from the government or where received from Indian corporations under agreements not approved by the government or which are not in accordance with the industrial policy are also taxed at the rate of 40 per cent (exclusive of surcharge and education cess) on a net income basis.

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

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

Dividend Income. Dividend income distributed by domestic corporations is exempt in the hands of the recipients. However, such corporations are required to pay DDT at the rate of 14.025 per cent (including 10 per cent surcharge and 2 per cent education cess thereon) on dividends declared, distributed or paid by them.

Interest on Foreign-Currency Loans. Non-resident corporations earning interest on foreign-currency loans extended to Indian business enterprises or to the government of India are taxed at the rate of 20 per cent on the gross amount of interest.

Overseas Financial Organizations. Specified overseas financial organizations earning income from units of specified mutual funds, purchased in foreign currency, are taxed at the rate of 10 per cent on the gross amount of such income. Long-term capital gains arising on the transfer of such units are also taxed at the rate of 10 per cent. However, if the transaction is liable to securities STT, then no tax is leviable on long-term capital gains, whereas short-term capital gains are subject to taxes at the rate of 10 per cent.

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

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

For a sample corporate tax calculation, see Appendix 7.

Minimum Alternate Tax (MAT)

The Indian tax laws provide for a minimum alternate tax, to be paid by corporations on the basis of profits disclosed in the financial statements. Corporations must pay 7.5 per cent (plus applicable surcharge and 2 per cent education cess thereon) of book profits as tax, if the tax payable as per regular tax provisions is less than 7.5 per cent of its book profits. Book profits for this purpose are computed by making prescribed adjustments to the net profit disclosed by the corporations in their financial statements.

MAT paid by corporations for income years ending on or after March 31, 2001 cannot be carried forward and set off against income tax payable in subsequent years under the normal provisions of the Income Tax Act, 1961. However, MAT paid by corporations for income years beginning on or after April 1, 2005 and MAT paid also for prior years (that is, for income years ending on or before March 31, 2000) may be carried forward for five years and offset against income tax payable under the normal provisions of Income Tax Act, 1961. The maximum amount that can be set off against regular income tax is equal to the difference between the tax payable on the total income as computed under the Income Tax Act and the tax that would have been payable under the MAT provisions for that year.

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

C.4 Corporate Taxes at a Glance

Corporate income tax for domestic companies (per cent)	30 (a)
Dividend distribution tax (per cent)	12.5 (a)
Long term capital gains tax (per cent)	20 (a) (d)(e)
Tax on foreign corporations tax (per cent)	40 (a)
Withholding tax (per cent) (a)	
Dividends	
Paid to domestic companies	0
Paid to foreign companies	0
Interest	
Paid to domestic companies	20
Paid to foreign companies	20 (b)
Royalties from patents, know-how, etc	
Paid to domestic companies	0
Paid to foreign companies	20 / 10
Technical services fees	

Paid to domestic companies	5
Paid to foreign companies	20/10
Branch remittance tax	0
Fringe benefit tax	30 per cent of value of fringe benefits (f)
Net operating losses (years)	
Carry back	0
Carry forward	8(c)
<p>(a) For the income year ending March 31, 2006, the rates listed above for corporate income tax, including capital gains tax, DDT and the withholding taxes are increased by a surcharge equal to 10 per cent of such taxes in case of resident corporations. In case of foreign corporations and branches, income tax, capital gains and the withholding taxes are increased by a surcharge equal to 2.5 per cent of such taxes. In addition, the tax payable by corporations is increased by an education cess, which is imposed at a rate of 2 per cent of the tax payable, inclusive of the surcharge</p> <p>(b) This rate applies only to the interest from foreign currency loans. Other interest is subject to tax at a rate of 41.82 per cent (including 2.5 per cent surcharge and 2 per cent education cess).</p> <p>(c) Unabsorbed depreciation may be carried forward indefinitely to offset taxable profits in subsequent years. Unabsorbed business loss may be carried forward to offset profits of eight subsequent assessment years.</p> <p>(d) Capital gains arising from the sale of assets held for more than three years (one year in the case of some assets such as shares, etc.) are termed as long-term capital gains. Capital gains other than such long-term capital gains are termed as short term capital gains, which are taxed at normal corporate rates.</p> <p>(e) Long-term capital gain arising on the sale of listed securities/units may be taxable at 10 per cent (without indexation benefit). Long-term capital gain arising from the transfer of equity shares or the units of an equity-oriented fund on any recognized stock exchange in India or from the transfer of units of an equity-oriented fund to the mutual fund, will be exempt from tax if STT is payable on such transaction.</p> <p>(f) Fringe benefit tax of 30 per cent (plus education cess and applicable surcharge) on the value of fringe benefits is levied on the employer in respect of the fringe benefits provided/deemed to be provided to the employees during any financial year commencing from April 1, 2005.</p>	

Tax Incentives

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

Profits from New Undertakings

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

Type of Business activities	Quantum of exemption	
	Percentage of Profit	Period
Undertakings engaged in the generation or generation and distribution of power or laying a network of new transmission or distribution lines or carrying out substantial renovation and modernization of the existing transmission or distribution lines (a)(c)	100	10 years
Companies (or Consortium of companies) carrying on the business of developing, or maintaining and operating or developing, operating and maintaining infrastructural facilities (b)	100	10 years
Undertakings which develop, develop and operate or maintain and operate an industrial park or a notified special economic zone on or before March 31,2006 (a)	100	10 years
Undertaking located in areas other than North Eastern region of India, that begins commercial production of mineral oil or refining of mineral oil	100	7 years

Type of Business activities	Quantum of exemption	
	Percentage of Profit	Period
Undertakings engaged in developing and constructing housing projects, approval by local authority before March 31, 2007 and completed within four years from such approval and fulfilment of other prescribed conditions	Entire profit derived from the project	
Undertakings manufacturing or producing any article or thing, not being specified articles or things in specified zones or areas in Sikkim, Himachal Pradesh, Uttaranchal and the North Eastern states (d) (e)	100	10 years
Undertakings manufacturing or producing any specified articles or things or commence any specified operations in Sikkim, Himachal Pradesh, Uttaranchal and the North Eastern states (d) (e)	100	10 years
Undertakings engaged in the integrated business of handling, storing and transporting food grains	100 30	5 years 5 years
Undertakings engaged in collecting and processing or treating of biodegradable waste for generating power; producing bio-fertilizers, bio-pesticides or other biological agents; producing biogas; or making pallets or briquettes for fuel or organic manure	100	5 years
Undertakings engaged in the business of processing, preservation and packaging of fruits and vegetables	100 30	5 years 5 years
Undertakings engaged in operating and maintaining hospitals in rural areas	100	5 years

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

- b) The exemption is available for a period of ten years falling within the period of initial 20 years. However, in the case of ports, airports, inland ports, inland waterways, the exemption may be available for 10 years falling in the period of initial 15 years.
- c) Generation and/or transmission and/or distribution (including by undertaking substantial renovation / modernization) should be before March 31, 2006
- d) Profit derived from substantial expansion undertaken by the existing undertaking or enterprise also eligible for exemption.
- e) 30 per cent for the last five years for Himachal Pradesh and Uttaranchal.

Undertakings established in SEZs

Undertakings established on or after April 1, 2002 but before March 31, 2005

Undertakings established in SEZs on or after April 1, 2002 are entitled to a deduction of 100 per cent for the first five years and 50 per cent for the following two years. For the next three consecutive years, the availability of deduction is contingent upon the credit of the profits to a specified reserve and utilization of such amounts in the prescribed manner. Further, the deduction available is capped at 50 per cent of the profits credited to such reserve.

Undertakings established in SEZs on or after April 1, 2005

Special Economic Zones Act 2005

Proposal to grant 15 year tax holiday to units which begin to manufacture or produce articles or things or provide any services in a SEZ with effect from income year beginning April 1, 2005 has been promulgated and is awaiting notification by the government.

As per the provisions, for the first 5 years, a tax deduction equal to 100 per cent of the profits derived from export of articles or things or prescribed services is available. For the immediately following 5 years, a further deduction to the extent of 50 per cent of profits and gains is available. For the next 5 years, the availability of the deduction is to the extent of 50 per cent of profits and gains subject to the allocation of the profits to a specified reserve and the use of such amounts in the prescribed manner.

The nature of incentive and some of the conditions to be fulfilled for eligibility are summarized below:

Nature of Corporate Tax Incentive

- Profits derived by undertakings setup in SEZs from the export of articles, things or computer software are allowed as a deduction from the computation of taxable income.

- No liability for minimum alternate tax on the profits derived by the undertakings setup in SEZs from exports.
- Undertakings set up in SEZs which provide the ITES also qualify for the incentive.

Conditions for Availing the Tax Incentive

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

Computation of Profits from Export

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

$$= \text{Profits of the business of the undertaking} * \text{export turnover} / \text{total turnover of the business of the undertaking}$$

Amount of Deduction

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

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

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

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

Exemption from Capital gains

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

The above deduction is also available to companies engaged in the cutting and polishing of precious and semi-precious stones.

Various other tax incentives are also available to corporations engaged in the business of convention centres, multiplex theatres, hotels, ships and other undertakings established in notified territories, and/or subject to the satisfaction of the prescribed conditions.

Exemption of rentals on lease of aircraft/aircraft engine

The lease rentals for an aircraft or aircraft engine paid by an Indian company engaged in the operation of aircraft, to a government of a foreign state or a foreign

enterprise, are exempt from income-tax if the agreement was entered into before April 1, 2006. However, the agreement should not have been entered into between April 1, 1997 and March 31, 1999.

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

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

Capital Gains and Losses

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

General Provisions

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

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

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

Gains derived from the transfer of the units of Unit Trust of India, mutual funds, or listed securities are taxed at the rate of 10 per cent, without allowing for indexation adjustments or at the rate of 20 per cent with indexation benefits.

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

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

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

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

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

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

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

In case the asset disposed is the only asset in the block, and a balance remains even after the proceeds are charged to the value of the block, the same may be claimed as a short-term capital loss.

Special Provisions Relating to Capital Gains

Domestic tax law contains a special provision for taxation of capital gains earned by non-residents from the transfer of shares and debentures of an Indian corporation acquired utilizing foreign currency. In computing such capital gains, the cost of acquisition and consideration for transfer are converted into the same foreign currency at specified exchange rates.

Any gain arising (short-term or long-term) is reconverted into Indian rupees at the exchange rate prevailing on the date of transfer to arrive at the taxable capital gains.

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

Amalgamations, Demergers and Slump Sale

Amalgamations. Amalgamations are tax neutral subject to the satisfaction of prescribed conditions. The amalgamated company is permitted to carry forward unabsorbed losses and depreciation of the amalgamating company without obtaining any regulatory approvals, provided the amalgamated company holds at least 75 per cent of the book value of fixed assets of the amalgamating company for five years from the date of amalgamation. Further, the amalgamated company should also continue the business of the amalgamating company for five years and fulfil the other prescribed conditions. Also, the amalgamating company should have been engaged in business in which, losses/depreciation occurred for three or more years and should have held as on date of amalgamation at least 75 per cent of the book value of fixed assets held by it two years prior to the date of amalgamation. The above benefit is available only if the amalgamating company owns a ship, hotel or an industrial undertaking engaged in the manufacture or processing of goods; manufacture of computer software; generation or distribution of electricity, or any other form of power; mining or construction of ships; aircrafts or rail systems; provides telecommunication services, whether basic or cellular, including radio paging, domestic satellite services, network of trunking, broadband network and internet services. The benefit is also available in the case of the amalgamation of the prescribed banking company with specified banks.

The amalgamated company, acquiring an industrial undertaking of the amalgamating company by way of amalgamation, should achieve the level of production of at least 50 per cent of the installed capacity of the said undertaking before the end of four years from the date of amalgamation and continue to maintain the said minimum level of production till the end of five years from the date of amalgamation. 'Installed capacity' for this purpose means the capacity of production existing on the date of amalgamation.

In case of non-compliance with any of the above stated conditions, any brought forward business loss and unabsorbed depreciation which has been set off by the amalgamated company is treated as its income for the year in which the failure to fulfil any of the conditions stated above occurs.

Demergers. Demerger of businesses by existing companies is tax neutral subject to the fulfilment of certain prescribed conditions. The accumulated losses and depreciation of the demerged company attributable to the resulting company will qualify to be carried forward and set off by the resulting company subject to satisfaction of the prescribed conditions.

Capital gains arising in the scheme of amalgamations and demergers are exempt from taxation subject to the fulfilment of certain prescribed conditions.

Slump sale. A 'slump sale' is the transfer of an undertaking or division for a lump sum consideration without assigning values to the individual assets and liabilities. Profits derived from such sales are taxed as long-term capital gains if the transferred undertaking has been held for more than 36 months.

Taxable capital gain arising from a slump sale is the excess of consideration received over the net-worth of the undertaking. The net-worth is the difference between the value of the total assets (the sum of the tax-depreciated value of assets that are depreciable for income tax purposes and the book value of the other assets) and the book value of the liabilities of such an undertaking or division.

Foreign Tax Relief

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

For a list of tax rates prescribed under various treaties, see Appendix 8.

C.5 Determination of Taxable Income

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

Deductions

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

Inventories

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

Provisions

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

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

Redundancy and Retirement Payments

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

Contributions to retirement benefits and other similar welfare funds are deductible

provided the corresponding payments are discharged before filing the ROI or else deduction is allowed in the year of actual payment.

Depreciation and Amortization Allowances

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

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

Tax depreciation rates (declining-balance method):

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

*Subject to fulfillment of certain prescribed conditions, accelerated depreciation equal to 20 per cent of the actual cost is allowed with respect to plant and machinery (other than ships or aircrafts) acquired or installed after March 31, 2005. Subject to fulfillment of certain prescribed conditions, for a new industrial undertaking or a substantial expansion by an existing industrial undertaking, accelerated depreciation equal to 15 per cent of the actual cost is allowed with respect to plant

and machinery (other than ships or aircrafts) acquired or installed after March 31, 2002.

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

Restrictions on Interest Deductions

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

Restriction on Payments to Residents and Non-residents

In order to enforce the tax withholding provisions, certain payments on which tax has not been withheld or deposited as per the law are allowed as deduction in the year in which the taxes withheld are deposited.

Foreign Exchange Losses

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

Relief for Losses

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

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

Dividend Distribution Tax

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

Fringe Benefit Tax

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

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

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

The employer is required to pay the FBT in respect of cost incurred or payment made for fringe benefits provided or deemed to be provided in each quarter at applicable rates on or before 15th of the month following that quarter. However, in case of the last quarter ending on March 31 of the income year, the advance tax shall be payable on or before March 15 of that income year. In addition to the above, the employer is also required to file an FBT return by October 31 of the following year.

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

Banking Cash Transaction Tax

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

Deemed Basis of Taxation

Income derived from providing services, facilities or plant and machinery with respect to prospecting, extraction or production of mineral oil, from the operation of ships or aircrafts, and also from the business of civil construction, etc. in certain turnkey power projects, by non-residents are taxed on a deemed-profit basis. However, in select cases, net basis of taxation can be opted for provided specified books of accounts are maintained for the purpose of audit and other prescribed conditions are satisfied.

Tonnage Tax Scheme

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

Oil and insurance companies have a separate code of taxation.

Related Companies

Transfer Pricing

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

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

TPRs contain definitions of various terms, including 'associated enterprise', 'ALP', 'enterprise', 'international transaction' and 'permanent establishment'. These regulations specify the following methods for determining ALP, which are in line with the guidelines of the Organization for Economic Cooperation and Development:

- Comparable uncontrolled price method.
- Resale price method.
- Cost-plus method.
- Profit-split method.
- Transactional net margin method.
- Any other method that may be prescribed by the CBDT.

The manner in which these methods are to be applied has also been prescribed.

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

Revenue authorities may determine the ALP and make adjustments, if they determine that any of the following conditions exist:

- The prices have not been determined in the prescribed manner.
- The prescribed documents and information have not been maintained.
- The information or data on the basis of which ALP was determined is not reliable or correct.

- Any information or document requested by the tax officer has not been furnished.

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

Controlled Foreign Corporations

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

Consolidated Returns

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

C.6 Other Significant Taxes

Securities Transaction Tax

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

Nature of transaction	Amount of STT
Delivery-based transactions in equity shares or units of an equity-oriented fund	Buyer and seller each to pay 0.075 per cent
Sale of units of an equity-oriented fund to the mutual fund	Seller to pay 0.15 per cent
Non-delivery based transactions in equity shares or units of an equity-oriented fund	Seller to pay 0.15 per cent
Derivatives (futures and options)	Seller to pay 0.01 per cent

Excise duty

Excise duty is a tax applicable to the manufacture of goods within the country. Excise duties are governed by the Central Excise Act, 1944, and the Central Excise Tariff Act, 1985. The term 'manufacture' has been interpreted to mean bringing into existence a new article having a distinct name, character, use and marketability. The definition of manufacture also includes within its ambit the activity of packing, labelling, etc. with respect to certain specified goods.

Most of the products attract a uniform rate of 16 per cent. Further, there is levy of special excise duty/and an additional duty of excise on specified products. National

calamity contingency duty is applicable on certain tobacco and petroleum products. In addition to the above, education cess at the rate of 2 per cent is levied on the aggregate of the duties of excise.

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

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

The Cenvat Credit Rules, 2004 (Credit Rules) allow manufacturers to avail and utilize the credit (cenvat credit) of the service tax (paid on input services used by it in relation to manufacture) for the payment of excise duty. This is in addition to the availment and utilization of credit of the additional customs duty/excise duty for the discharge of excise liability.

The government has also introduced other significant reforms like e-filing of excise returns, extension of export warehousing facilities, etc.

Customs Duty

Customs duty is levied on the import of goods into India. The levy and the rate of customs duty are as per the Customs Act, 1962 (the Customs Act), and the Customs Tariff Act, 1975 (the Tariff Act), respectively. Customs duty on imports comprises the following:

- Basic customs duty
- Additional customs duty
- Education cess

Any or all of the above duties could be reduced/ exempted for specified commodities/class of importers by the central government.

The rates of basic customs duty are specified under the tariff act for each item and vary according to the description of the said goods. A downward trend in customs duty rates has been seen over the past few years. The peak rate of basic customs duty has now been reduced to 15 per cent. Additional duty is equivalent to the excise duty that would have been payable if the goods were manufactured in India.

In addition, an additional levy of 2 per cent in the form of education cess is levied on the aggregate of customs duties on imported goods. Certain specified category of are exempt from this levy in accordance with commitments under the WTO. This

includes exemption to notified IT products covered by ITA from the basic customs duty. An additional duty of customs has however been levied at the rate of 4 per cent on import of IT products in lieu of sales tax which is applicable on domestic sales of such goods.

The primary basis for the valuation of goods under the Indian customs law is the transaction value. The transaction value of the goods is the price actually paid or payable by the buyer to the seller.

The drawback of duties paid on imported goods which are re-exported or on goods which are used in the manufacture of export goods are also available.

The government of India has entered into a number of free trade agreements with trade partners like Thailand, Sri Lanka, SAARC countries and Singapore to promote trade and allow preferential tariff rates for certain identified goods. On the anvil are similar trade agreements with Association of South East Asian Nations and Mercado Comun de Sur (South American Common Market) countries.

Service Tax

Service tax is a tax levied on certain identified taxable services provided in India by specified service providers.

Currently, service tax is levied at the rate of 10.2 per cent (inclusive of 2 per cent education cess). The Finance Act 2005 introduced nine new service categories taking the total service categories liable to service tax to more than eighty.

The value of the taxable services is defined as the gross amount charged by the service provider for the services rendered, excluding certain expenses that are reimbursed on an actual basis, provided the expenses are duly supported by documentary evidence. Further, while determining the value of taxable services, the value of goods and materials sold by the service provider to the recipient of the service are exempt and hence not liable to service tax.

Till recently, service tax was applicable only where the services were provided in India. However, vide an amendment in the provisions under the Finance Act 2005, it has been clarified that where any service is provided by a person located outside India (having a business/ fixed establishment/ permanent address outside India) and is received by a person located in India (having place of business/ fixed establishment/ permanent address in India) then such service shall be deemed to be taxable service in India. In such cases, the service recipient is liable to deposit service tax and the same is available as cenvat credit to the service recipient.

The exemption of service tax in case of foreign exchange receipts has been withdrawn with effect from March 15, 2005. Simultaneously, the government has issued Export of Services Rules, 2005 (the Export Rules) providing that export of services are not liable to service tax. The Export Rules contain guidelines for determining the basis on which a particular service would qualify as 'export'. The

guidelines are based on place of performance of services, location of the service recipient and location of the immovable property with respect to which the services are provided.

The Credit Rules allow a service provider to avail and utilize the credit of additional duty of customs/excise duty (paid on inputs/capital goods used in rendering output services) for the payment of service tax. This is in addition to the availment and utilization of the credit of service tax on input services for the discharge of output service tax liability.

The central government has recently notified rebate notifications providing for grant of rebate (i.e. refund) of the excise duty and service tax paid on inputs/ input services used in providing taxable service which is exported.

Under the rebate scheme, the exporter of taxable services has the following options:

- Charge service tax on the taxable exported service and discharge this liability by utilizing the cenvat credit of duty/ service tax paid on inputs/ input services and the pay the balance amount (i.e. service tax charged less the amount of cenvat utilized) in cash. Thereafter, claim rebate of the total amount paid (through cash and cenvat credit).
- Do not charge service tax on the exported service and claim rebate of the duty/ service tax paid on inputs/ input services. Under this option, the assessee can not avail cenvat credit on inputs/ input services as the same is available as rebate.

Value Added Tax/Sales tax

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

Under the sales tax regime, tax was mostly levied at a single point, generally only on the first sale of goods within the state. Thus, the value added by the intermediaries at subsequent stages of the distribution chain usually remained outside the purview of tax. In respect of manufactured goods, no credit/ set-off was usually available for sales tax paid on inputs and capital goods and hence, there was, in essence, a cascading of tax. The tax rates also varied from state to state.

In view of the above shortcomings, the sales tax regime was replaced by VAT regime in most states, with effect from April 1, 2005.

Interstate sales (where goods move from one state to another) continue to be liable to Central Sales Tax (CST), which is imposed by the central government. The rate of CST is generally 4 per cent when goods are sold for the purpose of use in manufacture or resale, for use in the telecommunication equipment or for generation of power, mining, etc. subject to the provision of the declaration forms prescribed under the CST Act. CST is now proposed to be phased out after introduction of VAT regime in most Indian states from April 1, 2005.

The key features of VAT are as follows:

- VAT is a multi-point tax system and is levied on value added at each stage.
- VAT has replaced existing state sales level taxes like sales tax, works contract tax, lease tax, turnover tax, resale tax, etc.
- The basic rate slabs under VAT are as follows:
 - 0 per cent for natural and unprocessed products and other essential goods;
 - 1 per cent for silver, gold ornaments, etc.;
 - 4 per cent for agricultural and industrial inputs, IT products, capital goods, items of basic necessities, etc.; and
 - 12.5 per cent for other goods.
- Existing sales tax incentives have been continued in different forms, after ensuring that VAT chain is not affected.
- Full input tax credit is available in respect of locally sourced goods and can be set off against output tax liability including CST.
- No credit is available for taxes paid in other states and CST.
- Full input tax credit / refund is available in respect of goods exported outside India.
- For stock transfer/ consignment sale of goods out of state, input tax paid in excess of 4 per cent is eligible for credit.
- Generally, input credit on capital goods is available on staggered basis - over a period of 24 to 36 months.
- Composition scheme is available for dealers having turnover up to Rs 5 million in most states. Under this scheme, tax is payable at a nominal flat rate (usually 1 per cent), without any provision for input tax credits.

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

Octroi/Entry Tax

Octroi/ Entry tax is a levy on the entry of goods into a particular municipal/state jurisdiction for use, consumption or sale within such jurisdiction. Some of the states allow set off of the Entry tax paid with the sales tax payable on the sale of goods. The rate of the above tax on different products may vary from state to state. With introduction of VAT, some of the states have abolished the entry tax legislations. In some states, entry tax paid is available as a setoff against the VAT liability of the importer.

Research and Development Cess

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

The term 'technology' is defined under the above-mentioned legislation to mean any special or technical knowledge or any special service required for any purpose whatsoever by an industrial concern under any foreign collaboration, and includes designs, drawings, publications and deputation of technical personnel.

Other Taxes

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

C.7 Financial Reporting and Auditing

Sources of Generally Accepted Accounting Principles

Companies in India follow fundamental accounting principles and practices. The Accounting Standards Board of the Institute of Chartered Accountants of India (ICAI) issues accounting standards to be followed by enterprises. All accounting standards issued to date are mandatory and companies are required to comply with these standards (the applicability of these standards varies for small and medium size enterprises.) and disclose significant accounting policies in the preparation of their financial statements. ICAI also issues guidance notes and auditing and assurance standards, which are designed primarily to guide auditors on matters that may result during the course of their professional work. ICAI issues expert advisory committee opinions, which suggest the accounting and auditing treatments applicable to specific issues. ICAI also issues Accounting Standard Interpretations which interpret the accounting standards. The government has constituted a National Advisory Committee on Accounting Standards (NACAS) which is empowered to specify the standards which will be applicable to corporates. Till such time NACAS issues accounting standards, the accounting standards issued by ICAI shall deem to be the accounting standards which will be applicable to the corporates.

Statutes/Bodies Governing the Reporting Requirements

The ICAI of India, NACAS, SEBI, the Companies Act, 1956 and the Income tax Act, 1961, primarily govern the financial reporting requirements of companies in India. Further RBI and the IRDA have regulatory powers for banking and financial companies and for insurance companies respectively. In addition, the central government, through special acts and orders, also governs the financial reporting requirements.

Sources of Accounting Standards

Indian accounting standards have been sourced from the International Accounting Standards (IAS), now renamed International Financial Reporting Standards

(IFRS). However, it may be noted that there are several differences between the Indian accounting standards and IAS.

Significant Fundamental Concepts

Accounting Methodology

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

All significant accounting policies should be disclosed in one place in a separate statement or schedule to the financial statements. The effect of any material changes in accounting policies must be quantified and the reasons for such changes explained. If, any material change is not quantifiable, the fact should be stated.

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

Change in Method of Accounting

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

Accounting Principles and Practices

The preface to the statements of accounting standards issued by ICAI states:

The ICAI, being a full-fledged member of the International Federation of Accountants, is expected, inter alia, to actively promote the International Accounting Standards Board's (IASB) pronouncements in the country with a view to facilitate global harmonization of accounting standards. Accordingly, while formulating the accounting standards, the ASB will give due consideration to IASs issued by the International Accounting Standards Committee (predecessor body to IASB) or IFRSs issued by the IASB, as the case may be, and try to integrate them, to the extent possible, in the light of the conditions and practices prevailing in India.

On the above basis, Indian Generally Accepted Accounting Principles (GAAP) has been sourced from IFRS. However, it may be noted that there are a number of significant differences between the Indian GAAP and IFRS.

Funding of Indian Businesses

Share Capital

The Companies Act, 1956 permits companies to issue only the following two kinds of share capitals:

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

The restriction is, however, not applicable to private companies which are not subsidiaries of a public company. These companies are free to issue other kinds of share capital. The nominal value of shares is not prescribed by the Companies Act, 1956 but it is normally Rs 10 per share for equity shares and Rs 100 per share for preference shares. Preference shares issued by a company must be redeemed within twenty years out of retained earnings available for dividends or out of proceeds from the fresh issue of shares made for the purposes of redemption.

The pricing of the new issues of share capital has been substantially freed from the administrative control authority that prevailed earlier. The issue of capital is governed by guidelines issued by SEBI, the body that regulates and oversees the functioning of the Indian stock markets.

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

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

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

Debentures and Borrowings

Companies can raise funds by issuing debentures, bonds and other debt securities. They can also raise funds by accepting deposits from the public. However, the Act strictly forbids debentures from carrying voting rights and prescribes the manner and the source from which deposits can be invited and accepted.

Debentures, especially convertible debentures, have been quite popular with Indian investors, and are one of the most common instruments that have been issued. Debentures can be redeemable or perpetual, bearer or registered and convertible or non-convertible.

Issue of Shares and Debentures

Shares can be issued freely as long as companies comply with SEBI disclosure requirements while issuing a prospectus. The prospectus has to be approved by the stock exchange before it is filed with the registrar of companies. It is also scrutinized by SEBI, which is responsible for regulating the securities market and protecting investors' interests.

Disclosure, Reporting and Filing Requirements

Disclosure Requirements

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

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

The balance sheet and the profit and loss account, should provide all disclosures necessary to give a true and fair view of the company's financial position and the results of operations. The balance sheet should be presented in the standard format detailed in Schedule VI to the Companies Act, 1956. The notes to the financial statements provide additional disclosures concerning the significant accounting policies, contingent liabilities, managerial remuneration, payment to auditors, value of goods imported, details of raw material consumption and the amount of foreign exchange received and expended. The notes to the financial statements should also include quantitative information relating to opening stock, purchases, production, sales and closing stock, as well as the production capacity.

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

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

Directors' Report. The directors' report must accompany each set of financial statements and must include the following information:

- The state of the company's affairs and any change in the nature of its business or its subsidiaries.
- The amount of proposed additions to any reserve account.
- The recommended dividend amount.
- Material conservation efforts (for example, additional investments to reduce energy consumption).
- Technology absorption (that is, details concerning the research and development carried out and the resulting expenses and benefits).
- Foreign exchange received and expended.
- The list of employees, if any, who have received remuneration exceeding Rs 200,000 per month or Rs 2.4 million per annum.

- Directors' responsibility statement indicating that proper accounting standards have been followed in preparing the annual accounts, accounting policies have been applied consistently, a reasonable and prudent basis has been adopted in making judgments and estimates, adequate accounting records have been maintained in accordance with the Companies Act, 1956 and that the financial statements have been prepared on a going concern basis.
- Specify reasons for failure, if any, to complete buy-back within the time specified
- Full information and explanation on every reservation, qualification or adverse remark contained in the auditors' report.

In the respect of listed companies, SEBI requires that as part of the directors' report or as an addition thereto, a separate section on corporate governance be included with a detailed compliance report on corporate governance. Non-compliance with any mandatory requirement with reasons thereof and the extent to which the non-mandatory requirements have been adopted should be specifically highlighted.

Auditors' Report. The auditors' report must include an opinion on the financial statements of the company and must state whether the company and its branches have maintained the books of account as required by law, and whether the books of account agree with the balance sheet and profit and loss account. Further, the auditors are also required to report if any of the directors are disqualified as being appointed as directors under section 274(1)(g) of the Companies Act, 1956.

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

Interim Financial Reporting Requirement of Listed Companies

Quarterly Financial Statements. Each listed company is required to announce unaudited financial results on a quarterly basis, within one month from the end of a quarter, in the specified format and announce the same in the newspapers and subject the results to limited review by the statutory auditors. If in respect of any item given in the same proforma format varies by 20 per cent or more from the respective unaudited quarterly results as determined after the 'limited review' by the Auditors, the company shall send a statement (approved by the board of directors) explaining the reasons to the Stock Exchanges alongwith 'review report'.

In respect of the results of the last quarter of the financial year, if the company intimates in advance the stock exchange that it will publish audited results within a period of three months from the end of the last quarter of the financial year, the company need not publish or furnish to the stock exchange the unaudited results for the last quarter. If the sum total of the first, second, third and fourth quarterly results

with respect to any item given in the format varies by 20 per cent when compared with the audited results for the full year the company shall explain the reasons to the stock exchange. Where the listed companies prepare the un-audited quarterly results, are these required to be approved by the board of directors and subjected to a limited review by the auditors of the company (or by a chartered accountant in the case of PSUs) and a copy of the review report is to be submitted to the stock exchange within two months after the close of the quarter.

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

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

Annual Reporting Requirements

Reporting. Companies in India are required to comply with the various reporting requirements. The requirements are greater for public companies than for private companies. The significant documents that need to be filed are the annual return, balance sheet, profit and loss account and the auditor's and board of directors' reports and charges.

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

At every AGM, the board of directors is required to present the company's financial statements comprising a balance sheet, profit and loss account, cash-flow statements and the auditors' and board of directors' reports to the shareholders.

The formats of the balance sheet and the profit and loss account are prescribed by the Companies Act, 1956 and companies are required to publish annual accounts in those formats.

Dividend Payments. Companies having shares are allowed to pay dividends only out of their profits after providing for depreciation on fixed assets in the manner prescribed by the Companies Act, 1956. However, before the payment of dividends, certain minimum amounts are required to be transferred to the company's reserves. Further, payment of dividends is permitted out of the company's accumulated reserves subject to compliance with certain prescribed rules.

Dividends can be recommended only by the board of directors and require shareholder approval. However, shareholders cannot dictate an increase in the percentage of dividend.

Dividends are declared in percentage terms, i.e. percentage of the face value of the shares and can be declared more than once a year.

Filing Requirements

After the annual financial statements have been presented at the AGM, three certified copies of the same must be filed with the registrar of companies within thirty days of adoption by the shareholders.

Requirement for Different Industries

The government requires certain manufactures to maintain cost accounts and may order an audit by a qualified cost auditor of the same. Banking, electricity and insurance companies are governed by special acts, rather than the Companies Act, 1956.

Audit Requirements

All companies, banks and financial institutions must have their accounts audited by an auditor who is a practicing member of the ICAI. The branch of a company is also required to be audited. Such audit can be conducted by the company's auditor or the branch auditor qualified to be appointed as such by the company.

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

Every company with gross revenues in the excess of Rs 4 million has also to get its accounts audited under the Income Tax Act, 1961. This audit is required to obtain an understanding and confirmation of the specific information required by the revenue authorities for tax assessments. The Companies Act, 1956 also grants the government the powers to order other audits like cost audits and investigations. In addition, every listed company or company with a paid-up capital and reserves exceeding Rs 5 million as at the commencement of the financial year, or average annual sales above Rs 50 million for three consecutive financial years immediately preceding the financial year concerned, is required to have an appropriate internal audit system.

D. Individuals

D.1 Income Tax

Liability for Income Tax

Liability for income tax is governed by the residential status of the individual during the tax year. Residential status is determined by the number of days spent in a tax year in India. Individuals are considered as 'residents', if they meet either of the following criteria:

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

Individuals who do not meet either of the above conditions are considered to be 'non-residents'.

Individuals are considered as 'not ordinarily residents' if they have been non-resident in India in 9 out of preceding 10 tax years or have been in India for an aggregate for 729 days or less in the preceding seven tax years.

Scope of Income liable to tax

Residents are subject to tax on their worldwide income.

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

- Accruing or arising in India;
- Deemed to accrue or arise in India;
- Income received in India; and
- Income received outside India arising from either a business controlled, or a profession established, in India.

Non-residents are taxed on the following income:

- Accruing or arising in India;
- Received in India, and
- Deemed to accrue or arise in India through a business connection, through or from an asset or source of income in India, or through the transfer of a capital asset situated in India (including a share in a company incorporated in India) or from other specified sources.

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

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

Types of Income Subject to Tax in India

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

Employment Income

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

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

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

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

In general, most elements of compensation are taxable in India. Bonus paid at the commencement or completion of employment is included in taxable salary income. Specified allowances are either tax-exempt or included in the taxable income at a lower value, subject to certain conditions.

Also, specified benefits, example company-provided accommodation receive preferential tax treatment, subject to certain conditions. Certain employer-provided benefits are taxed in the following manner in the hands of the employees:

- The benefit of company-provided housing accommodation is taxed at the lower of 20 per cent of the salary or the rent paid, reduced by the amount recovered from the employee. Furniture and appliances provided by the employer are taxed at a rate of 10 per cent of the original cost in case owned by the employer or hire charges paid in case hired by the employer.
- If an employee is provided with hotel accommodation for a period of more than 15 days on transfer, tax is imposed at the lower rate of 24 per cent of salary or actual hotel charges paid by the employer.
- Loans for amounts greater than Rs 20,000 that are interest free or granted at concessional rates to an employee or to a household member of an employee are taxable in the hands of the employee, at prescribed rates depending on the purpose of the loan.

- In general, the amount of tax paid by an employer on behalf of an employee is grossed-up and taxed in the hands of the employee. Effective April 1, 2002, the employer may pay taxes on non-monetary benefits without such taxes being grossed-up in the hands of the employee. However, the employer shall not deduct such taxes paid in computing his taxable income.

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

Taxation of Employer-Provided Stock Options

Special rules apply for the taxation of stock options in India. Taxability of stock income is determined based on whether a plan qualifies as a 'qualified plan' or 'non-qualified plan' as per the Indian income tax law.

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

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

Self-Employment and Business Income

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

Capital Gains and Losses

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

- Sale transaction is entered in to on or after October 1, 2004
- Sale transaction is through a recognized stock exchange or sale of units of equity oriented fund is to the mutual fund.

Short-term capital gains are taxed at normal progressive tax rates applicable in the respective tax year. Short-term capital gain arising on transfer of equity shares or units of an equity-oriented fund on any recognized stock exchange in India or from transfer of the units of an equity-oriented fund to mutual fund on or after October 01, 2004 will be taxable at a lower rate of 10 per cent.

Long-term capital gain is exempt, if such gain or the sale proceeds of the long-term capital asset are invested in certain specified assets (for example, property, specified bonds, etc.), on satisfying certain conditions. If the specified assets are sold within three years after purchase, the capital gains derived from the sale of the original asset are subject to tax in the year in which the specified assets are sold.

While calculating capital gains on the depreciable assets, the sale proceeds of an asset must be applied to reduce the declining-balance value of the class of assets (including additions during the year) to which the asset belongs. If the sales proceeds exceed the declining-balance value of a relevant class of assets, the excess is treated as a short-term capital gain and is taxed as ordinary income.

Short-term and long-term capital losses may not be offset against other income. Short-term capital losses arising during the tax year can be set off against short-term capital gains or long-term capital gains. If the entire loss is not absorbed, then the unabsorbed amount can be carried forward for the subsequent eight tax years in which it could be set off either against short-term or long-term capital gains.

Long-term capital loss arising during the tax year can be set off only against long-term capital gains, and not against any other income. If the entire loss is not absorbed, then the unabsorbed amount can be carried forward for the subsequent eight tax years in which it could be set off only against long-term capital gains.

For NRIs, long-term capital gains arising from the transfer of specified foreign exchange assets, are exempt from taxes if the net consideration for transfer is invested within six months in specified assets or deposited in saving certificates as notified by the central government.

Income from House Property

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

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

Income from other sources

Income which does not specifically fall under any of the above types (i.e. employment income, self employment and business income, capital gains and losses and income from house property) is liable to tax as 'income from other sources'. It includes investment income, winnings from lotteries etc.

Investment Income

Dividends are currently taxed in the following manner:

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

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

For certain categories of income, non-resident Indian nationals (including persons of Indian origin) may exercise an option to be taxed either as per the special provisions or the general provisions applicable to individuals.

Effective September 1, 2004, the definition of income shall include any sum of money received without consideration, meaning a 'gift', from any person.

Income of the nature described above will be taxable under the head 'income from other sources'. However, this would not include sum of money received:-

- From any relative
- On the occasion of the marriage of the individual
- Under a will or by way of inheritance
- In contemplation of death of individual

In addition, a general exemption of Rs 25,000 per year in aggregate has been provided.

Deductions

Effective April 1, 2005, an individual shall be allowed deduction in respect of life insurance premia, deferred annuity, contributions to provident fund, subscription to certain equity shares or debentures etc., but subject to maximum exemption limit of Rs 100,000.

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

Business Deductions

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

Rates

The following tax rates apply to resident and non-resident individual taxpayers for the year ending March 31, 2006.

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

* *The minimum threshold limit in case of resident woman and resident senior citizen is Rs 135,000 and Rs 185,000 respectively, as against any other individual.*

** *If the net taxable income exceeds Rs 1 million, a surcharge is levied at the rate of 10 per cent on the tax payable (See Appendix 9).*

*** *An education cess of 2 per cent is leviable on the income tax and surcharge*

Relief for Losses

Business losses arising to the individual may be set off against income from any other source except for salary income.

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

Tax Filing and Payment Procedures

All taxpayers, including non-residents, must file income tax returns if their taxable income exceeds the amount, which is not subject to tax in a tax year, i.e., Rs 135,000 in case of a woman resident, Rs 185,000 in case of a resident senior citizen and Rs 100,000 in case of any other individual. Residents must file a return regardless of the amount of their income if they meet any one of the following conditions during the preceding year:

- Occupied real property exceeding a specified size.
- Owned or leased a motor vehicle.
- Incurred expense on foreign travel.
- Held a credit card not being an add-on card.
- Held a club membership with an entrance fee of Rs 25,000 or more.
- Incurred an expense of Rs 50,000 or more towards consumption of electricity.

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

Married persons are taxed separately in their individual capacities. If an individual, directly or indirectly, transfers an asset to his/her spouse for an inadequate consideration, income derived from such asset is deemed to be the income of the transferor spouse. If an individual has a substantial interest in a business, remuneration paid by the business to the individual's spouse is taxed to the individual, unless the remuneration is attributable solely to the application of the spouse's technical or professional knowledge and experience. Passive income of minor children is aggregated with the income of the parent with the higher income.

Taxpayers with employment income pay tax by way of the employer withholding taxes from salaries. Individual taxpayers with a tax liability exceeding Rs 5,000 must make advance payments (after taking credit for taxes withheld) in three installments, which are due by September 15, December 15 and March 15.

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

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

D.2 Other Taxes

Wealth Tax

Wealth tax in India is payable at a rate of 1 per cent if the taxable value of the net wealth exceeds Rs 1.5 million. Assets subject to wealth tax include residential houses, cars, yachts, boats, aircraft, urban land, jewellery, bullion, precious metals, cash in excess of Rs 50,000 (in the hands of certain non-corporates), an amount not recorded in the books of the accounts of the company and commercial property not used as business, office or factory premises. However, a residential house and houses owned by an employer and provided to employees earning less than Rs 500,000 a year are not considered as assets for the purpose of computing wealth

tax. The above assets, other than urban land (held for more than ten years), are exempt from tax if they are owned as stock-in-trade or are used for hire. Productive assets, including shares, debentures and bank deposits, are not subject to wealth tax. A deduction is allowed for debts owed that are incurred in relation to the taxable assets. The tax is levied on the net wealth held on March 31 of the relevant tax year.

Wealth tax returns for individuals must be filed by July 31.

Inheritance (or Estate) and Gift Taxes

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

D.3 Social Security

No social security taxes are levied in India.

D.4 Double Tax Relief and Tax Treaties

Taxpayers have the option to choose between the provisions of the tax treaty or the Income Tax Act, whichever is beneficial to them (see Appendix 8).

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

D.5 Temporary Visas

Visitors to India need visas to enter the country unless they are Indian citizens. NRIs holding the citizenship of another country are also required to obtain visas before arriving in India unless they hold a PIO card issued by the Indian government. Visas must be obtained from the Indian embassy or consulate in the applicant's home country. Special permits are required for visiting the Andaman and Nicobar Islands, Bhutan, Lakshadweep, the remote North-Eastern states and Sikkim.

Tourist visas are valid for one to six months, generally beginning on the date the visa was issued and not on the date of entry into India. Tourist visas are generally multiple-entry visas, however, this option must be specifically requested at the time of application.

D.6 Visa and Registration Requirements

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

Nature of visa	Purpose
Employment visa	Persons intending to take up employment
Business visa	Visiting India on business visits
Tourist visa	Visiting India for tourism
Student visa	Pursuing studies/academic courses
Entry visa	Other purposes not covered elsewhere (including accompanying families of foreign nationals)
Long term visa	PIOs who have now obtained foreign nationality
Yoga visa	Persons interested in learning meditation or members of missionary organizations
Research visa	Pursuit of research in any
Transit visa	Travelers passing through the country
Missionary visa	Missionaries of registered charitable trusts
Journalist visa	Media representatives
Conference visa	Event organizers and visitors

Generally, all foreign nationals holding a visa (other than a tourist visa), which is valid for more than 180 days, must register with the Foreign Regional Registration Office (FRRO) within 14 days from the date of arriving in India. However, certain visas specify certain 'specific endorsements' for which registration formalities are to be processed accordingly. The FRRO registration entitles concessional hotels and local air travel. In cities where an FRRO office is not present, expatriates must register with the local police station.

Foreign Exchange Regulations

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

- The amount paid into the foreign bank account may not exceed 75 per cent of the salary. An employee who wishes to receive more than this percentage outside India must file a request with the central bank, i.e. the RBI.

- The remainder of the salary must be paid in rupees in India.
- Indian income tax must be paid on the entire salary amount, regardless of the bank account the salary is paid into.

Foreign nationals receiving salary in India from Indian firms or companies, are allowed to remit their salaries (net of retirement plan contributions and Indian taxes) to their home countries for the maintenance of close relatives or may, alternatively, open an Indian bank account to be repatriated on retirement.

D.7 Residential Permit

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

- Application form;
- Copy of the employment contract, if applicable;
- Letter of application stating the purpose of the expatriate's visit to India;
- An undertaking from the employer confirming to take responsibility of the conduct of the foreigner and agreeing to deport the foreigner in case of any adversities;
- HIV test results, for foreign nationals between 15 and 60 years of age (required in certain cities);
- Ten recent passport-size photos;
- Photocopies of the passport; and
- A copy of the certificate of incorporation/RBI approval of the company where such foreigner has to work.

The original passport and visa are also required at the time of filing the application with FRRO.

Registration is valid for the term of the visa and may be extended on application. Failure to register may result in the immigration authority's refusal to allow the foreign national to leave the country.

D.8 Family and Personal Considerations

Work Visas for Family Members

Entry visas are issued to accompanying family members of individuals visiting India on business or for employment.

Spouses or dependents of working expatriates must obtain separate work permits to be employed in India.

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

Driver's Permit

Foreign nationals are not allowed to drive in India using their home country driver's licenses. They must obtain international driver's licenses in their home countries, which are generally valid for six months.

To obtain an Indian driver's license, individuals must apply to regional transport authority, which issues learner's permits. This enables the individual to drive if accompanied by an adult who has a valid Indian driver's license. One month after the learner's permit is issued; a driving test and verbal examination of the local driving laws must be taken. On successful completion of the examinations, regional transport authority issues a driver's license.

Appendices

Appendix 1: Useful Addresses and Telephone Numbers

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

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

Foreign Investment Promotion
Board

Department of Economic Affairs
Ministry of Finance
North Block
New Delhi 110 001
Telephone: (11) 2309 4905
Facsimile: (11) 2309 3422
Website: www.finmin.nic.in

Software Technology Parks of India

Electronics Niketan
6, CGO Complex, Lodhi Road,
New Delhi 110 003
Telephone: (11) 2436 2811 / 3596
2436 3187 / 3484
Facsimile: (11) 2436 4336 / 3436
Website: www.stpi.soft.net

Regulatory Bodies

Reserve Bank of India	Central Office Shahid Bhagat Singh Marg Mumbai 400 001 Telephone: (22) 2266 1602 Facsimile: (22) 2266 2105 Website: www.rbi.org.in
Insurance Regulatory and Development Authority	3 rd Floor, Parisrama Bhavanam Basheerbagh Hyderabad 500 004 Telephone: (40) 55820964/ 55789768 Facsimile: (40) 5582 3334 Website: www.irdaindia.org
Securities and Exchange Board of India	Mittal Court B Wing 224, Nariman Point Mumbai 400 021 Telephone: (22) 2285 0451 Facsimile: (22) 2285 5585 Website: www.sebi.gov.in
Telecom Regulatory Authority of India	A- 2/14, Safdarjung Enclave New Delhi 110 029 Telephone: (11) 2610 1934 Facsimile: (11) 2610 3294 Website: www.trai.gov.in
Directorate General of Hydrocarbons	Hindustan Times House 4 th and 11 th Floors 18-20, Kasturba Gandhi Marg New Delhi 110 001 Telephone: (11) 2335 2650 / 17 2335 2647 Facsimile: (11) 2331 7081 / 2335 2649 Website: www.dghindia.org
Directorate General of Civil Aviation	Aurobindo Marg, Opposite Safdarjung Airport New Delhi 110 003 Telephone: (11) 2462 2495 Facsimile: (11) 2462 9221 Website: www.dgca.nic.in

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

Key Ministries in the government of India

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

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

Industry Associations

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

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

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

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

Appendix 2: Exchange Rates

The table below provides the RBI reference exchange rates of the Indian Rupee against the four major currencies as on December 30, 2005.

Currency	Exchange Rate
US Dollar	45.07
Euro	53.55
UK Pound	77.89
Japanese Yen (per 100 JPY)	38.44

Source: Reserve Bank of India

Appendix 3: Illustrative list of sectors in which FDI up to 100 per cent is allowed under automatic route

- Most manufacturing activities
- Non-banking financial services
- Drugs and pharmaceuticals
- Food processing
- Electronic hardware
- Software development
- Film industry
- Advertising
- Hospitals
- Private oil refineries
- Pollution control and management
- Exploration and mining of minerals other than diamonds and precious stones
- Management consultancy
- Venture capital funds/companies
- Setting up/development of industrial park/model town/SEZ
- Petroleum products pipeline

Appendix 4: Illustrative list of infrastructure sectors in which FDI up to 100 per cent is allowed under automatic route

- Electricity generation (except atomic energy)
- Electricity transmission
- Electricity distribution
- Mass rapid transport system
- Roads and highways
- Toll roads
- Vehicular bridges
- Ports and harbours
- Hotel and tourism
- Townships, housing, built-up infrastructure and construction development project

Appendix 5: Illustrative list of services sectors in which FDI up to 100 per cent is allowed under automatic route

- Advertising and films
- Computer related services
- Research and development services
- Construction and related engineering services
- Pollution control and management services
- Urban planning and landscape services
- Architectural services
- Health related and social services
- Travel related services
- Road transport services
- Maritime transport services
- Internal waterways transport services

Appendix 6: Actual disinvestment from 1991-92 onwards to 2004-05 and methodologies adopted

Year	No. of transactions in which equity sold	Target receipt (Rs in million)	Actual receipts (Rs in million)	Methodology
1991-92	47	25,000	30,380	Minority shares sold in December 1991 and February 1992 by auction method in bundles of 'very good', 'good' and 'average' companies.
1992-93	29	25,000	19,130	Shares sold separately for each company by auction method.
1993-94	Nil	35,000	Nil	Equity of six companies sold by open auction but proceeds received in 1994-95.
1994-95	17	40,000	48,430	Sale through auction method, in which NRIs and other persons legally permitted to buy, hold or sell equity, allowed to participate.
1995-96	5	70,000	1,690	Equities of four companies auctioned.
1996-97	1	50,000	3,800	GDR (VSNL) in international market.
1997-98	1	48,000	9,100	GDR (MTNL) in international market.
1998-99	5	50,000	53,710	GDR (VSNL) / domestic offerings with the participation of FIIs (CONCOR, GAIL). Cross purchase by three oil sector companies i.e. GAIL, ONGC and IOC.
1999-00	5	100,000	18,600	GDR-GAIL, VSNL-domestic issue, BALCO restructuring, MFIL's strategic sale and others.

2000-01	5	100,000	18,710	Strategic sale of BALCO, LJMC; Takeover - KRL (CRL), CPCL (MRL), BRPL.
2001-02 #	8	120,000	56,320	Strategic sale of CMC 51 per cent, HTL 74 per cent, VSNL 25 per cent, IBP 33.58 per cent, PPL-- 74 per cent, and sale of hotel properties of ITDC & HCI; receipt from surplus cash reserves from STC and MMTC.
2002-03 #	8	120,000	33,480	Strategic sale: HZL (26 per cent), IPCL (25 per cent), HCI, ITDC, Maruti: control premium from renunciation of rights issue, Put Option - MFIL (26 per cent), Shares to employees in HZL, CMC and VSNL.
2003-04	2	145,000	155,470	Strategic sale: Jessop & Co Ltd.- 72 per cent, HZL-18.92 per cent (call option), Public Offer: Maruti (27.5 per cent ICI Ltd. (9.2 per cent IBP (26 per cent), IPCL (28.945 per cent), CMC (26.25 per cent), DCI (20 per cent), GAIL (10. per cent) and ONGC (9.96 per cent)
2004-05	3	40,000	27,650	Offer for sale: NTPC-5.25 per cent, IPCL-5 per cent (to employees) and ONGC-0.01 per cent
Total		968,000	476,470	

Figures (inclusive of control premium, dividend/dividend tax, restructuring and transfer of surplus cash reserves prior to disinvestment)

Appendix 7: Corporate Tax Calculation

The following example illustrates the computation of taxable income and tax liability of a domestic company for the income year April 1, 2005 to March 31, 2006.

Net profit as per financial statement		14,500,000
Less:		
Net dividends received from domestic company (2,000,000) (exempt from tax)	(2,000,000)	
Income from sub-leased property (200,000) (considered separately)	(200,000)	<u>(2,200,000)</u>
		12,300,000
Add:		
Provision for tax	9,000,000	
Depreciation as per financial statements	3,000,000	
Disallowed expenses 200,000 (such expenses not related to the business)	200,000	<u>12,200,000</u>
		24,500,000
Less:		
Tax depreciation		<u>(5,560,000)</u>
Business income		18,940,000
Income from other sources:		
Net income from sub-leased property		<u>200,000</u>
Gross total income		19,140,000
Deduction:		
Taxable income		<u>19,140,000</u>
<i>Calculation of Tax</i>		
Income tax at 30 per cent on Rs 19,140,000		5,742,000
Add:		
Surcharge at 10 per cent		574,200
Education cess at 2 per cent		<u>126,324</u>
Tax payable		6,442,524
Less:		
Advance tax paid during the income year		<u>(5,700,000)</u>
<i>Balance tax payable/refundable with return of income(1)</i>		<u>42,524</u>

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

Appendix 8: Treaty Tax Rates

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

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

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


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

- (a) This rate applies to the interest on monies borrowed, or debts incurred, in foreign currency. Other interest is taxed at a rate of 40 per cent (plus a surcharge of 2.5 per cent and an education cess of 2 per cent).
- (b) A reduced rate of 0 per cent to 10 per cent applies generally to banks and, in a few cases, to financial institutions local authorities, political subdivisions and the government.
- (c) This rate is provided under the Indian income-tax law, being the rate lower than that prescribed under the relevant treaty. This rate is increased by a surcharge of 2.5 per cent and further enhanced by an education cess of 2 per cent for the year ending March 31, 2006. It applies to royalties (not effectively connected to permanent establishment or fixed base in India) paid to foreign corporations under agreements that are approved by the government of India or are in accordance with the industrial policy and that are entered into after May 31, 2005. However, if the royalty paid under agreement entered into after March 31, 2003 which is not approved by the central government or is not in accordance with the industrial policy, the royalties are taxed on a net basis at a rate of 40 per cent (plus a surcharge of 2.5 per cent and an education cess of 2 per cent).
- (d) This rate is provided under the relevant treaty. It applies to royalty not effectively connected to permanent establishment in India.
- (e) A more restrictive scope of definition of royalty may be available under the most favored nation clause in the relevant treaty.
- (f) Most of India's tax treaties also provide for withholding tax rates for technical services fees. In most cases, the rates applicable to royalties also apply to the technical services fees.
- (g) Under the Indian income-tax law, Indian companies must pay dividend distribution tax at a rate of 12.5 per cent (plus a surcharge of 10 per cent and an education cess of 2 per cent) on dividends declared, distributed or paid by them. Such dividends are exempt from tax in the hands of the recipients.

Appendix 9: Individual Income Tax Calculation

The following example illustrates the method of calculating taxable income and income tax liability for an individual for the income year April 1, 2005 to March 31, 2006.

	Rs.	Rs.
<i>Calculation of Taxable Income</i>		
Salary and perquisites		430,000
Income from self-occupied property		0
Less interest paid on construction loan, limited to Rs 150,000		(150,000)
Capital gains (long-term)		30,000
Income from other sources		
Interest income		<u>20,000</u>
Gross total income		330,000
Less allowable deductions:		
Medical insurance, limited to Rs 10,000	(10,000)	
Investments in: - (a)		
• <i>Provident Fund</i>	(20,000)	
• <i>Life Insurance</i>	(10,000)	
• <i>Other Tax Saving Investments</i>	<u>(20,000)</u>	<u>60,000</u>
Taxable income (b)		<u>270,000</u>
<i>Calculation of Tax Liability</i>		
Ordinary taxable income at rates from the personal income tax rate table [(240,000-150,000) x 20 per cent + 5,000] (c)		23,000
Capital gains (long-term of 30,000 x 20 per cent)		<u>6,000</u>
Total tax liability		29,000
Surcharge ¹		0
<i>Education cess at 2 per cent</i>		<u>580</u>
Total tax payable		29,580
Less:		
Taxes withheld on salary and interest	23,460	
Advance tax payment	6,120	<u>(29,580)</u>
Balance due with filing of return		<u>0</u>

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- a) Contributions/investments in the savings plan will be allowed as deduction from gross total income up to Rs. 100,000 effective April 1, 2005.
 - b) Taxable income consists of long-term capital gains (Rs 30,000) and ordinary taxable income (Rs 240,000).
 - c) Effective April 1, 2005 in case of a resident woman and resident senior citizen², the minimum taxable income threshold is Rs 135,000 and Rs 185,000 respectively, as against Rs 100,000 for any other individual.

¹ Surcharge is levied @10% on income tax where taxable income exceeds Rs 1 million.

² Senior citizen means an individual who is 65 years or more at any time during the previous year.

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