India

Legal overview

Executive Summary

The Foreign Direct Investment (FDI) policy has been dramatically liberalised since the evolution of economic reforms in India.

FDI up to 100 percent is allowed under the automatic route in most sectors/activities. However, for FDI in activities not covered under the automatic route, prior government approval is required to be obtained.

Company incorporation in India has been simplified, as all filings are completed electronically, making the process more economical and smoother.

Registered Companies and Partnerships

A foreign body corporate can use the following corporate structures to enter the Indian market:

- Incorporating a wholly owned subsidiary or through a joint venture;
- Incorporating a Limited Liability Partnership; or
- Setting up a liaison office/project office/branch office.

A company that is incorporated in India is deemed as a resident of India for taxation purposes.

A foreign company is deemed as a resident of India for taxation purposes if its 'Place of Effective Management' is in India in a given financial year.

Some business trade as partnerships. Following the introduction into Indian law of Limited Liability Partnerships (LLPs) as a legal entity, traditional partnerships are, however, becoming less popular because of the unlimited liability, and therefore significant potential exposure, of the individual partners.

LLPs enjoy various tax advantages such as lower tax rates, no dividend distribution tax or wealth tax, hence, it is more economical in comparison to a company.

Classification of Registered Companies

In India, companies are incorporated under the following three broad categories:

Companies limited by shares can be either private or public companies. The majority of companies registered in India are private companies limited by shares.

Companies limited by a guarantee. These companies are normally incorporated for non-profit making functions, with no share capital and members rather than shareholders. The members contribute a predetermined amount towards the assets of the company in the event of the company being wound up. Examples of companies which fall under this category are trade associations and co-operative societies for promoting social objects.

Companies with unlimited liability which may or may not have share capital. These companies are not very popular nor prevalent since the shareholders/members have unlimited liability in the event of the company being wound up.

Memorandum and article of association

The memorandum of association and the articles of association form the constitutional documents of a company.

The memorandum of association forms the foundation on which a company's structure is built. It defines the scope of a company's activities and provides basic details about the initial subscribers of the company.

The articles of association form the by-laws and rules which in turn define the rights, duties and powers of the management of a company, the form in which the business of the company is to be carried on and how the shareholders can exert their control over the board of directors.

There are statutorily prescribed formats for the memorandum and the articles of association, however, companies can amend them according to their business requirements.

Share Capital

Share Capital is categorised into authorised and paid-up/subscribed share capital.

The paid-up share capital of a company refers to the contribution invested by the shareholders from time to time. The subscribed share capital determines the liability of the shareholders towards the company.

Public offer of Shares

A public offer is the offer of shares of a company to the general public and can be initiated through an Initial Public Offer. A public company can offer to sell its shares in the primary market by listing its shares on recognised stock exchanges, such as the Bombay Stock Exchange (BSE) or the National Stock Exchange (NSE). The listing of shares helps to enhance the company's value in the long term, however, the company must comply with detailed listing regulations if it wishes to publicly list its shares.

Overall, listing is an expensive and extensive process, which involves many complex legal rules and procedures that must be followed in order to sustain in the public share market.

General Meetings

There are various decisions relating to a company that require the assent of the shareholders, particularly matters which directly concern the interests of the shareholders. Therefore, it is necessary to hold a general meeting/shareholders meeting to approve such decisions.

Each financial year, every company is required to hold an annual general meeting (AGM) in order for financial statements to be approved by the shareholders. The quorum of a valid AGM varies depending on whether the company is public or private.

In addition to the AGM, the board of directors may, whenever it deems necessary, call an extraordinary general meeting (EGM), so that the members of the company can approve specific matters. However, over the past few years, private companies have been exempted from obtaining shareholders' approval in an EGM, for certain decisions and these can be approved in a board meeting.

Directors

A public company must have a minimum of three directors and a private company must have a minimum of two directors.

Each director owes a fiduciary duty towards the company. Fiduciary duties are established under law and in the articles of association of each company.

In India, foreign residents can also become directors of a company. However, the company must have at least one director who, during a given financial year, has been staying in India for a total period of not less than 182 days.

Financing of a company

There are different ways to finance a company which are as follows:

- Investment in the share capital by shareholders or preferred investors;
- Issuing debentures;
- Unsecured loans from directors and their relatives;
- Inter-corporate deposits;
- Bank finance; and/or
- Grants from the government in case of NPOs and start-up companies.

Before availing any financial facility a company should, however, ensure that it complies with the applicable laws.

Directors may be required to give personal guarantees, in order for the company to take loans from banks and financial institutions. In these cases, the advantage of limited liability is negated.

Commencement of Business

In India, before a company may commence its business, it needs to fulfil various statutory requirements, such as obtaining a Certificate for Commencement of Business from Registrar of Companies along with other relevant licenses for operating its business, applying for tax registrations and opening a corporate bank account.

To make the process smoother, tax registrations are issued along with the Certificate of Incorporation. It takes a maximum of 7 days

to register a company in India.

For an overseas company to commence its business in India, the entire process of attaining operational status in the market takes around 4 to 8 weeks.

Mergers and acquisitions

Over the last few years, merger procedures have been simplified and the courts are no longer involved to approve mergers, as all mergers are now approved by the Central Government. Fast track mergers have been introduced for mergers of two or more small companies and mergers of subsidiaries with their holding company. Companies, other than small companies and wholly owned subsidiaries, must follow a slightly more extensive process.

Private limited companies are usually sold or acquired through private negotiations. Share-purchases are where one entity acquires the shares of another. Sometimes it is preferable to purchase the business of another entity, leaving liabilities with the target corporate entity and this is referred to as an 'asset-purchase'. The sale of shares in a private company are usually conducted confidentially with a small number of interested parties on a preferential basis.

In contrast, takeovers of public listed companies in India are strictly governed by the Takeover Code.

Corporate Insolvency

Recently, the law in relation to insolvency and bankruptcy has undergone a huge remodeling, to make it creditor friendly and a time bound process.

If a company becomes insolvent, the procedures include liquidation of the business, administration or restructuring by a qualified insolvency resolution professional.

Upon commencement of the corporate insolvency proceedings, the company is given breathing space called a moratorium, during which no alienation of assets or initiation of proceedings or any enforcement action may be initiated against the company. Following the moratorium period, the company may be wound-up.

During the process of insolvency resolution, each director's conduct is reviewed. If it is found that the business of the com-

pany has been conducted with the intent of defrauding its creditors or for any other fraudulent purpose, then persons, including directors who were knowingly party to such business, may be directed to make such personal contributions to the assets of the company, as the concerned authority deems fit. Moreover, parties may face imprisonment in cases of non-cooperation, submission of false information and/or the concealment of facts by the officers/managers of the company during the resolution process.

Hence, it is advisable that a director demonstrates that he took diligence of the affairs of the company and took decisions that were intended to minimise the losses or damages to the creditors of the company during the 'twilight period' (the preceding 12 months, however, this is extendable up to 2 years).

Winding up of companies

Although the winding up of a company or liquidation may be the most effective way to recover debts, it is only trigged after the exhaustion of all other remedies available under the law. Therefore, these procedures are considered as a last resort.

There are two types of liquidation, either compulsory liquidation by order of tribunal in cases where a company has defaulted in payment of its debts, or a voluntary liquidation by resolution of the company. Recent changes in India's law have made the process of voluntary winding up and compulsory winding up more streamlined.

Liquidation or winding up in cases of default in payment of its debts may be initiated by a creditor. This involves the appointment of a qualified insolvency resolution professional, who takes up management of the company. They provide the best possible resolution plan for the company under liquidation.

Voluntary liquidation by the company requires the members as well as creditors, if any, of the company who represent two-thirds in value of the debt, to approve the resolution to wind up the company.

The appointed qualified insolvency resolution professional shall endeavor to complete the liquidation process within 12 months.

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Tax overview

Accountancy

Company/Firm registration

Every new business, whatever its legal form, must register with the Related Governing Body. Companies or Limited Liability Partnerships (LLPs) are required to register with the Registrar of Companies (pursuant to provisions of the Companies Act 2013). Partnerships are required to register pursuant to the Partnership Act 1932

Setting-up Costs

The statutory cost of registering a company/LLP can start from two thousand Indian rupees. The cost depends upon various factors such as the authorised share capital and the state in which the registered office is located. There are no statutory registration costs in terms of taxation (PAN, TAN & GST) for a company/LLP except in case of partnerships where a nominal fee payable.

National current benefit taxation

Direct Tax:

Income tax for Body Corporates:

Taxable profits of both companies and branches carrying out business in India are subject to a corporate income tax rate of 25% if the turnover or gross receipt doesn't exceed Rs.50 Cr. otherwise the corporate income tax rate is 30%. The corporate income tax rate on foreign companies is 40%. Education cess and SHEC is charged at 4% over and above tax. A surcharge is also applicable and this may vary from 3% to 10%, depending upon the taxable income.

Income tax for Individuals:

Every Individual is liable to pay income tax (on income accrued or received in India). Individuals with an income up to Rs.2,50,000 is not liable to tax. The income tax on any income above Rs.2,50,000 is 5%. For an income of Rs. 10,00,000 the tax rate is 20% and for an income of above Rs.10,00,000 the income tax rate is 30%. A surcharge is also applicable for incomes which exceed Rs.50,00,000.

Indirect Tax:

Goods & Services Tax:

On 1 July 2017, India successfully implemented the "Goods & Services Tax". This has altered the entire indirect taxation system. GST was implemented to reduce the occurrence of double taxation. GST includes several indirect taxes, such as central excise duty, service tax and VAT.

Tax rates on various services and products range from 0% to 28%. For organisations where the turnover exceeds the amount prescribed, GST registration is mandatory. If an organisation is operating in different states of India, it is required to have GST registration in every particular state.

Value Added Tax (VAT):

Alcohol for human consumption, petrol and petroleum products and natural gas are do not fall under the scope of goods and service tax. However, VAT is still applicable on some specific products.

Securities Transaction Tax (STT):

STT is an indirect tax, which is levied at the time of sale and purchase of securities through the Indian Stock Exchanges. These securities include shares, mutual funds and F&O transactions.

Stamp Duty:

Stamp Duty is an Indirect Tax levied by the State Government on the transfer of immovable property located in their state. It is also levied by the government on all legal documents. The Stamp Duty Tax may vary from state to state.

Treaties for the avoidance of double taxation

India has a wide range of double tax treaties. The double taxation treaty cover almost all the industrialised countries and a number of others. The rates negotiated for withholding tax rates are often lower than other countries manage to obtain.

Benefit distribution (National withholding taxes)

India charges a dividend distribution tax on profit distributions by resident companies. The dividend distribution tax rate is 20.36%

(including surcharge and cess). A distribution of dividends by an Indian company to a shareholder is exempt from taxation in the hands of Shareholder.

Tax treatment of losses

Pursuant to the Income Tax Act 1961, losses may be carried forward for eight years, subject to certain conditions. Restrictions apply to losses that are classified as business losses. These business losses can be set-off against business profits of future years and are also subject to other conditions.

Furthermore, in the event of a major change of the ultimate shareholder, losses that have been incurred before the moment of the change cannot be offset against future profits unless certain conditions are met.

Employer obligations (salary taxes, social security)

In general, an employer is obliged to pay professional tax to the tax authorities (in specific states of India). In relation to payment of salary and wages, various laws must be complied with such as the Payment of Wages Act, the Payment of Bonus Act and the Payment of Gratuity Act. Organisations are also required to register itself under Employee Provident Fund Organization pursuant to the Employees' Provident Funds and Miscellaneous Provisions Act. Registration under Employees' State Insurance Corporation is also required.

In cases of Employee State Insurance and Provident Fund, both employer and employee contribute a specific percentage of an employee's salary and an employer must deposit the same within a specified time. Companies are also liable to comply with Corporate Social Responsibility pursuant to the Companies Act.

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