Grant Thornton
An instinct for growth™

A guide to establishing presence in India

2017

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Foreword

Prime Minister Narendra Modi won a landslide mandate in May 2014 - a single party government was formed for the first time in 30 years - on the promise of making India great just like he had previously transformed his home state, Gujarat.

With GDP growth of 7.1 per cent and FDI inflow of USD 60 bn in 2016-17, India is both, the fastest growing economy and the largest recipient of FDI, globally.

Over the last few years, the government has delivered landmark structural reforms which are expected to further propel this growth. This list includes Goods and Services Tax (GST) which integrates India into a single market and removes a spate of complex indirect taxes; a competition amongst India's 29 states to improve their 'Ease of Doing Business'; the 'India stack', which leverages the new biometric identification (Aadhaar) and mobile penetration of a billion plus Indians for digital financial transactions; and a sudden withdrawal of all high denomination currency notes along with strengthened legislation and enforcement to tackle corruption and unaccounted money.

The period between 31 March 2015 and 2017 saw a number of reforms coming together within the ambit of financial regulations in the country. The Indian equivalent of 'SOX' documentation and auditor attestation of controls (ICFR), Indian IFRS (Ind AS), and mandatory rotation of external auditors are some of the key reforms that will align India's practices to the best in the world.

There has never been a time in history where so much has happened in India. At Grant Thornton India LLP, we are delighted to be at the forefront of helping shape a more vibrant India working with the government, the leaders of India Inc., and global companies that want to maximise this amazing opportunity.

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Introduction

This is an interesting time for the Indian economy. Rated as one of the most stable economies, India continues to shine amidst global gloom. Led by the Modi government, a number of economic, financial and institutional reforms including the reforms leading to ease of doing business across states have been implemented. Strict monetary action taken by the government to bring back unaccounted money into the system paves the way for economic growth backed with digitisation. Banking regulations including the recent move to replace high value currency notes with new higher denominations has the potential to make the economy more robust and compliant. The government has also notified the final regulations related to the insolvency resolution process under the Insolvency and Bankruptcy Code 2016. The law aims to improve the ease of doing business in India by facilitating smoother and time-bound settlement of insolvency and faster turnaround of businesses, apart from creating a database of serial defaulters.

Among reforms, initiatives such as Make in India campaign, improving the ease of doing business in India and Startup India, Standup India will further pave the way for growth. Additionally, government's Digital India and opening of bank accounts for masses via the spread of Jan Dhan Yojna has been a welcome change.

The government has started several development schemes, which, in the longer run will make the country stronger and more stable. In addition to this, the property market, which was largely considered fragmented and unorganised, was regulated by the enactment of the Real Estate Regulation Act (popularly known as RERA). All the states had to implement the rules under the Act by 1 May 2017 to make the regulation a reality across the country. This has been supplemented by insolvency and bankruptcy laws, amendment in the Benami Transactions Act, arbitration and conciliation laws, and corporate governance laws.

While the country is now working towards the development of 100 smart cities, spreading financial inclusion to all will strengthen the hands of a large section of the population.

However, the biggest move by the government is its enactment of a legislation to introduce a national value-added tax (named Goods and Services Tax) with effect from July 2017, replacing the current multitude of central, state and local levies. The GST regime will create a much more integrated and productive economy in the longer run.

After two quarters, Indian economy is set to shine. The Economic Survey 2016-17 brought out by the Government of India in February 2017 expects economic growth to rebound from 6.75 per cent in 2016-17 to 7.5 per cent in 2017-18.

The International Monetary Fund (IMF) also expects India's GDP to grow more than 7 per cent this year, making India the world's fastest-growing large economy. Amidst slowing global growth, India remains a bright spot among emerging economies. The forecast by IMF factors in the wave of reforms that the country is witnessing. As corroborated by the World Economic Forum's (WEF) Global Competitiveness Index for 2016-17, India's ranking has improved 16 places to 39 on account of improving business environment and innovation. Following the centre's move, states too are eyeing significant share of foreign investments demonstrating both cooperative federalism and competitive federalism. All of this truly is poised to unlock the potential for growth in India and build a more vibrant economy, and we at Grant Thornton in India are all set to growing together with India. We hope this guide will support your growth plans of either setting up base or expand in India. We look forward to being your growth advisers in the land of emerging opportunities.

This guide is intended to serve as a primer for companies planning to enter the Indian market to tap significant opportunities in various sectors. It aims to provide business information on the country's legal, accounting and taxation framework.

Country profile

India has emerged as a key investment destination globally. The U.S. Department of Commerce has identified India as one of the world's top 10 'big emerging markets'.

According to the World Investment Report 2017 published by the UNCTAD, India continues to be among the top ten countries in terms of FDI inflows globally and the fourth in developing Asian region.

India's FDI inflows have increased to USD 44 bn in 2015 as compared to USD 35 bn in 2014, and the growth has been across the board, the report added. Globally, FDI activity has increased by 38 per cent, in a signal that a revival in investment sentiments is on the cards. The FDI inflows in 2016-17 were in excess of USD 60 bn, a new all-time high surpassing the inflows of USD 55.6 bn in 2015-16.

Summary

Outlined below are key facts and statistics that make India a favourable business destination worldwide:

- A growing middle class
- An abundant supply of raw material
- An extensive rail and road network
- World's largest working population in the age group of 25-45 years
- Large pool of skilled English speaking manpower
- Lower labour cost and hence, reduced cost of manufacturing especially in comparison to non-Asian countries
- Geographical location, which makes India closer to markets including Middle East, South Asia and Europe

Main ports of entry:
Chennai, Jawahar Lal Nehru, Kandla, Kochi, Mormugao, Kolkata, Mumbai, Paradip, Tuticorin, Ennore, Vishakhapatnam and New Mangalore1

Major international airports:
Chennai, New Delhi, Mumbai, Hyderabad, Kolkata, Bangalore, Goa and Thiruvananthapuram

Geographical location

India forms a natural subcontinent with the Himalayan mountain range to the North, and the Indian Ocean, the Arabian Sea and the Bay of Bengal to the South, West and East, respectively. The country is bordered by Pakistan on the northwest, China, Bhutan and Nepal on the northeast, and Bangladesh and Myanmar on the East. Near the country's southern tip, across the Palk Strait, lies Sri Lanka.

India has a land frontier of over 15,000 kilometres, stretching from the Himalayas in the north to the Palk Straits in the south, and from the Arabian Sea in the West to the Bay of Bengal in the East. It has a long coastline spanning over 7,000 kilometres. The climate varies from tropical in the south to temperate in the north.

Population and standard of living

India is the second most populated country in the world with a population of 1.324 bn (World Bank, 2016 estimates). According to the 2011 population census, there are 35 cities in India with a population of more than a million, with Mumbai, Delhi and Kolkata having population over 10 million. Around 70 per cent of the country's population resides in rural and semi-rural areas. One of the main reasons that India is considered as an attractive, high-growth market is its large pool of untapped and upper middle class population. Also, the standard of living in metropolitan cities of the country is comparable to the best in other developing nations.

As per estimates, 250 mn people are set to join India's workforce by 2030. With a significant chunk of population shifting into the working age group, there is a corresponding increase in disposable income and consumption demand. In fact, it is estimated that India will have 247,800 new millionaires by 2025

Diversity

India is rich in history, culture, religion and diversity. There are 22 officially recognised languages spoken in India across its 29 states and 7 union territories. India is secular through its constitution with people from all faiths residing here including Hindus, Muslims, Sikhs, Christians, Buddhists and Jains.

Sources:
World Bank, indexmundi.com, Ministry of commerce and industry, PIB, India

1 Ministry of Shipping: http://shipping.gov.in/writereaddata/l892s/27963559-Perspectiveplans.pdf

Education

The education system in India is considered as one of the best globally. The system comprises public and private schools, universities and other institutions for higher learning (MBA, PhD, MSc, etc.) These institutions are committed to impart excellent academic and vocational training, and encourage participation in sports and other extra-curricular activities. The current literacy rate in India stands at 74.04 per cent. The country offers quality education comparable to global standards in fields including finance, consulting, literature, computer engineering & programming, science & technology, medicine, dentistry and business management and administration. The Indian Institutes of Technology (IITs) and Indian Institutes of Management (IIMs) are recognised world-over as premier higher educational institutions.

Currency

The Indian Rupee (INR) is the official currency of the Republic of India. The Reserve Bank of India (RBI) is the national and sole currency issuing authority in the country. The exchange rate of the rupee is mainly market determined. The RBI takes a keen interest in the financial markets of the country and other countries globally to determine suitable monetary, regulatory and other measures. The current RBI reference rate for INR/1 USD is 64.07 (28 August 2017).*

Key economic statistics

India's economic policies are designed to attract significant capital inflows in the country on a sustained basis, and encourage technological collaboration with foreign firms. Policy initiatives taken over the past few years have resulted in significant inflow of foreign investment in all areas of the economy, except the public sector.

India is a Union of States with a parliamentary system of government Statistics (2016)

Population	1.324 bn (2016)
Area	3.29 mn square kilometres
GDP (current)	USD 2.264 trillion
GDP – per capita	USD 1,709.39
Exports	USD 22115.03 mn
Imports	USD 31955.94 mn
Literacy rate	74.04% (Census 2011)
Life expectancy	68.35 years
Urban population	33%
Local currency	Indian Rupee (INR)

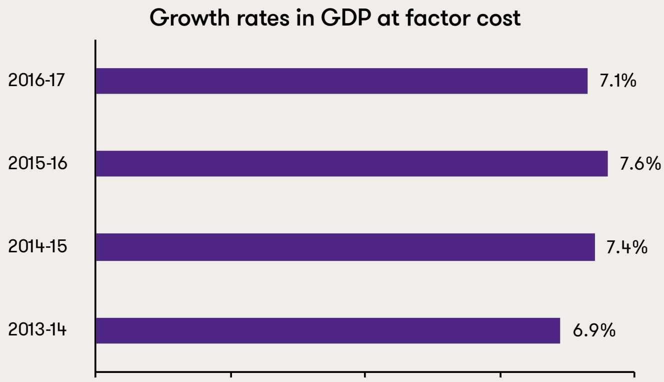
Key economic indicators of India

GDP and key fiscal indicators

- At a rate 7.1 per cent, India has been one of the fastest growing large economy globally in 2016-17. The growth has been supported by the contribution of key sectors including agriculture, manufacturing and financial services. However, faltering private investment, weak capital goods growth and lower exports were a concern. The GDP grew by 7.4 per cent and 7.6 per cent in 2014-15 and 2015-16, respectively
- During 2015-16, the fiscal deficit of the country stood at USD 81.2958 bn, which is equivalent to 3.5 per cent of the country's GDP. In 2014-15, the corresponding figure was USD 80.0321 bn (Revenue Estimate), which is equivalent to 4.1 per cent of the country's GDP
- Revenue deficit stood at 2.8 per cent of GDP for FY 2015-16

7.1%

GDP growth in 2016-17



Source: CSO

External factor and per capita national income

- Exports from India jumped year-on-year to USD 24.5 bn in February of 2017, the biggest gain since October 2011. This was primarily on account of the firming up of the rupee against slowing global economy.
- In comparison to the previous fiscal year, the country's exports jumped by 17.5 per cent.
- India is the third largest economy in the world in terms of purchasing power parity (Source: International Monetary Fund).
- Imports to India increased to USD 33.4 bn in February 2017, the biggest gain since November 2014, registering a surge of 21.8 per cent.
- According to First Advance Estimates provided by the CSO, in real terms (at 2011-12 prices) during 2016-17, the per capita income is likely to attain a level of INR 81,805 as compared to INR 77,435 for the year 2015-16. The growth rate in per capita income is estimated at 5.6 per cent during 2016-17, as against 6.2 per cent in the previous year.

21.8%

increase in imports in 2017

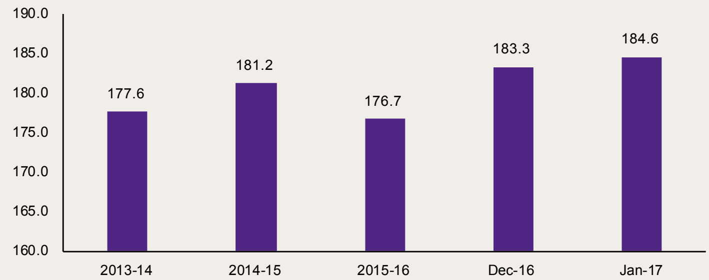
Money and credit

- As recorded in January 2017, the gross bank credit for FY 2016-2017 stood at INR 67113 bn (USD 1,047.5 bn) (Source: RBI)
- The gross fixed capital formation averaged USD 74.7 bn during the period 2001-2016. In the fourth quarter of 2016, it has reached INR 87.98 bn (USD 1.4 bn) (Source: Ministry of Statistics and Programme Implementation)
- India's current account deficit stood at 0.6 per cent of the GDP in the third quarter of the year 2016 as compared to 1.7 per cent of the GDP in the same period a year ago. (Source: RBI)
- External Debt in India increased to USD 484300 mn in the third quarter of the year 2016 from USD 479658 mn in the second quarter of the year 2016. The rise was due to increase in long term borrowings and global slowdown. (Source: RBI)
- India's foreign reserves touched USD 364.11 bn in second week of March 2017. However, towards the end of February 2017, the foreign currency assets (FCAs), which form a majority of the country's foreign exchange reserves, dropped by USD 59.1 mn to USD 339.72 bn. Gold reserves however, remained unchanged. (Source: RBI)
- India became the ninth largest (according to World Investment Report, 2017) recipient of FDI in 2016 in the world, grossing USD 55.46 bn following a series of reforms by the government, as compared to USD 44 bn in 2015 (Source: World Investment Report 2016 by the United Nations Conference for Trade and Development)
- PM Modi's demonetisation drive continues to push electronic transactions. Going forward, this will also spur the growth of fintech companies.

9th

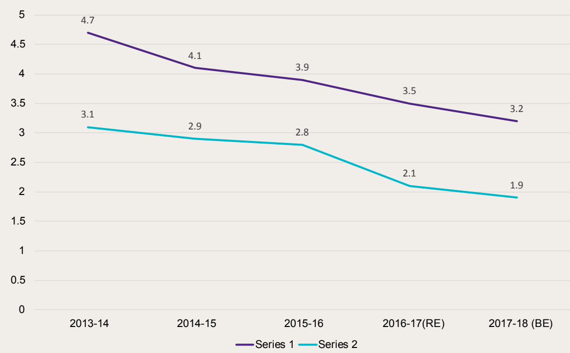
largest recipient of FDI in 2016 globally

Wholesale Price Index: Base Year 2004-2005



Source: Office of the Economic Advisor, Government of India; Department Of Industrial Policy & Promotion (DIPP)

Key fiscal indicators (per cent of GDP)



Key sectors: An overview

Manufacturing and Automotive

Government's 'Make in India' campaign has put manufacturing at the forefront. The sector encompasses a number of sub-sectors such as metals and mining, industrial manufacturing, chemicals, engineering, telecom and automotive, among others. It is expected that Manufacturing will contribute significantly to the country's growth in the coming decade.

India is the seventh largest producer of automobiles in the world and the fourth largest market by volume. The sector contributes 7.1 per cent to the GDP and employs 19 mn people. Around 31 per cent of small cars sold globally are manufactured in India. India is the world's largest motorcycle manufacturer. The two-wheelers segment contributes 81 per cent market share and leads the market on account of huge domestic demand from the youth and the middle class buyer. Thus automotive sector and its manufacturing remains a strong sector of growth for the country.

India is also a prominent auto exporter and fifth largest manufacturer of commercial vehicles and the second largest manufacturer of two-wheelers worldwide. The expanding economic activity has started to have an impact on the commercial vehicle segment. It is expected to register a double digit growth in the next one year. Some of the key foreign players are Suzuki, Honda, Nissan, Piaggio, Volkswagen, Renault, Hyundai, General Motors, BMW, Ford and Toyota.

Healthcare

The overall Indian healthcare market is worth around USD 100 bn and is expected to grow to USD 280 bn by 2020, at a CAGR of 22.9 per cent. Healthcare delivery, which includes hospitals, nursing homes and diagnostics centres, and pharmaceuticals, constitutes 65 per cent of the overall market. The Healthcare Information Technology (IT) market which is valued at USD 1 bn currently is expected to grow 1.5 times by 2020.

The Indian medical tourism industry, currently pegged at USD 3 bn per annum, with tourist arrivals estimated at 230,000, is expected to reach USD 6 bn by 2018, with the number of medical tourists set to double over the next four years. The hospital and diagnostic centres attracted FDI worth USD 3.59 bn between April 2000 and March 2016, according to data released by the DIPP. India's universal health plan that aims to offer guaranteed benefits to a sixth of the world's population will cost an estimated Rs 1.6 tn (USD 23.72 bn) over the next four years.

The Indian pharmaceutical industry is estimated to be USD 30 bn, growing by a CAGR of 16.5 per cent during the last five years (FY 2011-16). India continues to be among the largest producers and exporters of generic drug formulations in the world, accounting for around 20 per cent of total global generic drug exports. However, exports, particularly to regulated markets, have been affected on account of the continual USFDA alerts on Indian manufacturing standards and facilities and US alone accounts for about 40 per cent of India's drug exports. Pricing control being extended to include more and more essential drugs, are also discouraging multinational companies from introducing patented drugs in India. However, efforts are being taken to promote local manufacturing and reducing dependence on imports of API from China through the new bulk drug policy to be initiated, and the strong Make in India push in the sector.

The Medical Technology sector in India valued at USD 6.3 bn in 2013 at end consumer prices and is growing at 10-12 per cent per year. Currently the Indian medical devices industry represents just over 1.3 per cent of the global medical device market. The Indian medical devices industry consists of small and medium companies primarily focusing their R&D efforts and manufacturing capabilities for affordable medical devices such as disposables and medical suppliers – which come under low priced, high volume market segments. Requirement of high end medical equipment – nearly 75 per cent, are met by imports. The country's Make In India initiative is being implemented through a 'policy push' to encourage local manufacturing and shift from an import dependent to an export oriented market. The industry eagerly awaits the implementation of the Draft Medical Devices bill 2016, a long outstanding initiative which attempts to carve out the Medical Technology sector from Pharma.

Technology, Media and Entertainment

India is the world's largest sourcing destination for the IT industry, accounting for approximately 67 per cent of the USD 124-130 bn market. The industry has a workforce of about 10 mn. More importantly, the industry has led the economic transformation of the country and altered the perception of India in the global economy. The IT industry has also created significant demand in the Indian education sector, especially for engineering and computer science.

The Indian IT and ITeS industry is divided into four major segments – IT services, Business Process Management (BPM), software products and engineering services, and hardware. The Indian IT sector is expected to grow at a rate of 12-14 per cent for FY2016-17 in constant currency terms. The sector is also expected to triple its current annual revenue to reach USD 350 bn by FY 2025.

The Indian Media and Entertainment (M&E) industry is a sunrise sector for the economy and is making high growth strides. This sector is expected to grow at a Compound Annual Growth Rate (CAGR) of 14.3 per cent to touch INR 2.26 tn (USD 33.7 bn) by 2020, while revenues from advertising is expected to grow at 15.9 per cent to INR 994 bn (USD 15.5 bn). India is one of the highest spending and fastest growing advertising markets globally. The country's expenditure on advertising is expected to grow more than 12 per cent in 2016, and accelerate to 13.9 per cent in 2017, on the back of popular sporting events like T20 Cricket World Cup, the Indian Premier League (IPL) and the media blitz on State elections. Television segment, which continues to hold highest share of spending, is expected to grow by 12.5 per cent in 2017, led by increased spending by packaged consumer goods brands and e-commerce companies.

The Government of India has supported Media and Entertainment industry's growth through various initiatives such as digitising the cable distribution sector to attract greater institutional funding, increasing FDI limit from 74 per cent to 100 per cent in cable and DTH satellite platforms, and granting industry status to the film industry for easy access to institutional finance. Also, the Government launched the Digital India programme to provide several government services to the people using IT and to integrate the government departments and the people of India. The adoption of key technologies across sectors spurred by the 'Digital India Initiative' could help boost India's Gross Domestic Product (GDP) by USD 550 bn to USD 1 trillion by 2025. In India, government's Digital India, Make in India initiatives dominated the Indian IT industry in 2015 that also boosted the start-up revolution in the country.

Consumer products

The Indian retail and consumer industry is broadly segregated into urban and rural markets, attracting players from across the world. The sector has grown at an annual rate of 5.7 per cent between 2005 and 2015. Annual growth in the Indian consumption market is estimated to be 6.7 per cent during 2015 to 2020 and 7.1 per cent during 2021 to 2025. The maximum consumer spending is likely to occur in food, housing, consumer durables, and transport and communication sectors. India will be an interesting arena in the next few years for global retailers. With new large format malls providing anchor space to many international fashion retailers, the consumer will benefit with a plethora of choices. Further, the current and expected real estate correction along with economic reforms such as GST and infrastructure development schemes will also offer the brands an added incentive to stay invested in India.

The Government of India has allowed 100 per cent FDI under the automatic route in online retail of goods and services through the marketplace model, thereby providing clarity on the existing businesses of e-commerce companies operating in India. Many state governments, corporate and educational organisations are working towards providing training and education to create a skilled workforce of 500 million people by 2022. Union Cabinet reforms like implementation of the Goods and Services Tax (GST) and Seventh Pay Commission are expected to give a boost to consumer durable sector in India during FY 2017-18.

Real estate and construction

Housing is one the basic needs of the population. The sector not only employs the second most number of people directly and indirectly in the country but also supports around 250 ancillary industries. The sector contributes more than 6 per cent to the country's GDP. However, there is a huge demand-supply gap in the housing segment with a projected need of around 18 mn affordable housing units and over the years the sector has remained largely un-organised, which has significantly impacted the perception of the sector. Within last couple of years, Government has initiated various reforms - 'Housing for all by 2022' scheme, creation of 100 smart cities, relaxations in FDI norms to attract investments & REITs regime. Apart from this, government has finally been able to enact RERA and award infrastructure status to affordable housing segment.

The plethora of these reforms not only have the ability to change the landscape of the sector in terms of bringing in much needed transparency and accountability, but also attract significant amount of investments for the sector – both overseas & domestic.

Financial Services

Last year's demonetisation drive by the Indian Government, which aims to drive the country towards a cashless economy, is reflective of the rapidly changing scenario in the country. This, along with many more policy changes and reforms provides financial services a firm standing. While there are concerns related to high levels of non-performing assets (NPAs) with banks and other financial institutions, there is a silver lining. RBI, along with the government, has taken a number of initiatives for enhancing the accessibility and financial inclusion of all in the country. Bank account penetration in India increased from 35 per cent in 2011 to 53 per cent in 2014. With initiatives such as Jan Dhan Yojana, the number of unbanked population without any bank accounts in India has come down to around 233 mn by the end of 2015, reflecting a drop of 58 per cent over the last four years. As recorded in 2015, India has had a total of 1,440 mn deposit bank accounts and 1,170 mn saving bank accounts in 2015. The country also has around 144 mn of borrower accounts. With rising levels of digitisation and technology adoption, financial services is expected to deepen its penetration and reach in the country. Consequently, the Indian Banking industry has the potential to become fifth largest by the end of FY 2020 and third largest by the end of FY 2025.The Banking and Financial Industry is expected to recruit around 8.4 mn, and the sector is expected to be among the top employment creators in 2016.

Political and legal system

Introduction

India is the largest democracy in the world. It is estimated that the country, today, has more than 200 political parties. One feature of the political parties in India is the dominant role played by their leaders. There are both national and regional parties, one of which is the Indian National Congress (INC) that has been led mainly by the Nehru-Gandhi family since the independence of the country. To compete on a national level, many political parties form alliances. The two main alliances in the country are National Democratic Alliance (NDA) - a coalition led by the Bharatiya Janata Party (BJP), and United Progressive Alliance (UPA), a coalition led by the INC.

Structure of the government

India is the largest multi-party democracy in the world. It is a sovereign socialist secular democratic republic with a parliamentary system of government, and a constitution. The Constitution of India provides for a parliamentary form of government which, although has certain unitary features, is federal in structure. The council of the Parliament of the Union consists of two legislative houses - the Rajya Sabha (Upper House), which represents the states of the Indian federation, and the Lok Sabha (Lower House), which represents the people of India as a whole. At present, the country is a Union of 29 states and seven Union Territories (UTs). Each state is governed by a government comprising elected representatives of the public.

The Central and State governments comprise a council of ministers headed by a Prime Minister and a Chief Minister, respectively. The head of the state is the President of India, while the head of the government is the Prime Minister. The Prime Minister and the Chief Minister are usually the heads of the political parties that are elected by the people. They have support of all the majority members in the Parliament. Elections for the State, Centre and UTs are held after every five years.

New Delhi is the national capital of India. The seat of the Central government is New Delhi. All the other State governments have primary responsibility for matters such as law and order, education, health and agriculture. Currently, Mr. Narendra Modi is the Prime Minister of India. India is a member of major international organisations including South Asian Association for Regional Cooperation (SAARC), Brazil, Russia, India, China and South Africa (BRICS), and the Commonwealth of Nations, among others.

Judiciary and law

India has a well-established, independent judicial system. The Supreme Court of India is based in New Delhi. In each state, there is a High Court in its capital city. The States also have several district courts.

India derives most of its judicial framework from the English legal system. The main goal of the Indian law is to protect the promotion of business entities, provide a healthy industrial and social environment and ensure robust labour protection. Till 1991, many trade barriers were in place so as to promote the local industry, but since 1991 many barriers were lifted to promote the influx of foreign investors in the country.

Source: Grant Thornton Deal Tracker

Foreign investment

Introduction

Foreign investors keen to set up operations in India are required to comply, inter alia, with the foreign exchange control laws of the country, particularly the consolidated FDI Policy, issued by the Government of India from time to time. Accordingly, the Companies Act 2013, Foreign Exchange Management Act, 1999 (FEMA) and the Regulations thereunder govern the setting-up of incorporated entities (joint ventures or wholly-owned subsidiaries) and of unincorporated entities (branch, liaison or project offices).

Foreign direct investment policy

In recognition of the important role played by FDI in accelerating the economic growth of the country, the government initiated a slew of economic and financial reforms in 1991. India is now ushering in the second generation reforms aimed at furthering the integration of the Indian economy with the global economy.

FDI is freely allowed in some sectors, in the country, including the services sector. FDI is permitted, subject to certain specified conditions. On the other hand, in a few sectors, the existing and notified sectoral policy does not permit FDI beyond a ceiling.

For certain class of items/activities, FDI can be brought in through the 'automatic route' without seeking any prior approval from the central government or from the central bank of India i.e. the Reserve Bank of India. For the remaining items/activities, FDI can be brought in after obtaining an approval from the government. The approving authority used to be the FIPB which used to function under the Ministry of Finance. The government has abolished FIPB with effect from May 2017. New proposals for FDI under approval route are now directly handled by the concerned ministries. Towards this end, the DIPP has issued the 'Standard Operating Procedures' (SOP) for processing FDI proposals. This SOP clearly lays down the procedure to submit the online application through the FIPB portal (now known as the Foreign Investment Facilitation Portal).

The table below gives an indicative summary of the sectoral FDI policy:

FDI Policy Parameter	Sectors
Automatic route	FDI up to 100 per cent permitted under automatic route in most services, manufacturing, infrastructure sector and services, B2B trading
Approval route	FDI in these activities is permitted only with prior government approval e.g. non-operating holding companies, broadcasting content services (FM Radio), print media (newspaper and periodicals), private security agencies, satellite services, FDI beyond 49 per cent in defence and beyond 74 per cent in existing pharma companies
Sectoral caps	FDI in these sectors is subject to sectoral caps such as insurance (49 per cent), defence industry subject to industrial license (49 per cent), broadcasting content services – FM radio/news & current affairs TV channels (49 per cent), multi brand retail trading (51 per cent), airlines (49 per cent)
FDI linked conditions	FDI in these sectors is subject to specified conditions – floriculture, horticulture, apiculture and cultivation of vegetables & mushrooms under controlled conditions, wholesale trading, single brand retail trading, e-commerce, construction development – townships, housing and built up infrastructure, print media, asset reconstruction companies

FDI is not permitted in the following sectors:

- Lottery business including government/ private lottery, online lotteries, etc.
- Gambling and betting including casinos, etc.
- Agriculture (excluding plantations - tea/coffee/rubber/ cardamom/palm oil tree/olive oil tree)
- Activities/sectors not open to private sector investment e.g. atomic energy and railways (except mass rapid transport systems)
- Business of chit fund
- Nidhi company
- Trading in transferable development rights (TDRs)
- Real estate business, or construction of farmhouses (subject to certain exceptions)
- Manufacturing of cigars, cheroots, cigarillos and cigarettes, tobacco or tobacco substitutes

Foreign technology collaboration in any form including licensing for franchise, trademark, brand name and management contract is also prohibited for lottery business, gambling and betting activities.

To make India an attractive destination for foreign investors, the FDI policy allows repatriation of all profits, dividends, royalty, and know-how payments, freely.

Exchange controls

FEMA replaced the Foreign Exchange Regulation Act, 1973 to facilitate external trade and payments, and to promote orderly development and maintenance of the foreign exchange market in India.

As per the current foreign exchange control regulations, transactions are divided into current account and capital account transactions. Capital account transaction refers to such a transaction which alters the assets or liabilities, including contingent liabilities, outside India, of a person resident in India; or assets or liabilities in India of a person resident outside India. Thus, investment by a body corporate or an entity in India and investment therein by a person resident outside India are capital account transactions.

Current account transactions, on the other hand, are transactions other than capital account transaction. Such transactions comprise, for instance, payments due in connection with foreign trade, other current business services, and short-term banking and credit facilities, in the ordinary course of business. Broadly speaking, current account transactions are permitted, unless specifically barred, and capital account transactions are prohibited, unless specifically permitted.

Capital instruments

FEMA, read with relevant regulations governing FDI provide, inter alia, that Indian companies can issue equity shares, fully and mandatorily convertible debentures, fully and mandatorily convertible preference shares and warrants, subject to the pricing guidelines/valuation norms and reporting requirements, to foreign investors subject to certain prescribed requirements. The FDI policy allows optionality clauses in equity shares and compulsorily and mandatorily convertible preference shares/ debentures issued to non-resident investors under the FDI Scheme subject to certain conditions. The policy provides that shares with call/put options may be issued to non-resident investors provided the non-resident investor is not guaranteed any assured exit price at the time of making the investment.

General permission is also available for issuing shares/ preference shares against lump sum technical know-how fee, royalty due for payment, subject to entry route, sectoral cap and pricing guidelines, and compliance with applicable tax laws. Last year, the government also allowed companies to issue equity shares against any other funds payable by the investee company (subject to bonafides being satisfied regarding legitimacy of dues), remittance of which does not require prior permission of the government or RBI under FEMA or any rules/regulations framed or directions issued thereunder.

Foreign Currency Loans

In terms of the FEMA and the relevant regulations governing External Commercial Borrowings (ECBs), Indian companies operating in certain specific sectors are permitted to avail ECB from certain categories of non-resident lenders with a specified minimum average maturity period for specified end users, under the general permission or specific permission route as applicable. Importantly, optionally convertible and redeemable instruments like redeemable preference shares, optionally convertible shares and debentures, also need to comply with the ECB regulations.

At present there is a three track system under which Indian corporates can avail ECBs from overseas. The following table depicts the key parameters under the three tracks:

Parameter	Track I (short-medium term foreign currency ECB)	Track II (long-term foreign currency ECB)	Track III (INR denominated)
Minimum average maturity	Minimum average maturity of 3/5 years.	Minimum average maturity of 10 years.	Indian Rupee (INR) denominated ECB with minimum average maturity of 3/5 years.
Recognised lenders	International banks, international capital markets, foreign equity holders, long term lenders, suppliers of equipment etc.	Same as Track I except overseas branches/subsidiaries of Indian banks.	Same as Track II
Permitted end uses	Capital expenditures such as import of capital goods, local sourcing of capital goods, new projects, expansion or modernisation	All purposes excluding real estate activities, investment in capital markets, on lending, purchase of land, etc.	Same as Track II
Eligible borrowers	Manufacturing companies, software development sector, infrastructure sector, SEZ units, core investment companies, holding companies, infra-related NBFCs, etc.	Track I entities, Real Estate Investment Trusts and Infrastructure Investment Trusts	Track II entities and all NBFCs, companies engaged in miscellaneous services such as research and development, training and logistics services and not for profit entities

Import/export controls

Over the years, Indian trade policy has undergone fundamental shifts to correct the previous anti-import bias, through the withdrawal of quantitative restrictions, reduction and rationalisation of tariffs, liberalisation in the trade and payments regime, improvement in access to export incentives, and establishment of a realistic and market-based exchange rate.

Export and import of goods and services from India is allowed under FEMA, read with the Foreign Exchange Management (Current Account) Rules as amended from time to time. The said Export and Import Regulations stipulate, guidelines pertaining to settlement and payment of export and import transactions, realisation of proceeds, advance receipts and payments written off and limits permissible for the same.

The Export Regulations also set out the obligations for Indian exporters of goods such as submission of certain prescribed declarations along with supporting documents. While no forms are prescribed for export of services nevertheless the export proceeds are required to be realised within a stipulated time period (currently nine months).

Similarly, the import regulations provide the manner and documents required to be followed by persons, firms and companies for making payments towards imports into India. Further, the said regulations provide the timelines within which remittances against imports should be completed or an approval be sought from the AD/Reserve Bank of India prior to the expiration of the due date.

Overseas direct investment

Indian Parties (company incorporated in India or a body created under an Act of Parliament or a partnership firm registered under the Indian Partnership Act 1932 or a Limited Liability Partnership (LLP) incorporated under the LLP Act, 2008) are eligible to undertake 'overseas direct investment' outside India signifying a long-term interest in the foreign entity (joint venture or wholly owned subsidiary).

An Indian Party can make overseas direct investment under the automatic route in any bonafide activity up to the prescribed limit of its net worth (currently 400 per cent of net worth). It may be noted that real estate and banking business are the prohibited sectors for overseas direct investment. Overseas investment in financial services sector is subject to specified conditions including a satisfactory track record of the investing party, and with prior approval of the concerned financial regulator in India.

The regulations also prescribe provisions with respect to aspects such as issuance of guarantee, ongoing compliance and reporting requirements and conditions for disinvestment.

Finance

Introduction

Financial sector in India is intrinsically strong, operationally sundry and exhibits competence and flexibility besides being sensitive to India's economic aims of developing a market oriented, industrious and viable economy. The sector can be broadly classified into two categories:

The organised sector: Comprises private, public and foreign owned commercial and cooperative banks, which are known as scheduled banks and insurance sector.

The conventional sector: Comprises individual or family-owned money lenders and non-banking financial companies (NBFCs).

The force of liberalisation has transformed the structure of financial industry. There have been significant banking reforms in the country since the liberalisation of the economy. These reforms have attracted foreign players in the banking and financial sector.

The RBI policy rates heavily influence the Indian Financial Services. The current RBI rates as on August 28, 2017 are Bank rate: 6.25 per cent; Repo rate: 6.25 per cent; Reverse Repo rate: 5.75 per cent. The reserve ratios are CRR: 4 per cent and SLR: 20 per cent.

Indian financial services sector:

Indian financial sector has the following broad categories:

Sr. No.	Categories
1	Commercial and Retail Banks
2	White Label Automated Teller Machine (WLA)
3	Payment banks/ wallets
4	Non-banking financial companies (NBFC)
5	Housing finance companies (HFC)
6	Microfinance institutions (MFIs)
7	Insurance companies
8	Capital markets
9	Pension funds
10	Mutual funds
11	Private equity and Venture Capital (VC) funds
12	Asset reconstruction companies (ARCs)
13	Real estate investment trusts (REITs) / Infrastructure investment trust (InVIT) fund
14	Angel or start-up fund

The banking sector is dominated by scheduled commercial banks. Commercial banks deal in all types of commercial banking businesses including cash management system, automated teller machines (ATMs), credit cards, term and working capital loans, housing and consumer finance and purchase and sale of foreign currencies. Many financial institutions are becoming dynamic and entering new domains within banking such as home loans finance, car finance, retail banking, etc. and have separate departments for offering investment and structuring services.

Recently, in an endeavour to promote a cashless economy, the government announced demonetisation of existing currency notes through RBI. The demonetisation process is expected to have a positive impact on the Indian economy, channelising idle money through legitimate banking channels. Hence, growing deposits in the banks may result in lowering the interest rates, further dropping the lending rates as well. This would further help in promoting retail activities in the economy.

White label automated teller machine (WLA)

ATM's set-up, owned and operated by non-bank entities are called WLAs. They provide banking services to the customers of banks in India, based on the cards (debit/credit/prepaid) issued by banks. The Union Cabinet has approved 100 per cent FDI under the automatic route for non-bank entities that operate WLA, subject to certain conditions as prescribed.

Payment banks/ wallets

Payments banks are a new model of banks conceptualised by the RBI for financial inclusion by providing (i) small savings accounts and (ii) payments/remittance services to migrant labour workforce, low income households, small businesses, other unorganised sector entities and other users. It has reached customers mainly through the mobile phones rather than conventional banks. Payments banks are governed by the final guidelines released by the RBI for payment banks on November 27, 2015.

Airtel has launched India's first live payments bank. Further, with payment banks using technology-mobile phones and biometric system (Aadhar Card enabled bank accounts), the use of currency circulation in these areas too will decrease drastically.

Non-banking financial companies (NBFC)

NBFCs, are financial institutions that provide certain types of banking services, however, does not hold a full banking license. NBFCs under their permissibility criterias are permitted to offer substitute to the banking services such as loans, credit facilities, etc. rather generally engaged in non-fund based activities that keep them outside the scope of traditional oversight required under banking regulations.

NBFC sector in India has undergone a significant transformation over the past few years, with NBFC loans expanding 16.6 per cent in the year, twice as fast as the 8.8 per cent credit growth across the banking sector on an aggregate level.

Housing finance companies (HFC)

The mandate of the RBI is to promote housing finance institutions to improve/strengthen the credit delivery network for housing finance in the country. HFCs are expected to regulate the housing finance system of the country to prevent the affairs of any housing finance institution being conducted in a manner detrimental to the interest of the depositors or in a manner prejudicial to the interest of the housing finance institutions.

The biggest highlight of the government was to bring housing loans of up to INR 5 mn under affordable housing, INR 2.8 mn in urban and INR 2.5 mn in other centres under priority sector lending. The decision of the RBI to increase loan to value (LTV) ratio to 90 per cent for loans up to INR 3 mn or less was another positive step to enable HFCs to lend more to low-and moderate-income (LMI) group.

Microfinance institutions (MFIs)

The Prime Minister of India has launched the Micro Unit Development and Refinance Agency (MUDRA) to fund and promote MFIs, which would in turn provide loans to small and vulnerable sections of the business community. MFIs are the pivotal overseas organisations in each country that make individual microcredit loans directly to villagers, micro entrepreneurs, impoverished women and poor families. As a dedicated credit delivery channel for vast unbanked/under-banked segments, NBFC-MFIs have been playing a significant role in taking forward the financial inclusion agenda of the Government of India.

Insurance companies

The Insurance Regulatory and Development Authority of India (IRDA), as part of its endeavour to increase insurance sector growth, has allowed a new distribution avenue called the 'point of sale' person, who will be allowed to sell simple standardised insurance products in the non-life and health insurance segments, which are largely pre-underwritten. The relaxation in the FDI limit to 49 per cent in the insurance sector and permission for offshore reinsurance to enter the Indian markets would assist India become the largest insurance market in the world. Over five reinsurance licences have been granted in India to promote the reinsurance business activities.

The gross market size of India's insurance sector is projected to touch USD 350-400 bn by 2020, with the Indian insurance industry planning to increase the penetration level in the market from the current 3.9 per cent to 5 per cent by 2020.

Capital markets

The Indian capital market comprises equity, debt, foreign exchange, derivative markets and futures markets in commodities. Further, in a potential move to encourage foreign investment into the debt markets, the RBI released draft circular on 16 May 2016 proposing to expand the basket of permissible instruments for foreign portfolio investors ('FPI') to include unlisted debt securities as well.

According to the DIPP, the total FDI investments India received in FY 2016-17 was USD 60.08 bn. FPIs net investments stood at USD 8.58 bn in March 2017, the main growth driver for FPIs being the equity market.

Pension funds

Pension Funds are created by an employer to make contributions of funds set aside for a worker's future benefit. The passage of the Pension Fund Regulatory and Development Authority (PFRDA) Act 2013, investment corpus in India's pension sector is expected to cross USD 1 trillion by 2025. Foreign investment in the pension sector is permitted up to 49 per cent.

Mutual funds

Mutual funds are popular in India, because they offer the ability to easily invest in increasingly complicated financial markets. A large part of the success of mutual funds is also the advantages they offer in terms of diversification, professional management and liquidity.

After the tightening of regulation, and with rising incomes, India now has several fund houses with record Assets Under Management (AUM) of over INR 13,000 bn at last count, and several lakh unit holders.

Other sources of finance

Private equity and venture capital (VC) funds

In India, VC is regulated by SEBI. A venture capital may be set up by a company or a trust after a certificate of registration is granted by SEBI. A VC can raise money from any Indian or non-resident Indian (NRI). Recently, SEBI proposed to enhance the investment limit for venture capital funds (VCFs) from 10 per cent to 25 per cent in offshore venture capital undertakings with an Indian connection.

Over the last few years, India has emerged as the third largest base for start-ups in the world, after the US and the UK. One of the most common ways a startup raises money for its seed capital and further funding is by venture capital. Alternative Investment Funds (AIF) refers to any privately pooled investment that may be from Indian or foreign sources known as 'private placement'.

In 2015, the RBI notified regulation which allowed foreign investment and simplified the procedure for investment in AIFs. This move has been applauded by the AIF industry, which is relatively new in India. With a fresh inflow of foreign investment, there will be accelerated growth in domestic AIFs, which yield better returns to investors as well as better investments for new and emerging businesses, social ventures and infrastructure.

Asset Reconstruction Companies (ARCs)

ARCs have been created to bring about a system for recovering Non Performing Assets (NPAs) from the books of secured lenders and unlocking the value of NPAs. 100 per cent FDI is allowed in ARCs under automatic route to help tackle the issue of declining asset quality of banks.

REITs/InVIT fund

REIT or InVIT is an alternate fund raising mechanism offered to capital intensive industries for companies that own income-producing real estate or infrastructure. As such, the unit holders of a REIT / InVIT earn a share of the income produced through real estate investment, without actually having to go out and buy or finance property. SEBI relaxed rules for REIT and InVIT by allowing them to invest more in under-construction projects, rationalised unit holder consent on related party transactions and removed restrictions on special purpose vehicle (SPV) to invest in other SPVs holding the assets.

Angel or Start-up Fund

Angel investors are experienced entrepreneurs who have been through the same phase and understand what it takes to create a big company from an idea. There are around 280 investors that are a part of this network . The main sectors that prominently involve angel investment are e-commerce, information technology, healthcare, agriculture and the mobile segment of the telecommunications sector.

Business entities

Introduction

A foreign company has the following business entity options through which it can establish its presence in India:

Unincorporated entities	• Liaison office • Branch office • Project office • Partnership firm
Incorporated entities	• Limited Liability Partnership firm (LLP) • Limited company (Public/ Private)

These forms of business entities are discussed in detail as follows:

Liaison office

A foreign company (a body corporate incorporated outside India, including a firm or other association of individuals) may establish its liaison office (LO) in India by making an application to the Authorised Dealer Bank (AD Bank) if the principal business of the entity resident outside India falls under sectors where 100 per cent FDI is permitted in terms of the FDI policy. In certain cases, the application is to be made to the RBI and processed in consultation with the government for instance where the applicant is an NGO, applicant is from certain specified countries and setting up the LO in specified states in India etc.

An LO is suitable for a foreign company, which wishes to set up a representative office as a first step to explore and understand the business and investment climate in the country. This office serves as a communication channel between the parent company overseas and its present/prospective customers in India. The LO can also be set up to establish business contacts or gather market intelligence to promote the products or services of the overseas parent company. The LO cannot undertake any business activity or earn any income in India.

Branch office

A foreign company may establish its branch office (BO) in India by making an application to their AD Bank in most cases. The BO should be engaged in the activity in which the parent entity is engaged and permissible activities for a BO include export/import of goods, rendering professional or consultancy services, undertaking research work, promoting technical or financial collaborations, representing the parent company in India and acting as buying/selling agent in India, rendering information technology services and rendering technical support.

The BO is not permitted to undertake any manufacturing activity in the country except where the BO is set-up in a special economic zone.

Project office

A foreign company may open a project office in India without prior approval from the RBI, provided it has secured a contract from an Indian company to execute a project in India and met the prescribed conditions. Once the project execution is completed, as per the terms of the contracts awarded, the project office would have to be closed down.

Partnership firms

Under the current FDI policy and the Foreign Exchange Management Law, foreign investment into Indian partnership firms (other than by non-resident Indians or persons of Indian origin) requires prior permission from the RBI. A partnership is an association of two or more persons to carry on as co-owners of a business for profit. Each partner of a partnership has unlimited liability.

Limited Liability Partnerships

A limited liability partnership (LLP) is a hybrid between partnership firm and company. It is a separate legal entity, liable to the full extent of its assets, with the liability of the partners being limited to their agreed contribution in the LLP. Foreign investment into a LLP is permitted under automatic route (without requiring prior approval) in those sectors in which 100 per cent FDI is allowed. However, it should be noted that LLPs are not permitted to raise ECBs.

An LLP is governed as per the LLP agreement between the partners and in the absence of such agreement the LLP would be governed by the framework provided in the Limited Liability Partnership Act, 2008. This Act describes the matters relating to mutual rights and duties of partners of the LLP and of the limited liability partnership and its partners. Importantly, the Act makes it mandatory to have two designated individual partners, at least one of whom should be residing in India.

Any existing private company or existing unlisted public company can be converted into LLP by complying with the relevant provisions of LLP Act, 2008. Tax neutrality conditions have been stipulated for such conversion.

Limited company

A limited company is an incorporated entity, which is a separate legal entity distinct from its members/ shareholders. As mentioned above, foreign investment in India is governed by the FDI policy of the government as well as the Foreign Exchange Management Law. As per the current policy, all companies in India have to be incorporated under the provisions of the Companies Act, 2013.

With effect from May 2015, the minimum capital requirement for the companies has been done away with. Customary practice is to set up a company with a minimum paid-up capital of INR 1,00,000.

Private company: A minimum of two members and two directors are needed to establish a private company with at least one director being resident in India.

Public company: A public company can be incorporated with minimum three directors and seven members with at least one director being resident in India.

Foreign investors while deciding to set up an entity in India as a private vis-à-vis a public company consider several factors such as:

- While the private company can provide for restrictions on transfer of its shares can by inserting suitable clauses in the Articles of Association, however, no such restrictions can be put on transfer of shares in public company, shares of public company are freely transferable.
- A private company as the name suggests cannot invite public to subscribe its securities.
- The compliances applicable to a private company under the Companies Act 2013 are fewer as compared to those applicable to a Public Company such as formation of various governance committees, secretarial audits, appointment of independent directors, ceilings of managerial remuneration, etc.

Labour

Employment Contract

India has adopted various measures to regulate the conditions under which fixed-term employment contracts are written, applied, and interpreted. Labour is a concurrent topic in the Indian Constitution - it is subject to legislation from both State and Central governments. The Indian Contracts Act, 1872 defines the term contract as an agreement legally enforceable by law. There must be a lawful offer and a lawful acceptance to result in an agreement.

Customary working hours and holidays

The normal working hours in a factory per day are eight. The usual working hours in India are 9 am to 5:30 pm or 9:30 am to 6 pm. In case of corporates, it is seven hours per day, six days a week. Indian subsidiaries of multinational corporations usually follow a five day – eight hour per day week. Normally, 10 days of casual leave and 20-30 days of privilege leave is allowed in a year. May Day, which is known as the International Workers Day, is celebrated every year on 1 May in India.

Minimum wage

There are laws in India for workers to receive a minimum wage. It is one of the most important aspects of starting a new line of work or running an organisation successfully. There is a law as well, which enforces the employers to pay the set minimum wages in India. This law is known as the Minimum Wages Act, 1948. The main goal of this Act is to prevent exploitation of a worker.

Work permits for foreign workers

A foreign national coming to India to work is required to get an employment visa. Employment visas are usually granted for one year, or the term of the employment / project contract and the time period can be extended once in India. All foreigners (including foreigners of Indian origin) visiting India on long term visas (Student, Medical, Research and Employment Visa of more than 180 days) are required to get themselves registered with the Foreigners Regional Registration Officer (FRRO) concerned having jurisdiction over the place where the foreigner intends to stay, within 14 days of arrival in the country.

Persons of Indian Origin (PIOs) that fall within a certain category, as specified, who have migrated from India and acquired citizenship of a foreign country other than Pakistan and Bangladesh, are eligible to avail the Overseas Citizen of India (OCI) status as long as their home countries allow dual citizenship in some form or the other under their local laws. Persons registered as OCI do not have right to vote, or eligibility to contest for elections to public/government offices, etc. Registered OCIs shall be entitled to the following benefits:

- Multiple entry, multi-purpose life-long visa to visit India
- Exemption from reporting to police authorities for any length of stay in India
- Parity with NRIs in financial, economic and educational fields, except in the acquisition of agricultural or plantation properties

A person registered as OCI for five years, is eligible to apply for Indian citizenship, if he/she has been residing in India for one year out of the five years, before making the request.

Social security

Social security is valid only for those individuals who are employed in the organised sector. The Employees' State Insurance Scheme provides medical care and other benefits for employees or labourers earning less than USD 300 a month (INR 21,000).

The Employees' Provident Fund Organisation (EPFO) is a statutory body under the Ministry of Labour and Employment, Government of India that administers social security regulations in India. It is mandatory for all employers who employ more than 20 people to apply the fund for the benefit of their workers. It covers all the pensions and the survivor benefits in the event of any employee's death. All employees are required to contribute 12 per cent of their salary to EPFO. This is automatically deducted by the employer. Employees earn a tax-free interest on contributions made to the fund. Even foreign or international workers who are employed in India are subject to the terms of this fund. Recently, the Finance Ministry allowed EPFO to invest 5 per cent of its corpus in exchange traded funds .

India also has a social security agreement, which is a bilateral agreement between two governments. This agreement serves to protect the interests of Indian citizens working in the following countries:

- Australia
- Austria
- Belgium
- Czech Republic
- Canada
- Denmark
- France
- Finland
- Germany

- Hungary
- Japan
- Republic of Korea
- Luxembourg
- Netherlands
- Norway
- Swiss Confederation
- Sweden

Sickness and pension arrangements

It is compulsory for an employer to provide medical facilities to its workforce by contributing towards Employees' State Insurance Scheme, or by providing medical benefits to its employees and their family members.

The employer contributes towards a Provident Fund Scheme and a certain portion of the contribution is appropriated towards a Pension Scheme, which provides pension benefits to the employees and their family members. Workers are also entitled to gratuity on completion of five years of continuous service. However, contribution towards a Provident Fund Scheme is not required, if the number of employees in that organisation does not exceed 20.

Trade unions

The trade unions in India are generally divided on political lines. Trade unions have struggled hard to achieve an adequate measure of protection against exploitation. The trade unions work to protect the interest of the workers and discuss key workplace-related issues with the management such as wages and benefits.

The six major Central Trade Unions (CTU) in India are the United Trade Union Congress (UTUC), Bhartiya Mazdoor Sangh (BMS), Hind Mazdoor Sang (HMS), All India Trade Union Congress (AITUC), Centre of Indian Trade Unions (CITU) and the Indian National Trade Union Congress (INTUC). A trade union will be recognised if it functions for more than a year after its registration. In case an organisation has more than one union, for it to be recognised, it must have at least 15 per cent of workers as its members.

Source: Ministry of Labour and Employment, Ministry of Overseas Indian Affairs

Accounting, reporting and audit requirements

Summary

In India, accounting, reporting and auditing requirements of business entities are primarily governed by the regulations issued by the Institute of Chartered Accountants of India (ICAI), the Securities and Exchange Board of India (SEBI), the Ministry of Corporate Affairs (MCA) and the Central Board of Direct Taxes (CBDT).

The ICAI has issued accounting standards that are applicable to all entities engaged in commercial, industrial or business activities. The legal recognition to these standards have been given by the Central Government by notification of the standards under the Companies Act, 2013 (2013 Act). The 2013 Act is an act of Parliament of India which governs the incorporation of a company, manner of conducting the affairs of a company, responsibilities of its board of directors and other provisions including winding up. It also prescribes the financial reporting and auditing requirements to be followed by all companies including foreign companies as defined in the 2013 Act.

The companies listed on recognised stock exchange in India are governed by rules and regulations issued by the SEBI from time to time. In addition, there is industry specific guidance relating to financial reporting issued by the relevant authorities such as RBI.

Following sub-sections discuss some of the common requirements:

Records to be maintained

Company should follow accrual basis of accounting. The 2013 Act requires that the records can also be maintained in electronic mode in the prescribed manner and are required to be retained for a minimum period of eight years. Further, the Central government has the power to direct the company to retain the statutory books for longer periods, in certain cases.

Preparation of financial statements

Every company is required to prepare both separate and consolidated financial statements on an annual basis in accordance with accounting framework applicable to the company. Further, a listed company is also required to publish quarterly or half yearly, as the case may be, interim financial information, subjected to review, in the formats prescribed by SEBI within the prescribed timelines.

Contents of financial statements

2013 Act lays down the format for presentation of financial statements of companies except insurance, banking and electricity companies and other class of companies for which form of financial statements is specified by the governing Act. Financial statements comprise of balance sheet, statement of profit and loss, cash flow statement, a statement of changes in equity (if applicable) and related notes.

Consolidation

The 2013 Act mandates preparation of consolidated financial statements, if a company has one or more subsidiaries unless the following conditions are compiled:

- It is a wholly-owned subsidiary or partially owned subsidiary of another company and all its other members, including those not otherwise entitled to vote, having been intimated in writing and they do not object to the fact that company is not presenting consolidated financial statements.
- Its securities are neither listed nor in the process of listing on any stock exchange, in India or outside India; and
- Its ultimate or any intermediary holding company files consolidated financial statements with the registrar which is in compliance with the applicable accounting standards.

Audit of financial statements

Every company in India, irrespective of its size, must have its financial statements audited by a Chartered Accountant in practice (member of the ICAI). The audits are required to be conducted in accordance with the auditing standards issued by ICAI and notified by the Central Government under the 2013 Act. In addition, Income Tax Act, 1961 mandates audit, to be conducted by a Chartered Accountant in practice (member of the ICAI), of tax payers meeting certain specified thresholds.

Auditing standards

The Standards of Auditing issued by the ICAI are substantially similar to the auditing standards issued by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC).

Reporting on internal financial controls

In case of a listed company, directors are required to lay down internal financial controls to be followed by the Company and report annually whether such internal financial controls were adequate and operating effectively. In case of other companies, directors are required to report whether such internal financial controls were adequate.

In case of all companies, auditors are required to report whether internal financial controls over financial reporting in relation to separate and consolidated financial statements were adequate in operating effectively.

2013 Act does not prescribe internal control framework for the purpose of reporting by auditors and directors.

Mandatory Firm Rotation

To reduce the risks of excessive long term familiarity, 2013 Act prohibits auditor appointment for a period of more than five consecutive years (in the case of individual as an auditor) or ten consecutive years (in the case of an audit firm as an auditor) by listed and certain other class of companies. Individual/Audit firm as an auditor that has completed the above prescribed period of appointment is eligible for appointment as auditors after a period of five years from the completion of the above mentioned period.

Inspection of records

The books of accounts and other records are open to inspection by any director, Registrar of Companies and other government authorities such as those involved with excise and sales tax.

Accounting year

Under the 2013 Act, companies are required to adopt uniform financial year ending on 31 March unless specifically permitted by the authorities. Similarly, the accounting year must end on 31 March every year for income-tax purposes.

Filing of financial statements/results

A company is required to hold an Annual General Meeting (AGM) within six months of the end of the financial year, and filing of the financial statements with the Registrar of Companies is required within 30 days of the AGM. Further, listed companies also need to file the audited (or reviewed, as applicable) financial results with the stock exchange within 60 days, in case of annual periods, and 45 days, in case of quarterly periods except last quarter.

Language in which business records are required to be maintained

There is no prescribed language for maintenance of books and business records. It can be maintained in any Indian language. Companies generally maintain their accounts in English.

Maintenance of accounting records in a foreign currency and presentation of financial statements.

The accounting records, whether electronic or manual, have to be kept in Indian currency. However, the foreign currency amounts may also be disclosed.

Accounting framework

2013 Act prescribes two accounting framework, Indian Accounting Standards (Ind AS), which are based on International Financial Reporting Standards as issued by International Accounting Standards Board with certain carve-outs, mandatory for certain class of companies, and standards that are substantially different from Ind AS. Companies are required to determine the relevant accounting framework as per the applicable law. Further, company may irrevocably opt to prepare Ind AS compliant financial statements for the accounting periods beginning on or after 1 April 2015.

Ministry of Corporate Affairs (MCA) has notified 39 Indian Accounting Standards (Ind-AS), which are based on International Financial Reporting Standards (IFRS) with certain carve-outs. Ind AS are applicable to companies in the manner specified in the roadmap issued by MCA. Following is the roadmap for mandatory adoption of Ind-AS by all companies other than insurance companies, banking companies and non-banking finance companies (NBFCs):

- The applicability of Ind AS is made mandatory under phase I for companies whose net worth is of INR 5 bn or more for accounting periods beginning on or after 1 April 2016, with comparatives for the period ending 31 March 2016 or thereafter.
- Under Phase II, Ind AS is made mandatory for accounting periods beginning on or after 1 April 2017, with comparatives beginning for period ending 31 March 2017 or thereafter for the companies having net worth more than INR 2.5 bn but less than INR 5 bn.
- Both under phase I and phase II, Ind AS would be mandatorily applicable to companies whose equity and debt securities are listed or are in the process of listing on any stock exchange in India or outside India, also to holding, subsidiary, joint venture or associate companies of companies covered above.

Separate road maps have been issued for banks, insurance companies and NBFCs to transition to Ind AS, earliest period is accounting period beginning on or after 1 April 2018.

ROC filing

The MCA requires filing of financial statements with the Registrar of Companies, using the eXtensible Business Reporting Language (XBRL) taxonomy, for the following companies:

- all companies listed in India and their Indian subsidiaries;
- all companies having paid up capital of INR 50 mn and above; and

- all companies having turnover of INR 1 bn and above.

For the remaining companies, it is required to fill the prescribed forms.

The XBRL documents of financial statements are required to be certified by a Chartered Accountant or Company Secretary or Cost Accountant in whole time practice.

Income Computation and Disclosure Standards (ICDS)

In view of the significant developments in convergence with IFRS, ICDS were notified under the IT Act, which are, in principle, closer to the existing Indian GAAP than the IFRS based Ind AS. These standards are effective from the current financial year (2016-17) itself and are required to be followed by all taxpayers following mercantile system of accounting for the purpose of computation of income from business and 'other income' chargeable to tax.

Direct tax

Income tax is chargeable on taxable income computed in accordance with the provisions of the Income-Tax Act, 1961 (hereinafter referred to as 'IT Act'). Income can be brought within the tax net under the following heads of income:

1. Income from salary
2. Income from house property
3. Profits and gains from business and profession (PGBP - Business income)
4. Capital gains
5. Income from other sources (Income not specifically covered under above heads of income like interest, dividend, etc.)

All taxpayers are required to follow a uniform tax year from 01 April to 31 March for tax purposes, referred to as 'previous year', irrespective of the financial year ('FY') followed for accounting purposes.

India follows a mix of source based and residence based taxation. Global income of a resident is taxable in India. However, non-residents are taxable on certain India sourced income.

Taxation of individuals

Depending upon the duration of physical presence in India, an individual can be:

- Resident and ordinarily resident (ROR)
- Resident and non-ordinarily resident (RNOR)
- Non-resident (NR)

Scope of taxation of an individual is as follows:

- ROR are taxable on their worldwide income
- RNOR and NR are taxable for their India-sourced income

The personal tax rates for the financial year 2017-18 are as follows:

Income slabs (USD)	Income slabs (INR)	Rate of tax (%)
Up to $3,750*	Up to INR 250,000	Nil
$3,750 to $7,500	250,000 to 500,000	5% # of the amount of total income exceeding INR 2,50,000
$7,500 to $15,000	500,000 to 1,000,000	INR 12,500 + 20% of the amount of total income exceeding INR 500,000
Above $15,000	Above 1,000,000	INR 112,500 + 30% of the amount of total income exceeding INR 1,000,000

*USD rate taken at 66.66

*Minimum exemption limit for:

Senior citizen (age 60 years and above but less than 80 years): INR 300,000 (USD 4,500)

Very senior citizen (age 80 years and above): INR 500,000 (USD 7,500)

The rates, mentioned above, are exclusive of applicable surcharge, education cess and secondary and higher education cess. Please refer to the section on 'Rate of surcharge, education cess and secondary and higher education cess' for further details.

Taxation of Partnership firm (including LLP)

Scope of taxable income of a firm is as follows:

- Resident: Taxed on worldwide income
- Non-resident: Taxed on (a) receipt, (b) deemed receipt, (c) accrual and (d) deemed accrual - of income in India

A firm is said to be resident in India in every case except where during that year the control and management of its affairs is situated wholly outside India.

The tax rates for the financial year 2017-18 is 30 per cent, exclusive of applicable surcharge, education cess and secondary and higher education cess.

Corporate income tax rates

Scope of taxable income of a company is as follows:

- Resident*: Taxed on worldwide income
- Non-resident: Taxed on (a) receipt, (b) deemed receipt, (c) accrual and (d) deemed accrual - of income in India

*From FY 2016-17 onwards, a company shall be a resident in India, if it is an Indian company or its place of effective management is in India. Place of effective management (PoEM) has been defined to mean a place where key management and commercial decisions that are necessary for the conduct of business of an entity as a whole are, in substance made. The Indian revenue authorities have also released guidelines for determination of PoEM of a foreign company in India.

Tax rate for domestic company

The corporate tax rates for the financial year 2017-18 is 30 per cent, exclusive of applicable surcharge, education cess and secondary and higher education cess.

A reduced tax rate of 29 per cent is applicable to domestic companies for FY 2016-17 with a total turnover/gross receipts of upto USD 0.75 mn (INR 50 mn) in FY 2014-15. Further, the Finance Act 2017 has legislated a lower corporate tax rate of 25 per cent for FY 2017-18 for domestic companies, whose total turnover in FY 2015-16 was not more than INR 500 mn (USD 7.5 mn).

The above tax rates as applicable for both the financial years, is exclusive of applicable surcharge, education cess and secondary and higher education cess.

Domestic companies set up on or after 01 March 2016, engaged solely in manufacture or production have an option to be taxed at 25 per cent subject to fulfilment of certain specified conditions (see section 'manufacturing companies' for further details).

The above tax rate is exclusive of applicable surcharge, education cess and secondary and higher education cess.

Tax rate for foreign company

The corporate tax rates for a foreign company is 40 per cent, exclusive of applicable surcharge, education cess and secondary and higher education cess.

Rate of surcharge and cess

Companies	Net Income (USD)		
	< 0.15 mn (INR 10 mn)	0.15 mn ~ 1.50 mn (INR 10 - 100 mn)	> 1.50 mn (INR 100 mn)
Domestic	Nil	7%	12%
Foreign	Nil	2%	5%

Rate of surcharge

Individuals/AoP are subject to surcharge of 15 per cent if their total income exceeds USD 0.15 mn (INR 10 mn) while firms are subject to surcharge of 12 per cent if its total income exceeds USD 0.15 mn (INR 10 mn).

The Finance Act 2017 has introduced a surcharge of 10% for individuals/AoP if their total income exceeds USD 75,000 (INR 5 mn) but does not exceed USD 0.15 mn (INR 10 mn).

Rate of education cess and secondary and higher education cess.

Cess is applicable on all taxpayers and all levels of income, and is computed on the amount of tax computed, inclusive of surcharge (wherever applicable).

Particular	Rate of Tax %
Education cess	2%
Secondary and higher education cess	1%

Minimum alternate tax (MAT)/ Alternate minimum tax (AMT)

India has minimum tax regime, whereby MAT is payable by corporates on profits as per books (subject to specified adjustments), where tax payable on total income under the normal provisions of Income-Tax Act is less than MAT. Similarly, AMT is payable by other persons on their 'adjusted total income'.The tax rates for the financial year 2017-18 is 18.5 per cent, exclusive of applicable surcharge, education cess and secondary and higher education cess.

Type of taxpayer	Rate of tax (%)	Applicability	Credit availability
Company	18.5 per cent of book profits	MAT is leviable where tax payable on the total income is less than 18.5 per cent of book profits.	The excess of MAT over normal tax is treated as credit, which can be set-off in any 10 subsequent years against normal tax liability subject to prescribed limitation.*
LLP claiming certain specified deductions Persons (other than company and LLP) claiming certain specified deductions$	18.5 per cent on adjusted total income	AMT is leviable where tax payable on the total income is less than 18.5 per cent of adjusted total income.	The excess of AMT over normal tax is treated as credit, which can be set-off in any 10 subsequent years against normal tax liability subject to prescribed limitation.*

$ It is applicable when the adjusted total income exceeds USD 0.03 mn (INR 2 mn)

Time limit for claiming credit of MAT/AMT has been increased to 15 years as against existing 10 years by the Finance Act 2017.

As regards foreign companies, it has been clarified that MAT provisions do not apply to a foreign company if it does not have a permanent establishment in India (in accordance with the provisions of relevant tax treaty) or in case where there is no tax treaty available, it is not required to seek registration under any law for the time being in force relating to companies.

Taxation of dividends

The rate of DDT mentioned above is exclusive of applicable surcharge @ 12 per cent, education cess and secondary and higher education cess @ 2 per cent and 1 per cent, respectively. Further, DDT is required to be calculated on the grossed-up amount.

Particular	Rate of tax (%)	Basis for levy
Indian company paying dividend	15% as Dividend Distribution Tax (DDT	Dividends declared, distributed or paid after specified adjustments**

DDT

Where a resident individual, HUF or firm receives aggregate dividend in excess of INR 1 mn (USD 15,000) from domestic companies, tax at the rate of 10 per cent on the amount of dividend in excess of INR 1 mn shall be levied. The Finance Act, 2017 has proposed to extend this tax to all residents (except domestic companies and specified charitable institutions)

**Deduction of dividends received from a subsidiary is allowed, subject to certain conditions, for computing DDT. However, no credit of DDT paid on the dividend received is allowed under the Indian laws. Further, DDT is not a tax deductible expense.

Dividend received from a foreign company is taxable in the hands of Indian shareholders at their effective tax rates. However, in the case of dividends received by an Indian company from a foreign company in which the Indian company holds 26 per cent or more equity, tax at a concessional rate of 15 per cent is levied.

Taxation on income distributed by way of buy-back of unlisted shares

Tax is levied @ 20 per cent (plus applicable surcharge and cess) on the 'distributed income' paid by unlisted companies to their shareholders on buy-back by a company of its own shares.

'Distributed income' is computed as the difference between the amount paid as consideration for buying back the unlisted shares and the consideration received by the company at the time of such shares computed in accordance with prescribed rules. Such tax would be paid by the company while buying back its own shares.

Buy-back receipt taxed in the hands of the company would be exempt from tax in the hands of the shareholders.

Capital gains tax

Capital gains tax is leviable on transfer of a capital asset for a value greater than its cost of acquisition. In case of non-resident investors, gain from transfer of shares/debentures of an Indian company is computed in foreign exchange used for the investment and then converted in Indian Rupee on the date of transfer, thus providing for adjustment of fluctuation in foreign exchange. The capital gains are further categorised into short-term capital gain (STCG) and long-term capital gain (LTCG) depending on the period of holding of the asset transferred.

A short term capital asset is an asset held for not more than 36 months. However, shorter holding period of 12 month and 24 months is prescribed for listed security/unit of an equity-oriented fund and unlisted shares respectively. The Finance Act 2017 has reduced the holding period to 24 months (from 36 months) in case of immovable property (being land or building or both) in order to qualify as a long term capital asset. Capital asset which do not qualify as short term are treated as long term capital asset.

STCG is chargeable at the normal rate of tax depending on the taxability of transferor. However, STCG on transfer of listed security/unit of an equity-oriented fund etc. (subject to Security Transaction Tax) is taxable at 15 per cent tax rate.

LTCG is computed on adjusted gains computed after considering inflation (based on cost inflation Index), except in the case of LTCG accruing to non-resident investors from transfer of shares/debentures of an Indian company. Tax rate on LTCG can be categorised as follows:

Nature of long term capital asset transferred	Tax rate
Listed security / unit of an equity-oriented fund etc (subject to STT)	Exempt*
Unlisted securities or shares of a private company transferred by a non-resident (without considering foreign exchange fluctuation)	10%
Other assets	20%

*As per the Finance Act 2017, the exemption on listed security shall be available only in cases where acquisition of such security was subject to STT. Certain exceptions to this requirement are already notified vide notification no 43 of 2017 dated 05 June 2017.

There is a separate computation mechanism for depreciable business assets, which form part of block of assets held by a taxpayer.

Taxation of non-residents

Non-residents are taxable on the income received or accruing in India and income deemed to have been received or accrued in India. Deemed accrual provides for taxation on following terms:

Business income: Business income of a non-resident is taxable in India, if it is effectively connected with a 'business connection' of such non-resident in India. The term 'business connection' is not defined in the IT Act. Though it has a wider scope, it is conceptually similar to permanent establishment (PE) as defined in tax treaties. Profits from a business income of a non-resident, attributable to operations carried out in India, are taxable in India.

Fees for Technical Services (FTS): Fees for managerial, technical or consultancy services rendered by a non-resident is taxable in India (where a non-resident does not have a PE in India) @ 10 per cent of gross receipt.

Royalty income: Royalty payable to a non-resident is taxable @ 10 per cent, plus surcharge and cess. The final tax rate would be an inter-play between the rates provided in the treaty and the Act. Specific explanations seek to tax payments for use of computer software and telecommunication charges as Royalty.

Interest income: Tax @ 20 per cent is applicable on interest payable by an Indian company to a non-resident for monies borrowed in foreign currency. A lower withholding rate of 5 per cent is provided for external commercial borrowings and long term bonds before 01 July 2017. This benefit is proposed to be extended to borrowings before 01 July 2020 and payment for interest on rupee denominated bonds). Similarly, lower rate of withholding of 5 per cent is available for interest payable to a FII or a Qualified Foreign Investor (QFI) on a rupee denominated bond of an Indian company or a government security issued before 01 July 2017, subject to certain other conditions. The Finance Act 2017 has extended the sun-set clause to 01 July 2020.

The rates mentioned above are exclusive of applicable surcharge, education cess and secondary and higher education cess. Please refer to the section on 'Rate of surcharge, education cess and secondary and higher education cess' for further details.

Capital gains: Gains accrued on a non-resident on account of transfer of a capital asset situated in India, are taxable in India. Shares or an interest in a foreign company shall be deemed to be situated in India, if such shares or interest derives, directly or indirectly, its value substantially from assets located in India.

Tax treaty benefit: A non-resident eligible for a tax treaty can be taxed under the provisions of tax treaty, at a location deemed more beneficial. India has a vast network of favourable tax treaties. Till date, India has entered into comprehensive tax treaties with 96 countries.

Tax treaties with various countries such as Mauritius, Singapore, Cyprus, Netherlands etc. provide benefits in form of capital gains exemption on transfer of shares of Indian companies. However, tax treaties with Mauritius, Singapore and Cyprus have been revised to withdraw capital gains exemption on transfer of shares acquired on or after 01 April 2017, while simultaneously grandfathering tax benefit to the shares acquired before 01 April 2017. Further, tax treaties with Australia, US, UK, Singapore, etc. provide beneficial tax treatment for income from FTS.

A non-resident is required to furnish a Tax Residency Certificate, which is issued by the Revenue authorities of his/ her State of residence. In addition, the non-resident needs to furnish a declaration in the prescribed format to be eligible for claiming tax treaty benefit.

Equalisation levy:

An equalisation levy of 6 per cent of the amount of consideration for specified services i.e. online advertisement, provision for digital advertising space etc. payable to a non-resident (not having a PE in India), is to be deducted by the remitter with effect from 01 June 2016. The levy has been introduced to tax digital services rendered by foreign service providers without having a presence in India.

Security transaction tax (STT)

Security Transaction Tax (STT) is levied on various security transactions carried out through a recognised stock exchange in India. A reduced/ nil rate of capital gains is prescribed for the transactions which have been subjected to STT.

Commodities transaction tax (CTT)

The Commodities Transaction Tax (CTT) is levied along the lines of STT. CTT is levied on taxable commodities traded at recognised associations.

Wealth tax

Wealth tax has been abolished vide Finance Act, 2015.

Gift tax

India does not levy gift tax under a separate statute. However, certain receipts of sum of money or property by an individual, without adequate consideration, are taxed as other income. Similarly, receipt of certain shares by a company or a firm without adequate consideration are taxed as other income in the hands of the recipient. Further, consideration received from a resident in excess of the fair value of shares issued is taxable in the hands of the company issuing such shares.

The Finance Act 2017 has proposed to extend this provision to receipt of property (immovable or moveable) by any taxpayer without adequate consideration.

Estate duty

No estate or death duty is charged.

Computation of business income

Business income is generally taxable on the net basis i.e. gross income less allowable tax deductions. Generally, all expenses laid out and expended for business purposes (other than capital expenses) are deductible (subject to compliance with withholding tax provisions) from the income of the taxpayer for income-tax purposes. The deductibility is further subject to exceptions and fulfilment of conditions as stated in the IT Act.

The following principles are generally applied for examining the admissibility of an expense:

- Expense should be incurred for the business
- Expense should be incurred in the previous year
- Expense should not be of a personal nature
- Expense should be of a revenue nature - expenses of a capital nature are not allowed
- Expense should not be for a purpose prohibited by law
- No deduction of expenses incurred in respect of exempt income

Certain expenses are specifically disallowed or the quantum of deduction is restricted. These include:

- Income-tax
- Expenditure incurred on CSR activities
- Expenditure for the purpose of earning exempt income
- Expenses incurred in cash beyond specified limit.
- Provision for taxes, duties, interest on loans from public financial institutions or on term loans from a scheduled bank

and certain contributions to statutory funds on behalf of employees, not actually paid. However, such expenditure is deductible in the year in which it is actually paid.

Depreciation of capital assets is allowed on the basis of the reducing balance method using varying rates, depending on the nature of assets. All similar type of assets eligible for the same rate of depreciation are clubbed together in a 'block' and depreciation is charged on the value of that block. Depreciation is available for a full year, irrespective of the actual period of use of the asset. However, in the year of acquisition of the asset, depreciation is allowed at half the normal rates, if the asset is used for less than 180 days in that year.

Depreciation on intangible assets such as know-how, patents, copyrights, trademarks, licenses, franchises or other similar business or commercial rights, is also available.

The rates of depreciation for different blocks of assets are as follows:

For FY 2016-17, the rate of 40 per cent is capped for the companies claiming 25 per cent tax rate.

Blocks of assets	Rates
Residential buildings except hotels and boarding houses	5%
Buildings meant for non-residential purposes such as hotels and boarding houses	10%
Furniture and fittings	10%
General plant and machinery	15%
Intangible assets	25%
Computers	60%

Income computation and disclosure standards (ICDS)

The Central government has notified ICDS, which prescribes the detailed provisions to be applied while computing tax under the heads – Profits and Gains from Business and Profession and other income. These standards are applicable for FY 2016-17 onwards.

Set-off of business loss and unabsorbed depreciation

Business losses, other than from speculation business, are permitted to be set off against income from any other source (except income from employment i.e. salary income) in the same year. Business losses, which could not be so set off, are permitted to be carried forward for setting off against business profits arising in the eight subsequent years. Unabsorbed depreciation is permitted to be carried forward for an unlimited period.

Key direct tax incentives/ tax holidays

India provides various tax incentives in form of higher deduction/tax exemptions. Finance Minister in his speech in 2015 union budget proposed to phase out tax incentives and reduce corporate tax rate from 30 per cent to 25 per cent over next four years. Thereafter, a plan for phasing out of tax incentives was issued for public comments.

Research and development (R&D) activities

The Income-Tax Act provides for deduction for expenditure incurred on scientific research ranging from 125 per cent to 200 per cent of the amount of expenditure. It also allows for weighted deduction for donations made to certain institutions, associations, company for scientific research.

Manufacturing companies

- Domestic companies set up on or after 01 March 2016, engaged in the business of manufacture or production of article or thing have an option to pay taxes on a lower corporate income tax rate of 25 per cent. The total income of such companies should be computed in prescribed manner and the company shall not be eligible for any tax incentives.
- 100 per cent deduction available for 10 consecutive tax years to any undertaking involved in the manufacture and production of any article/thing, located in North-Eastern states (provided the undertaking commences manufacturing by 31 March 2017) and carries on any eligible business.
- A deduction of 15 per cent of the cost of new plant and machinery [investment more than USD 3.74 mn (INR 250 mn)] acquired and installed by a manufacturing unit in any one financial year. This one-time allowance is over and above the normal depreciation and additional depreciation allowable under the Act. The allowance is available only if such assets are acquired and installed on or before 31 March 2018.

Special economic zones

A specifically delineated duty-free enclave deemed to be a foreign territory for purposes of trade operations, duties and tariffs.

The deductions are:

- To SEZ developer: For 100 per cent of profits and gains derived from developing and maintaining a SEZ for ten consecutive assessment years out of fifteen years commencing from the year in which a SEZ has been notified by the central government. The deduction shall not be available where development of SEZ begins on or after 1 April 2017.

- To SEZ unit: For profits and gains derived by its unit set up in any SEZ that commences manufacture or production or article or thing or start providing services on or before 31 March 2020 as follows:
  i. 100 per cent export profits for the first five tax years
  ii. 50 per cent of export profits for the next five tax years
  iii. Upto 50 per cent of export profits for the next five tax years (subject to transfer of profits to a special reserve)

Start-ups

- The Finance Act, 2016 has introduced 100 per cent deduction of the profits earned by a start-up during any of the three years out of the initial five* years of its operations.
- The deduction is however available only to a new entity which is not set up by way of the splitting up or restructuring of an existing undertaking.
- The start-up should be engaged in a business which involves innovation, development, deployment or commercialisation of new products, processes or services driven by technology or intellectual property.
- Further, the startup should not have a turnover exceeding USD 3.74 mn (INR 250 mn) per annum during FY 2016-17 to FY 2020-21

* The Finance Act 2017 has increased the window of claiming 100 per cent deduction from five years to seven years.

Business specific incentives for capital expenditure

100 per cent deduction on capital expenditure available for the following categories of specified businesses which commences its operation on or after specified dates:

- Laying down or operating cross country natural gas or crude pipeline:
  - Laying down and operating slurry pipeline for transportation of iron ore
  - Setting up and operating semi-conductor and wafer fabrication manufacturing facility
  - Building and operating a hotel of two star or above
  - Bee-keeping and production of honey and beeswax
  - Setting up and operating an inland container depot or a container freight station
  - Developing or operating and maintaining a new infrastructure facility on or after 1 April 2017
- 150 per cent deduction (restricted to 100 per cent with effect from 01 April 2017) on capital expenditure shall be available for the following categories of specified business which commences its operations on or after specified dates:
  - Setting up and operating a cold chain facility
  - Setting up and operating a warehousing facility for storage of agricultural produce
  - Building and operating a hospital with at least 100 beds for patients
  - Developing and building a housing project under specific schemes
  - Production of fertilizer

Patent box regime

- In order to encourage indigenous research and development activities, royalty income of the eligible assessees in respect of a patent developed and registered in India, shall be taxable at 10 per cent on the gross amount of royalty.
- An 'eligible assessee' means an Indian resident who is the true and first inventor of the invention and whose name appears on the patent register as the patentee in accordance with Patents Act, 1970.

Corporate tax compliance

Withholding tax

The IT Act casts an obligation on each taxpayer to withhold tax on specified payments, among others, on the following:

- Salaries
- Interest
- Rent
- Commission or brokerage
- Payments to contractors
- Professional/technical fees/royalty
- Consideration payable on transfer of immovable property

All payments to non-residents, which are taxable in India, attract tax withholding.

Indian tax withholding provisions also extend to payments made by non-residents. Thus, in certain situations, a non-resident making payment to another non-resident/resident is required to undertake tax withholding as per the Indian regulations.

Further, the deductee, i.e. the person whose receipts are subject to tax withholding, needs to disclose his/her Permanent Account Number (PAN). In case the person fails to do so, withholding tax rate would be the higher of the following rates:

- The rate prescribed in the IT Act
- At the rate in force i.e. the rate mentioned in the Finance Act, 2017
- At the rate of 20 per cent

However, the increased rate of withholding tax would not trigger for payments to non-residents, not having PAN, if the non-resident furnishes prescribed information.

Quarterly returns (in prescribed form depending on the nature of payment) need to be filed with respect to taxes withheld during the relevant quarter.

Extensive provisions are built in for enforcing compliance with tax withholding obligations.

Advance tax

Every taxpayer is required to pay his/her tax liability for the year during the previous year itself, in instalments prescribed. The tax liability is to be worked out on the basis of an estimate of current income, and the income tax thereon shall be calculated at the rates in force during the relevant previous year. Interest is levied for non-compliance with advance tax provisions.

Self-assessment tax

Every taxpayer is liable to compensate the required tax payable (if any) on the basis of actual income, after considering the credit for the advance tax paid and taxes deducted at source. Self-assessment tax is payable after the completion of the previous year, but before filing the return of income.

Permanent account number (PAN)

All taxpayers are required to make an application for the allotment of tax registration number, termed as PAN. The application is to be made in Form 49A, Form 49AA (depending upon the residential and/or registration status of an assessee).

This number is to be quoted on all tax returns, correspondence with the tax authorities and documents relating to the prescribed categories of transactions. Failure to quote PAN by the income recipient may result in a higher rate of tax withholding.

Tax deduction account number (TAN)

Every person responsible for withholding tax in accordance with the provisions of the IT Act is required to make an application for the allotment of withholding tax registration number which is called the tax deduction account number (TAN). The application is to be made in Form 49B, within one month from the end of the month in which the tax is deducted.

Other compliances

All the companies or firms are required to file a return of income for a previous year within the prescribed due dates.

Different due dates have been prescribed for this purpose under the IT Act, which are as below:

In case of:	
• A company; • A person (other than a company) whose accounts are required to be audited under the IT Act or under any other law in force during the period; • A working partner of a firm whose accounts are required to be audited under the IT Act or under any other law in force during the period.	30th day of September of the assessment year
• In the case of a taxpayer who is required to file an accountant's report under the transfer pricing regulations.	30th day of November of the assessment year
• In the case of any other assesse	31st day of July of the assessment year

The Finance Act 2017 has prescribed a maximum fees of INR 10,000 (USD 150) where return of income is filed after prescribed due dates.

General anti-avoidance rules (GAAR)

To control 'impermissible avoidance arrangement' (IAA) entered into by a person to avoid taxes, the provisions of General Anti-Avoidance Rules (GAAR) have been introduced in India. It is noted that an arrangement would be considered an IAA where its main purpose is to obtain a tax benefit. An agreement will also be treated as an IAA if it lacks 'commercial substance' and does not meet the criteria of being a bonafide business transaction in the ordinary course.

Notwithstanding the above, GAAR provisions will not attract to an arrangement where the tax benefit arising in aggregate does not exceed INR 30 Mn

GAAR deals with aggressive tax planning involving the use of sophisticated structures. The provisions of GAAR is effective 01 April 2017.

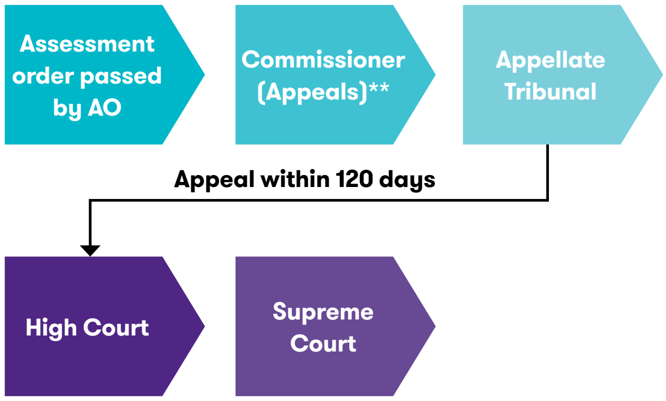
Direct tax enforcement in India

*AO can make a reference to the transfer pricing officer (TPO) for transfer pricing (TP) audit. The TPO completes TP audit on receipt of reference from AO and forwards the TPO order to the AO for merging it with the assessment order on completion of the audit of return of income.

It takes about 21 to 33 months (depending upon whether a reference is made to TPO) to complete an audit from the end of the assessment year. This period is proposed to be gradually reduced to 12 months over next three years.

Direct tax dispute resolution process

Dispute resolution is a multi-layered process in India.



**Alternatively, application may be filed with the dispute resolution panel objecting to variations proposed by the AO to the income of the taxpayer.

The entire litigation, till the Supreme Court level, generally gets settled over a period of 10 years.

Other alternatives to resolve tax litigation

- Settlement commission
- Advance ruling for transactions (including proposed ones) involving non-residents
- MAP - An alternate mechanism under tax treaties for resolving international tax disputes by the competent authorities of each state.

Finance Act, 2016 introduced the direct tax dispute resolution scheme to provide for a window to withdraw pending appeal and settle the dispute with the tax department. The taxpayer can make a declaration of the amount of tax, interest and penalty which is pending as on 29 February 2016 before any CIT (Appeal) in the prescribed form and manner.

Nature of Tax	Domestic Company		Foreign Company	
	7% surcharge	12% surcharge	2% surcharge	5% surcharge
Corporate Tax	33.06%/ 27.55%*	34.61%/ 28.84%*	42.02%	43.26%
Dividend Distribution Tax**	17.30%	17.30%	NA	NA
Minimum AlternateTax	20.39%	21.34%	NA	NA
Tax on LTCG	22.04%	23.07%	21.01%	21.63%
Tax on LTCG (without forex adjustment)	NA	NA	10.51%	10.82%
Tax on LTCG (where transfer is subject to STT)	NIL	NIL	NIL	NIL
Tax on STCG	33.06%	34.61%	42.02%	43.26%
Tax on STCG (where transfer is subject to STT)	16.53%	17.30%	15.76%	16.22%
Buy Back Tax$	23.07%	23.07%	NA	NA

Please refer to the section on 'Rate of surcharge, education cess and secondary and higher education cess' for details on surcharge and cess.

* For companies having applicable corporate tax rate of 25 per cent.

** before grossing up

$ Surcharge of 12 per cent is applicable in all cases.

Indirect tax

Introduction of Goods and Services Tax ('GST') on 1 July 2017 had been a significant reform in the Indirect taxation of the nation. Absorbing the large number of Central and State taxes mainly Central Excise, Service Tax, Value Added Tax, Central Sales Tax, Entry Tax, Octroi, Entertainment Tax, Luxury Tax, Countervailing Duty and Special Additional Duty on Customs in itself, GST had led the way for a common national market. Key indirect taxes applicable in the country are:

- **Goods and Services Tax** – Tax on supplies of goods and services
- **Customs Duty** – Duty imposed on import of goods to India
- **Professional Tax** – Tax on professions, trades, callings and employments

Goods and Services Tax

The Government of India have made possible the introduction of nation's biggest tax reform – GST. It aims to mitigate the cascading or double taxation by way of single point taxation system with free flow of input credits.

Scope of GST

GST is to be levied on supply of all goods and services except the supply of alcohol for human consumption. Levy of GST on petroleum crude, high speed diesel, motor spirit (commonly known as petrol), natural gas and aviation turbine fuel have been postponed and to be notified by the government at a later date.

Dual structure levy

GST is a dual structure wherein Centre and States/Union territories, both have the power to levy the tax on supplies on goods and services. The dual levy structure will be as under:

- Central Goods and Services Tax ('CGST') to be levied by Centre and State Goods and Services Tax ('SGST')/Union Territory Goods and Services Tax ('UTGST') to be levied by respective states/union territories on all supplies within a state/union territory;
- Integrated Goods and Services Tax ('IGST') to be levied by Centre on all supplies between the two different states/union territories. Further, IGST is also to levied on export/import of goods or services from/to India.
- Compensation Cess ('Cess') to be levied on specified supplies for the purpose to compensate the states for the loss of revenue on account of implementation of GST.

Nature of supply

Levy of CGST & SGST/UTGST or IGST will depend upon the nature of supply. Separate provisions for goods and services have been incorporated under GST law to identify the nature of supply. Location of supplier and the place of supply of goods or services are the two factors to determine the nature of supply.

- Intra-state supply: Location of supplier and place of supply of goods or services are within the same state/union territory

- Inter-state supply: Location of supplier and place of supply of goods or services are with different states/union territory

Point of levy under GST

The earlier indirect taxes prevailing in India entails multiple points of levy. For instance, excise duty is levied on the manufacture of goods. Service tax is levied on the provision of taxable services. VAT is levied on the sale of goods.

The triggering point for levy of GST is the supply. Provisions for determining the time of supply have been provided, both in respect of goods and services. Hence, the tax incidence would be at the 'time of supply' as against the multiple points of levy under earlier regime.

Tax rates under GST

All goods and services are fitted into a four tier rate structure of 5, 12, 18 and 28 percent. While essential items like food grains will attract a zero rate, demerit and luxury goods will attract the highest rate and may attract cess also.

Anti-profiteering

One of the major objective for implementation of GST were to provide a free flaw of the input tax credits which should result into reduction in prices of goods and services. To safeguard the consumers, anti-profiteering provisions have been incorporated under GST casting responsibilities on the suppliers to reduce their prices of goods and services on account of benefit of reduced tax rate or availability of input tax credits. Suppliers not complying with the anti-profiteering provisions are liable for penal consequences and it could also lead to cancellation of registration under GST.

Customs Duty

Customs duty, a federal government levy is leviable on import/export of goods to/from India. The taxable event for levy is 'import/export' and import/export duty is payable at the time of import/export of goods to/from India. India follows the Harmonised System of Nomenclature (HSN) classification rules and the goods are classified under different chapter/tariff headings, primarily according to their description, components and use. The duties or taxes applicable on import shall comprise:

- Basic customs duty – 'BCD' (standard rate of 10 per cent)
- Customs cess (leviable on component of BCD @ 3 per cent)
- IGST @ 18per cent (leviable on total value of BCD plus customs cess)

Presently, the effective standard rate of customs duty that is applicable on the import of goods is approximately around 30.15 per cent with input tax credit of IGST, subject to exemption/concession as may be available/notified from time to time and Free Trade Agreements entered into by India with other countries. However, presently there is no export duty leviable on goods exported from India, except for a few goods such as minerals, etc. (which are scarcely available).

Professional tax

Professional tax is a levied by the State on professions, trades, a calling or employment in a State. Thus, every person who is engaged in any of the activities mentioned above is liable to pay professional tax. Not all the State governments levy professional tax, currently. In States where such a levy exists, every enterprise and employee earning a salary is required to register and pay professional tax.

Transfer pricing in India

Background
Globalisation and increased integration between economies worldwide has paved way for global business operations and subsequently complex inter-company transactions. These transactions could lead to base erosion and shifting of profits to opaque tax jurisdictions. Therefore, transfer pricing is under constant scrutiny of tax authorities globally.

Indian Transfer Pricing Regulations (TP Regulations) were introduced in India in 2001 to avoid shifting of profits from India to another jurisdiction arising due to the international transaction with the related parties i.e. associated enterprise(s) (AEs). Further, the scope of TP Regulations was extended to include specified domestic transactions (SDT) with effect from 2012.

Legislation
As per the TP regulations, the international transaction and SDT between the AEs should comply with the arm's length principal i.e. a price which is applied or proposed to be applied in a transaction between persons other than associated enterprises, in uncontrolled conditions.

International transaction
The Act defines the term 'international transaction' to mean a transaction between two or more AEs, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, financing or any other transaction having a bearing on the profits, income, losses or assets of such enterprises or any cost contribution agreement.

Further the definition of international transaction also includes 'deemed international transaction' which means that a transaction entered into by an enterprise with a person other than an AE (whether resident or non-resident) shall be deemed as an international transaction, if:

- there exists a prior agreement between such other person and the associated enterprise; or
- the terms of such a transaction are, in substance, determined between such other person and the associated enterprise.

Specified Domestic Transactions (SDT)
Transfer pricing provisions were also introduced for SDT so as to curb the shift of profits between resident entities. The nature of transaction includes transaction entered into with entities/ within business units claiming tax exemptions. SDT provisions are applicable where the aggregate of such transactions exceeds a sum of USD 3 mn[6] (INR. 200 mn) in a year.

Associated enterprises

International transactions
In the Indian TP Regulations, the definition of AEs is broadly similar to the definition in the Organisation for Economic Co-operation and Development (OECD) TP Guidelines. AE(s) in relation to another enterprise means an enterprise:

- which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise; and
- in respect of which, one or more persons who participate, directly or indirectly, or through one or more intermediaries, in its management or control or capital, are the same persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise.

Further, the Act prescribes 13 situations where two or more enterprises are considered as AEs.

Specified Domestic Transactions
AEs for the purpose of SDT, are as follows:

- Expense with directors/partner/member, subsidiaries or entities in which the taxpayer directly or through its directors of a company/partner/member in case of a corporate or their relatives have substantial interest in an entity;
- For entities claiming certain specified tax holidays/ exemptions benefit, any closely connected entity.

Methodologies
The arm's length price (ALP) in relation to an international transaction and SDT is required to be determined by any of the following methods:

- Comparable uncontrolled price method (CUP)

[6] The limit is applicable from FY 2015-16. Earlier, the limit was USD 0.75 mn (INR. 50 mn)

- Resale price method (RPM)
- Cost plus method (CPM)
- Profit split method (PSM)
- Transactional net margin method (TNMM)
- Any other method as prescribed

The TP regulations do not prescribe any priority criteria in terms of selection/application of methods.

Arm's length price (ALP)

The ALP means price charged or would have been charged for a transaction between independent parties under similar situation. The TP regulation prescribes the use of either range concept (35th to 65th per centile) or arithmetic mean depending on the method applied and number of comparables selected.

Compliance requirement

Compliance requirement	Due date of submission
Obtain accountant's report in Form 3CEB Accountant's report is a brief summary of international transaction(s) and SDT **along** with the method used to justify the **arm's length** nature. **This document is to be certified by a Chartered Accountant or a firm of Chartered Accountants**	**30 November** of each **Assessment Year** for international transactions or SDT undertaken during the relevant financial year (April – March)
TP documentation (TP Study) TP study is a detailed documentation (requirements are in line with the OECD guidelines) relating to international transaction(s) or SDT which is used to justify their **arm's length** nature. This documentation is to be maintained, and updated on an annual basis, if the aggregate value of the **international transaction(s) entered by the enterprise exceeds USD 0.1 mn (INR 10 mn)**	Enterprise is required to maintain **contemporaneous documentation** and needs to submit documentation on **request by the Income-tax department**

Country-by-Country reporting

In order to meet the commitment to Base Erosion and Profit Shifting ('BEPS') initiative of G-20 and the 'OECD', a new section has been inserted in the Act which mandates the requirement of country-by-country ('CbC') reporting in line with Action 13 of the BEPS action plans. However, detailed rules on the same are awaited.

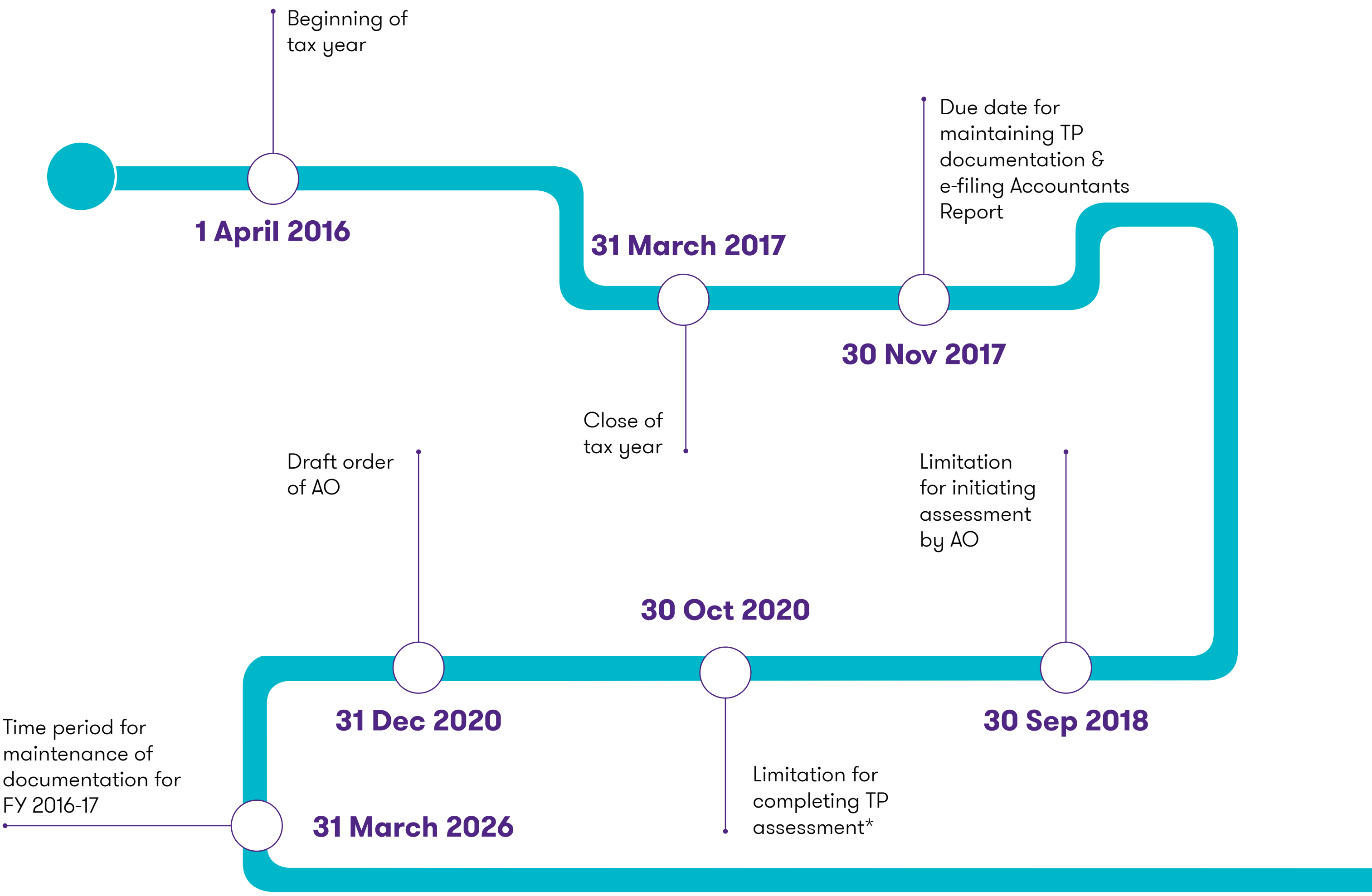
These regulations require an Indian entity which is part of a Multinational Enterprise ('MNE') group, to maintain the following group information by way of three files (in addition to the information already required in relation to international transactions):

- Master File
- Local file
- CbC reporting is required to be filed by the parent entity of an MNE group with annual consolidated group revenue in the immediately preceding accounting year of more than € 750 mn (INR 53.95 bn, USD 807.78 approx.)

The CbC report for FY 2016-17 would need to be filed by 30 November 2017.

[7] OECD Transfer Pricing guidelines for Multinational Enterprises & Tax Administrations, July 2010

Compliance timelines



Safe Harbour Rules

'Safe harbour' is defined as the circumstances in which the income-tax authorities shall accept the transfer price that is declared by the assessee. Safe harbour rules are effective in India from the financial year 2012-13, and are available for a period of three years. At present, safe harbour rules have been prescribed for the following transactions:

- Provision of Software development services
- Provision of IT enabled services
- Providing corporate guarantee
- Contract R&D services relating to software development
- Manufacture and export of core auto components
- Manufacture and export of non-core auto components
- Low value adding intra group services

Penalty provisions

Penalty provisions for following non-compliances have been prescribed by the Act:

- Underreporting and misreporting of income
- Failure to maintain statutory TP documents
- Failure to report a transaction in accountant's report
- Failure to furnish master file
- Failure to furnish accountant's report

Transfer Pricing Audit

Transfer pricing audit is conducted by the Transfer Pricing Officer (TPO), a specialised officer from the revenue department. If the regular Assessing Officer (AO) of a taxpayer considers it necessary or expedient so to do, he may with the previous approval of the Commissioner, refer to the computation of the ALP in relation to the international transactions or SDT of the taxpayer to the TPO.

The taxpayer has the option of approaching the dispute resolution panel or filing appeal before the commissioner of income tax (appeals).

Safe harbour rules and APA are dispute avoidance mechanisms and MAP is dispute resolution mechanism. Change alignment accordingly.

Advance pricing agreement

The advance pricing arrangement (APA) programme was introduced in the Indian TP Regulations in 2012. Under the APA scheme available from FY 2013-14, any person can enter into an agreement with the board, after the approval of the central government, for determining the ALP or for specifying the manner in which the ALP is to be determined in relation to an international transaction to be entered into by that person.

APA can be entered in relation to an international transaction only. The APA can be unilateral, bilateral or multilateral.

In 2014, roll-back provisions were introduced in the Indian APA scheme, which enable persons entering into an APA to roll-back the results of the APA to a period not exceeding four preceding years from the year from which the APA is proposed to be applicable.

Mutual agreement procedure

In order to avoid double taxation, mutual agreement procedure (MAP) has proved to be an effective method where the revenue authorities of two different nations try to resolve a dispute together.

Under MAP, an agreement, which seeks to avoid economic double taxation or conflicting taxation, would be reached between the tax authorities. Also, under MAP, disputes are resolved through competent authorities (CAs) of the contracting states.

Glossary of Abbreviations

CSO: Central Statistics Office

GST: Goods and Services Tax

DIPP: Department of Industrial Policy & Promotion

USFDA: US Food and Drug Administration

FIPB: Foreign Investment Promotion Board

APA: Advance Pricing Arrangement

REIT: Real Estate Investment Trust

FEMA: Foreign Exchange Management Act

NBFC: Non-Banking Financial Company

SEBI: Securities and Exchange Board of India

CBDT: Central Board of Direct Taxes

ROR: Resident and Ordinarily Resident

RNOR: Resident and Non-Ordinarily Resident

MAT: Minimum Alternate Tax

AMT: Alternate Minimum Tax

ICDS: Income Computation and Disclosure Standards

GAAR: General Anti-Avoidance Rules

BCD: Basic Customs Duty

CD: Countervailing Duty

TP: Transfer Pricing

TPO: Transfer Pricing Officer

AO: Assessing Officer

SDT: Specified Domestic Transaction

RBI: Reserve Bank of India

FEMA: Foreign Exchange Management Act 1999

Fintech: Financial Technology

CAGR: Compound annual growth rate

USFDA: United States Food and Drug Administration

IT & ITeS: Information technology & Information Technology Enabled Services

REIT: Real Estate Investment Trust

AoP: Association of Persons

Acknowledgements

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