I. Establishing and Running a Business
II. Tax and Accounting in India
III. Human Resources and Payroll Considerations
Annual Subscription 2015

India Briefing Magazine will be published six times in 2015. Its content covers foreign direct investment, legal, tax, financing, cost and operational issues across India. Written in-house by professionals in Indian law, tax and compliance based in India, India Briefing is the ideal starting point for CEOs and CFOs considering India as an investment destination.

Disclaimer

Contributors to and editors of this guide include the staff and consultants at Dezan Shira & Associates India and India Briefing. This guide was designed by Jessica Huang.

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Preface

As a destination for foreign direct investment (FDI), India is looking better now than ever before. A perceived high level of risk has previously limited its ability to attract foreign businesses, but with a slew of new policies implemented in 2014, India is now perfectly positioned to compete with the world’s premier investment locations.

India can offer investors a unique array of advantages. Its skilled and low-cost labor force is one of the largest in the world, and it has a high level of English fluency relative to other countries in Asia. The reforms that have been implemented are numerous and include infrastructural improvements, the raising of FDI caps, and the simplification of visa obtainment procedures.

This publication, designed to introduce the fundamentals of investing in India, was created at the close of 2014 using the most up-to-date information at the time. It was compiled by Dezan Shira & Associates, a specialist foreign direct investment practice that provides corporate establishment, business advisory, tax advisory and compliance, accounting, payroll, due diligence and financial review services to multinationals investing in emerging Asia.
About Dezan Shira & Associates

At Dezan Shira & Associates, our mission is to guide foreign companies through Asia's complex regulatory environment and assist them with all aspects of establishing, maintaining, and growing their business operations in the region. With over 20 years of on-the-ground experience and a large team of professional advisers, we are your reliable partner in Asia. Since its establishment in 1992, Dezan Shira & Associates has grown into one of Asia’s most versatile full-service consultancies with offices across China, Hong Kong, India, Singapore, and Vietnam, as well as liaison offices in Italy, Germany, and the United States, and partner firms across the ASEAN region.

In our continued effort to provide legal, tax and audit advisory services in multiple Asian jurisdictions, Dezan Shira & Associates has selected local practices with strong capabilities to be part of the Dezan Shira Asian Alliance. In coordination with our Alliance member-firms, Dezan Shira & Associates will now be able to provide global multinational companies pan-Asian advisory services.
Dezan Shira & Associates India

Dezan Shira & Associates expanded into India in 2007, opening offices in Mumbai and later New Delhi in 2008. The launch of Dezan Shira’s India offices was coupled with the launch of India Briefing, which is now a premier source of business and regulatory intelligence related to the Indian market.

Our services in India include corporate establishment, business advisory, tax advisory and compliance, accounting, payroll, due diligence, and financial review. Dezan Shira & Associates’ experienced business professionals in India are committed to improving your understanding of investing and operating in emerging Asian markets.

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Adam Livermore
Managing Partner
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Contents

1. Establishing and Running a Business
   - What are my options for investment?
   - Setting up a Wholly Foreign-Owned Business in India
   - Navigating FDI Caps and Restrictions

2. Tax and Accounting in India
   - Key Taxes in India
   - India’s Audit Process

3. Human Resources and Payroll Considerations
   - Key Considerations when Hiring Staff
   - Payroll and Social Insurance
I. Establishing and Running a Business

1.1 What are my Options for Investment?
1.2 Setting up a Wholly Foreign-Owned Business in India
1.3 Navigating FDI Caps and Restrictions
1.1 What are my Options for Investments?

Prospective companies and investors seeking to take advantage of India’s liberalized FDI caps must carefully consider their options for investment in the country and the available avenues for establishing a business presence.

Here, we outline the functions and requirements for three entities that can be established when a business enters India or expands its scope of operations. We discuss the following:

1) Liaison Offices
2) Branch Offices
3) Project Offices
1.1.1 Liaison Offices

Foreign companies can open a liaison office in India to facilitate and promote the parent company’s business activities and act as a communications channel between the foreign parent company and Indian companies. Unable to engage in commercial, trading, or industrial activities, liaison offices must be sustained by private, inward remittances received from their foreign parent company.

A liaison office is permitted to engage in the following activities:

- Facilitate communication between the overseas head company and parties in India
- Promote imports/exports between countries
- Establish financial and technical cooperation between overseas and Indian companies
- Represent the overseas head company in India

The Foreign Exchange Management Act (FEMA) governs the application and approval process for the establishment of a liaison or branch office. Under the Act, foreign enterprises must receive specific approval from the RBI to operate a liaison office in the country. Applications are to be submitted through Form FNC (Application for Establishment of Branch/Liaison Office in India). The approval process generally takes 20 to 24 weeks and permission to operate a liaison office is granted for a three-year period, which can be extended at a later date.

Additionally, an enterprise must also meet the following conditions before qualifying for the establishment of a liaison office:

- Must have a three-year record of profitable operations in the home country
- Must have a minimum net worth of US$ 50,000 verified by the most recent audited balance sheet or account statement

If a company does not meet these requirements, but a subsidiary of the company does, the parent company may submit a Letter of Comfort on the subsidiary’s behalf. A company must submit a Certificate of Incorporation or Memorandum & Articles of Association, and a copy of the parent company’s latest audited balance sheet. The liaison office must also obtain a Permanent Account Number (PAN) from the Income Tax Authorities.
Within 30 days of establishment, the liaison office must register with the Registrar of Companies (RoC) by filing Form 44 through the Ministry of Corporate Affairs’s online portal. The following documents must also be provided:

- A copy of the liaison office charter or Memorandum & Articles of Association in English
- Full address for the enterprise’s principal place of operation outside of India
- Name and address of the liaison office in India
- List of directors
- Name and address of the company’s official representative based in India (e.g. the person authorized to accept delivery of notices and documents served to the company)

Each year, the liaison office must file an Annual Activity Certificate (AAC), prepared by a chartered accountant, to the RBI verifying the office’s activities are within its charter. An AAC should also be filed with the Directorate General of Income Tax within 60 days of the close of the financial year.
1.1.2 Branch Offices

Foreign companies, including those engaged in manufacturing and trading activities, are able to establish branch offices to carry out business activities substantially the same as those carried out by their parent company. Branches are permitted to carry out trading activities, but may not engage in manufacturing activities on their own—these may be subcontracted to Indian manufacturers. Branch offices operating in SEZs, however, are permitted to undertake manufacturing and service activities in sectors with 100 percent FDI approval.

Branch offices are permitted to engage in the following activities:

- Export/import of goods
- Rendering professional or consultancy services, IT services, or technical product support
- Carrying out research work
- Representing the parent company as a buying/selling agent or in order to establish technical or financial collaborations with Indian companies
- Operating as a foreign airline or shipping company

* Can manufacture if in SEZ with 100 percent FDI

Shilpa Goel
Associate
Business Advisory Services
Dezan Shira & Associates
New Delhi Office

“For foreign companies wanting to either import products into or procure goods from India, a branch office is an excellent option. BOs are able to import and export, receive payment in INR and, if established in an SEZ, can even manufacture goods themselves.”
The FEMA also governs the application and approval process for the establishment of a branch office, requiring that companies receive approval from the RBI. Permission to operate a branch office is granted for a three-year period, which can be extended at a later date. An enterprise must also meet the following conditions before qualifying for the establishment of a branch office:

- Must have a five-year record of profitable operations in the home country
- Must have a minimum net worth of US$100,000 verified by the most recent audited balance sheet or account statement

If a company does not meet these requirements, but is a subsidiary of a company that does, the parent company may also submit a Letter of Comfort on the subsidiary’s behalf during the application process. The process for establishing a branch office is identical to that required for a liaison office, and the same documents including Form FNC, the Certificate of Incorporation or Memorandum & Articles of Association, and an audited balance sheet must be submitted. A PAN must also be acquired, and the office must register with the Registrar of Companies through the Ministry of Corporate Affairs’ online portal.

Each year, the branch office must file an AAC, prepared by a chartered accountant, to the RBI verifying the office’s activities were within its charter. An AAC should also be filed with the Directorate General of Income Tax within 60 days from the end of the financial year. All profits earned by the branch office may be remitted from India, and will be subject to payment of all applicable taxes.
1.1.3 Project Offices

If a foreign company has secured a contract from an Indian company to execute a project in India and has attained the appropriate funding source or governmental clearance, a project office may be established. One of the following criteria must be met in order to obtain permission to establish a project office:

• The project is funded directly by inward remittance from the overseas head company
• The project is funded by a bilateral or multilateral international financial agency such as the World Bank or IMF
• The project has received clearance by the relevant authorities within India
• The Indian company awarding the contract has received a term loan for the project

If none of the above criteria are met, an overseas company looking to establish a project office in India must make a specific request with the Central Office of the RBI for approval.

The project office should notify the relevant regional Director General of Police within five days of the office’s establishment. Within two months the overseas company must also submit a report to the relevant regional office of the RBI through the authorized dealer branch bank (AD) that will be used by the foreign company. This report should include:

• Name and address of the overseas company
• Reference number and date of project contract
• Particulars of the authority awarding the project contract
• Total amount of the contract
• Brief details of both the project undertaken and authorized dealer branch bank
• Project details, including project office tenure and contact Information

Each year, the project office will be required to submit a Project Status report compiled by a chartered accountant to the company’s AD branch. This report ensures the activities undertaken by the project office conform with the activities permitted by the RBI.

Project offices may open a non-interest bearing foreign currency banking account with an authorized dealer branch in India for project expenses and credits. The office may maintain both a foreign currency account and a rupee account while operating in India. Project offices are allowed occasional remittances to their parent companies and must provide a chartered accountant certificate verifying the offices can still meet their liabilities. Following project completion, the project office may repatriate any capital surplus once all tax liabilities have been paid, a final audit of the project accounts has been completed, and a document verifying the remittable surplus provided.
1.2 Setting up a Wholly Foreign-Owned Business in India

1.2.1 Establishing a Wholly Owned Subsidiary

Under Indian law, foreign investors are able to establish wholly owned subsidiary companies (WOS) in the form of private limited companies if they operate in sectors that permit 100 percent foreign direct investment (FDI). With India’s recent loosening of FDI caps, companies are now also able to establish WOS in the telecom services and asset reconstruction sectors. Establishing a private limited company can be a lengthy and complicated process involving multiple steps.

First, a minimum of two directors must be appointed and registered through India’s e-filing system for Director Identification Numbers (DIN). Minimum requirements for the establishment of a private limited company include the existence of two directors, two shareholders (who may be the same person as the directors), and a minimum share capital of INR 100,000 (1 Lakh).

Second, a suitable name must be selected that indicates the main objectives of the company, and submitted with the RoC along with a brief description of the business’s proposed functions to verify both the name’s appropriateness and availability. Upon successful name registration, the applicant company has 60 days to file its Memorandum of Association (MOA) and Articles of Association (AOA), and proceed with formal incorporation filings. Both the MOA and AOA must be stamped with the appropriate duty after the needed RoC fees and stamp duty have been paid, and both forms signed by at least two subscribers with a witness.

Within this 10-day time window, the following documents must also be filed with the Ministry of Corporate Affairs web portal along with the requisite filing fees:

- Form 1 - Application for incorporation along with the MOA and AOA
- Form 18 - Notice of situation for the registered office (proof of address, etc.)
- Form 32 - Details of the company’s board of directors

Upon successful submission of the above documents, the RoC will issue a Certificate of Incorporation and a Corporate Identification Number (Corporate Identity). The process generally takes 7 to 8 weeks to complete, and private limited companies are permitted to commence business immediately following their successful incorporation.
Applicable Taxes
While India has been liberalizing its governing policies since 1991, the country’s tax structure remains among the most complex and difficult to navigate in the world. Understanding the wide variety of laws, regulations and procedures can be confusing for even the savviest of business operators. Foreign companies that do not seek specialized advice often end up overpaying on taxes or on the associated penalties and interest that go along with them. What follows is a brief description of the various taxes which should be taken into consideration when incorporating a private limited WOS company in India.

<table>
<thead>
<tr>
<th>Type of Company</th>
<th>Taxable Income Below INR 10 Million</th>
<th>Exceeds INR 10 Million</th>
<th>Exceeds INR 100 Million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Domestic company</td>
<td>30%</td>
<td>32.45% (30% plus surcharge of 5%, plus education cess of 3%)</td>
<td>33.99% (30% plus surcharge of 10%, plus education cess of 3%)</td>
</tr>
<tr>
<td>Foreign company</td>
<td>40%</td>
<td>42.02% (40% plus surcharge of 2%, plus education cess of 3%)</td>
<td>43.26% (40% plus surcharge of 5%, plus education cess of 3%)</td>
</tr>
</tbody>
</table>

Tax on the Distribution of Dividends
Corporate entities are subject to a tax on the distribution of dividends. However, in the case of shareholder dividends, the associated income is exempt from tax. The current effective rate of the Dividend Distribution Tax is 16.995 percent (15 percent plus a 10 percent surcharge and an education cess of 3 percent). No exemption from payment of the DDT is granted for the profits relating to SEZ developers.

To avoid a situation of double taxation being created by the DDT, it is permitted that, for the purpose of computing the tax, any dividend received by a domestic company during any financial year from its subsidiary shall be allowed to be deducted from the dividend to be distributed. This is provided the dividend received by the domestic company has been subject to DDT and the domestic company is not the subsidiary of any other company.
Minimum Alternate Tax
All companies declaring low or zero profits are subject to the Minimum Alternate Tax (MAT). Presently, MAT is levied at 18.5 percent of book profits plus the applicable surcharges and education cess. The MAT is levied on companies whose tax payable under normal income tax provisions is less than 18.5 percent of book profits. Additionally, MAT is applicable to SEZ developers/units for income arising on or after April 1, 2012.

Taxation of Royalties/Technical Fees
Under domestic tax law, the royalties/technical fees that are payable to non-residents with a permanent establishment in India are taxed on a different basis compared to non-residents without permanent establishment in India. Concessional tax rates apply if the agreement relates to a matter that has been approved by the government of India. The payments made are subject to tax avoidance agreements entered into by the non-resident’s country.

Wealth Tax
Wealth tax is calculated on March 31st of every year (referred to as the valuation date). Wealth tax is charged to both individuals and companies at the rate of 1 percent of the amount by which the “net wealth” exceeds INR 3,000,000.

The term “net wealth” is basically defined as the excess value of certain assets over accumulated debt. Assets include guest and residential houses, motorcars, jewelry/bullion/utensils of gold and silver, yachts, boats, aircraft, urban land and cash in hand. A debt is an obligation to pay a defined sum of money arising from the assets included in “net wealth.”

For information on the indirect taxes that a company will encounter in India, see our Tax and Accounting in India section.
1.3 Navigating FDI Caps and Restrictions

Amendments in Indian FDI policy last year opened a number of key business sectors to increased foreign investment and, in several instances, eliminated the need for foreign investors to obtain approval from the Indian government before investing. These amendments have been further augmented this year, with several sectors significantly increasing the amount of foreign investment permitted. Additional 2013 policy changes that alter the legal definition of 'control' as pertaining to the determination of sectorial caps, as well as regulations for single and multi-brand retail trading, are also important for foreign institutional investors (FII) and firms considering foreign direct investment.

1.3.1 FDI Routes and Forms

Foreign investment into India falls under one of two FDI routes:

- **Government Route:** For investment in business sectors requiring prior approval from the Foreign Investment Promotion Board (FIPB).
- **Automatic Route:** For investment in business sectors that do not require prior approval from the government, but the filing of a notification after the incorporation of the company and issue of initial shares.

Foreign investment takes one of two principal forms:

- **Foreign Direct Investment (FDI):** The acquisition of shares or other securities in an Indian company.
- **Foreign Institutional Investment (FII):** Investment by foreign institutional investors (such as hedge funds, insurance companies, or mutual funds) registered with the Securities and Exchange Board of India (SEBI).

These distinctions are important when interpreting recent changes in foreign investment policy, as FDI caps and approval routes often vary by both industry and investor.

### Unchanged FDI Caps

<table>
<thead>
<tr>
<th>Sector/Industry</th>
<th>Investment Cap</th>
</tr>
</thead>
<tbody>
<tr>
<td>Civil Aviation</td>
<td>49%</td>
</tr>
<tr>
<td>Defense</td>
<td>26%</td>
</tr>
<tr>
<td>Airports</td>
<td>74%</td>
</tr>
<tr>
<td>Print Media</td>
<td>26%</td>
</tr>
<tr>
<td>Brownfield Pharmaceuticals</td>
<td>100%</td>
</tr>
<tr>
<td>Multi-Brand Retail</td>
<td>51%</td>
</tr>
</tbody>
</table>
1.3.2 Changes to FDI Caps and Approval Routes

2013’s FDI amendments are now being further augmented under the new Narendra Modi administration, with several sectors significantly increasing the amount of foreign investment permitted. Of particular interest are the hikes that will be seen in the insurance and railway sectors; the former rising from 26% to 49%, and the later from 0% to a massive 100%.

Once these new policies are fully implemented, India’s revised list of FDI caps will look something like this:

<table>
<thead>
<tr>
<th>Sector/Industry</th>
<th>Pervious Policy</th>
<th>2014 Revised Policy</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Investment Cap</td>
<td>Approval Route</td>
</tr>
<tr>
<td>Commodity Exchanges</td>
<td>49% (FDI + FII)</td>
<td>Government</td>
</tr>
<tr>
<td></td>
<td>FDI Cap: 26%</td>
<td></td>
</tr>
<tr>
<td>Power Exchanges</td>
<td>49% (FDI + FII)</td>
<td>Government</td>
</tr>
<tr>
<td></td>
<td>FDI Cap: 26%</td>
<td></td>
</tr>
<tr>
<td>Asset Reconstruction</td>
<td>74% (FDI + FII)</td>
<td>Government</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Insurance</td>
<td>26% (FDI)</td>
<td>Automatic</td>
</tr>
<tr>
<td>Telecom Services</td>
<td>Up to 49%</td>
<td>Automatic</td>
</tr>
<tr>
<td></td>
<td>Above 49% and up to 74%</td>
<td>Government</td>
</tr>
<tr>
<td>Courier Services</td>
<td>100%</td>
<td>Government</td>
</tr>
<tr>
<td>Test Marketing</td>
<td>100%</td>
<td>Government</td>
</tr>
<tr>
<td>Petroleum Refining by Public Sector Undertakings</td>
<td>49%</td>
<td>Government</td>
</tr>
<tr>
<td>Defense Production</td>
<td>26% (FDI)</td>
<td>Government</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Railways</td>
<td>N/A</td>
<td></td>
</tr>
</tbody>
</table>
Changes in the Definition of ‘Control’
A changed definition of control is also expected to apply to FDI in sectors where a sectorial cap currently exists. Prior to the 2013 amendments, companies were considered to be ‘controlled’ by resident Indian citizens if Indian citizens held a 51 percent stake in the firm and had the power to appoint a majority of directors in that company.

Under the broadened definition of control introduced this year, ‘control’ now includes not only the power to appoint a majority of directors, but also the ability to control the management or policy decisions via shareholding, management rights, shareholder agreements, or voting agreements. Indian citizens must exercise ‘control’ under all limbs of this new definition for a company to be considered domestically controlled.

Consequently, companies previously considered to be ‘Indian’ may now be viewed as foreign controlled and subject to FDI caps and other restrictions on downstream investment.

Changes in Single and Multi-Brand Retail Trading
While previous FDI policy only permitted one non-resident entity with ownership of a brand (or rights to a brand) to invest in Indian companies engaged in the retail trading of that brand, policy changes now allow multiple non-resident entities to invest in Indian entities engaged in single-brand retail trading of that brand (as long as each own or have rights to the brand via a legally binding agreement).

<table>
<thead>
<tr>
<th>Single-Brand Retail Trading</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Former Position</strong></td>
</tr>
<tr>
<td>**Cap</td>
</tr>
<tr>
<td>100%</td>
</tr>
<tr>
<td>Above 49% and up to 100%</td>
</tr>
</tbody>
</table>

In respect to multi-brand retail trading, changes made in 2012 permitted up to 51 percent FDI with prior government approval. Conditions for investment, however, required companies to invest at least 50 percent of the total FDI proceeds into ‘back-end infrastructure’ such as manufacturing, processing, packaging and distribution. Changes made in 2013 now clarify that at least 50 percent of the first US$100 million invested must be in ‘back end infrastructure.’

Furthermore, the previous requirement for multi-brand retail trading companies (MBRTCs) regarding manufacturing and processing 30 percent of products in ‘small industries’ has been discontinued, and companies are now permitted to source their products from any manufacturing or processing entity so long as investment in plant and machinery is below US$2 million at the first engagement. MBRTCs are now also allowed to establish outlets in a wider range of locations, as the previous restriction to cities with populations of at least 1 million has been scaled back. State governments now possess the authority to permit MBRTCs to operate in their region.
1.3.3 Investing

The issuance of shares by Indian companies falls under the compliance guidelines outlined in the Foreign Exchange Management Act (FEMA). Companies seeking capital through the public route should base the issuance price on SEBI guidelines. Unlisted companies seeking capital may not issue private shares at a price less than fair value based on the discounted cash flow method, and price will be determined by a SEBI registered merchant or chartered accountant. The acquisition of unlisted shares by a non-resident from an Indian resident must be exchanged at market price based on the SEBI guidelines.

Units operating in SEZs may issue shares at a price based on the valuation against the import of capital goods. This valuation must receive approval from a Development Commissioner Committee and the appropriate customs officials. Shares must be officially issued within 180 days of receipt of invested capital, or the funds must be refunded to investors.

Upon the issuance of shares to foreign investors, the issuing company has 30 days to file Form FC GPR, which outlines the company's activities and relevant details, through the appropriate regional office of the RBI. A certificate declaring compliance with the Companies Act 1956 and Companies Act 2013, as applicable from time to time, shall be submitted at the same time. The issuing company shall also obtain a certificate confirming the price of issue is in line with the prescribed guidelines.

Possible Changes for this Year

Hikes in the FDI caps for defense, insurance and railways are all recent and are still in the process of being formally implemented. The Indian government has also recently announced that its construction sector, where 100 percent FDI is already permitted, will be further liberalized with a relaxation of minimum capitalization and minimum built-up area conditions.

A number of other changes in FDI caps have also been hinted at for the near future, with suggestions that the government may move to liberalize business-to-consumer e-commerce. In bonds, the government may transition from a fixed ceiling on FDI in government securities to link limits to proportion of GDP.

Whatever the changes, foreign investors should be familiar with Indian investment regulations and compliance requirements before moving to invest in regulated sectors. Despite India's liberalized investment environment, the nation still ranks among the most difficult countries in which to start and conduct business according to the World Bank. As such, firms and individuals considering investment in the country should strongly consider consulting a professional services firm before attempting to navigate India's foreign investment environment.
2. Tax and Accounting in India

2.1 Key Taxes in India
2.2 India’s Audit Process
2.1 Key Taxes in India

2.1.1 Value Added Tax

India has a Federal structure of taxation. The graphic below provides a description of the existing administration.

The Central Sales Tax imposes a tax on manufacturing, and the state government imposes a tax on the selling and distribution of goods. Hence, the manufacturer and service provider pay excise duty and service tax and claim credit for the same at the time the goods are sold to manufacturers under the nomenclature of CENVAT Credit (i.e. Centralized Value Added Tax), and the dealer pays VAT and claims VAT credit.

Value Added Tax (VAT) is a tax on the final consumption of goods or services, and is ultimately borne by the consumer. It is a multi-stage tax with the provision to allow Input Tax Credit (ITC) on tax at an earlier stage, which can be appropriated against the VAT liability on subsequent sale. This credit means setting off the amount of input tax by a registered dealer against the amount of output tax. It is given for all manufacturers and traders for the purchase of inputs/supplies meant for sale, irrespective of when these will be utilized/sold. The VAT liability is calculated by deducting input tax credit from tax collected on sales during the month. If the tax credit exceeds the tax payable on sales in a month, the excess can be carried over to the end of the next financial year. If there is any balance excess or unadjusted input tax credit at the end of second year, then the same shall be eligible for refund.

“An overseas company is not liable to register for VAT in India unless it has an office in India which is engaged in the sale of goods. However, there is no restriction on overseas companies applying for voluntary registration.”

Chris Devonshire-Ellis
Founding Partner
Dezan Shira & Associates
VAT is managed exclusively by respective states. The state governments, through taxation departments, carry out the responsibility of levying and collecting VAT. The central government plays the role of facilitator for the successful implementation of VAT.

Every dealer of goods and commodities is required to register under the relevant state act as applicable according to their area of operation. The limit for the threshold is set by the states and may vary between them from INR 1,000,000 (US$16,900) to INR 1,500,000 (US$25,300). Further, the premise of availing the tax credit for any amount of VAT paid is based on the issue of an invoice. An invoice plays a pertinent role in the functioning of the VAT system as it aids in substantiating the VAT claim during subsequent sales. The entire system of claiming input tax credit is crucially based on the documentation of a tax invoice or bill. Mandatory to follow, this tax invoice is to be signed and dated by the dealer, showing the requisite particulars.

For identification/registration of dealers under VAT, the tax payer’s Tax Identification Number (TIN) is used. TIN consists of 11 digits with its first two characters representing the state code and the set-up of the next nine characters varying by state.

Presently, there are two basic rates of VAT (four percent and 12.5 percent). There is also an exempt category and a special rate of 1 percent for a few select items. Gold, silver, and precious stones, for example, have been put in the 1 percent schedule. VAT paid on items such as motor spirit (petrol, diesel and aviation turbine fuel), liquor, etc. are not eligible for offsetting VAT payment.

Some of the other VAT features at the state level are:

- State taxes on the purchase or sale of goods subsumed in VAT, not excluding Entry Tax.
- A provision for allowing Input Tax Credit (ITC) which is the basic feature of VAT.
- An intra-state transaction does not cover inter-state sales transactions (i.e. credit for VAT paid within the state shall not be allowed on inter-state purchases).
- Items destined for export have been made zero-rated by giving credit for all taxes on inputs/purchases related to such exports.
- The procedure for the VAT system is favorable for businesses as it provides for self-assessment by dealers. Further, there is a provision for introducing a threshold limit for the registration of dealers when annual turnover is INR 10 lakhs (US$16,850) and a provision for the composition of tax liability up to an annual turnover limit of INR 50 lakhs (US$84,300). It should also be noted that no credit is available on the basis of invoices provided by unregistered dealers or to those opting for the composition scheme.
**VAT Procedure**

- Input VAT - Payable on goods and services purchased from another dealer.
- Output VAT - Payable on goods and services rendered.

<table>
<thead>
<tr>
<th>Manufacturer</th>
<th>Supplier</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods and Service purchased</td>
<td>Input VAT payable</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Dealer</th>
<th>Customer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods and Service sold</td>
<td>Output VAT payable</td>
</tr>
</tbody>
</table>

\[
\text{VAT payable} = \text{Output VAT} - \text{Input VAT}
\]
### Example 1

A registered dealer under VAT affects purchases and sales, both locally, in a year

<table>
<thead>
<tr>
<th>Input</th>
<th>Output</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exempted goods</td>
<td>Exempted goods</td>
</tr>
<tr>
<td>200,000</td>
<td>150,000</td>
</tr>
<tr>
<td>Goods taxable at 4%</td>
<td>Goods taxable at 4%</td>
</tr>
<tr>
<td>300,000</td>
<td>180,000</td>
</tr>
<tr>
<td>Goods taxable at 12.5%</td>
<td>Goods taxable at 12.5%</td>
</tr>
<tr>
<td>800,000</td>
<td>670,000</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>TOTAL</strong></td>
</tr>
<tr>
<td>1,300,000</td>
<td>1,000,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Input Tax Credit</th>
<th>Output Tax Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exempted goods</td>
<td>Exempted goods</td>
</tr>
<tr>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Goods taxable at 4%</td>
<td>Goods taxable at 4%</td>
</tr>
<tr>
<td>12,000</td>
<td>7,200</td>
</tr>
<tr>
<td>Goods taxable at 12.5%</td>
<td>Goods taxable at 12.5%</td>
</tr>
<tr>
<td>100,000</td>
<td>83,750</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>TOTAL</strong></td>
</tr>
<tr>
<td>112,000</td>
<td>90,950</td>
</tr>
</tbody>
</table>

#### VAT Payable

| Output VAT payable          | 90,950                        |
| Input VAT available         | 112,000                       |
| VAT payable                 | NIL                           |
| VAT credit carried forward  | 21,050                        |

### Example 2

A registered dealer under VAT affects purchases and sales, both locally and inter-state, in a year

<table>
<thead>
<tr>
<th>Input</th>
<th>Output</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exempted goods</td>
<td>Exempted goods</td>
</tr>
<tr>
<td>200,000</td>
<td>150,000</td>
</tr>
<tr>
<td>Goods taxable at 4%</td>
<td>Goods taxable at 4%</td>
</tr>
<tr>
<td>200,000</td>
<td>180,000</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>330,000</strong></td>
</tr>
</tbody>
</table>

#### VAT Payable

- No liability under VAT Act, since total turnover under VAT Act is less than Rs 5 lakhs
- **OUTPUT (CST)**
  - Goods taxable at 4% - 150,000
  - (with form C)

The dealer is liable under the CST Act irrespective of total turnover under the VAT Act. There is no liability under the VAT Act, but the dealer can avail input tax credit for liability under the CST Act.

<table>
<thead>
<tr>
<th>Input Tax Credit (Under VAT)</th>
<th>Output Tax Credit (Central Sales Tax)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exempted goods</td>
<td>Exempted goods</td>
</tr>
<tr>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Goods taxable at 4%</td>
<td>CST due</td>
</tr>
<tr>
<td>8,000</td>
<td>6,000</td>
</tr>
<tr>
<td>Goods taxable at 12.5%</td>
<td>Adjustment from Input Tax credit</td>
</tr>
<tr>
<td>100,000</td>
<td>6,000</td>
</tr>
<tr>
<td>Input Tax Credit (to be carried over to next month): 2000</td>
<td>CST payable</td>
</tr>
</tbody>
</table>
2.1.2 Service Tax

A tax on services was put into effect in India for the first time in 1994. With the initial imposition of only 3 services, over the years various other services have been added raising the count to 119 in the year 2011. The basic premise of imposing a service tax is that the manufacturing sector can only be taxed to a certain extent on specified activities while fostering healthy competition. Presently, services form more than 57 percent of India’s GDP, and are expected to reach around 70 percent. This tax will be subsumed into the Goods and Services Tax, which is expected to be in place in the near future. The regulatory provisions pertaining to service tax are given in Chapter V and V(A) of the Finance Act 1994. The levy of the service tax extends to the whole of India except that it does not extend to a service provider offering taxable services from the state of Jammu and Kashmir by virtue of section 64, Chapter V, of the Finance Act.

A new service tax regime was introduced in India’s 2012 budget, under which all services are taxed, with services specified under the negative list entry otherwise exempted. The CBEC also issued a notification in June 2012, commonly referred to as the ‘Mega Exemption Notification’ enumerating the services which shall be exempt from the payment of service tax with effect from July 2012. Earlier there were numerous notifications and litigations challenging the service tax. The present rate of service tax is 12 percent, and EC and SHEC of 1 percent and 2 percent shall be charged to the existing rate. The negative list of services signifies that all services, excluding those specified by the negative list, will be subject to service tax. Additionally, there will be exemptions, abatements, and composition schemes as issued by the CBEC from time to time.

Procedure for Service Tax Registration

1. Filing the Service Tax registration form (Form ST – 1) online
2. Generation of acknowledgement
3. Arrangement of relevant documents
4. Submission of documents with jurisdictional officer
5. Verification of documents by the jurisdictional officer
6. Award of certificate of registration
The Mega Exemption Notification mentions 38 services on which service tax can be exempted, thereby including all other services. A simplistic approach has been laid out that services which are not mentioned in the negative list will attract service tax liability. Services covered in the negative list category are as follows:

1) Health care services by a clinical establishment, an authorized medical practitioner, or paramedics

2) Services provided by an individual as an advocate or a partnership firm of advocates by way of legal services to:
   » An advocate or partnership firm of advocates providing legal services
   » Any person other than a business entity
   » A business entity with a turnover up to INR 10 lakh (US$16,600) in the preceding financial year

3) Services provided to a recognized sports body by:
   » An individual as a player, referee, umpire, coach, or team manager for participation in a sporting event organized by a recognized sports body
   b) Another recognized sports body

4) Auxiliary educational services and renting of immovable property by educational institutions

5) Services by way of training or coaching in recreational activities related to arts, culture, or sports

6) Temporary transfer, or permitting the use or enjoyment, of a copyright relating to original literary, dramatic, musical, artistic works, or cinematograph films

7) Services provided in relation to the serving of food or beverages by a restaurant, eating joint, or a mess, other than those having:
   » The facility of air-conditioning or central air-heating in any part of the establishment at any time during the year
   » A license to serve alcoholic beverages

The payment of service tax must be completed on a monthly basis. The due date is the 7th of the month following the month to which the amount of tax pertains. Additionally, a service tax return must be filed on a half yearly basis. The due date for filing the return falls on the 25th of the month following the period ending in September and March.
2.1.3 Customs Duty

Customs duty is levied by the central government on the import and export of goods from India. The rate of customs duty applied to imported and exported products depends on its classification under the Customs Tariff Act. (CTA) In the case of exports from India, duty is levied only on a very limited list of goods. The Customs Tariff is aligned with the internationally recognized Harmonized Commodity Description and Coding System of Tariff Nomenclature promulgated by the World Customs Organization. The Indian central government has the power to exempt any specified goods from the whole or part of the customs duties.

In addition, preferential/concessional rates of customs duty are available under the various bilateral and multilateral trade agreements entered into by India. Customs duty is levied on the transaction value of the imported or exported goods. Under the Customs Act 1962, transaction value is the sole basis of valuation for the purposes of import and export. Although India has adopted general principles of valuation for goods that are in accordance with the World Trade Organization’s agreement on customs valuation, the central government has established independent Customs Valuation Rules applicable to the import and export of goods. India has no uniform rate of customs duty, thus duty applicable to any product is based on a number of components. The types of customs duties are as follows:

Basic Customs Duty (BCD) - BCD is the basic component of customs duty levied at the effective rate stipulated in the First Schedule to the Customs Tariff Act, 1985 (CTA) and applied to the landed value of the goods.

Countervailing Duty (CVD) - CVD is equivalent to, and is charged to counter the effect of, the excise duty applicable on goods manufactured in India. CVD is calculated on the landed value of the goods and the applicable BCD.

Educational Cess (EC) - EC at 2 percent and Secondary & Higher Education Cess (SHEC) at 1 percent are also levied on the CVD. Further, EC at 2 percent and SHEC at 1% are also levied on the aggregate customs duties. An Additional Duty of Customs (ADC) at 4 percent is also charged.

Duties of Excise

Central Value Added Tax (CENVAT) is a tax levied by the central government on the manufacture or production of movable and marketable goods in India. The rate at which excise duty is leviable on the goods depends on the classification of the goods under the Excise Tariff. The Excise Tariff is primarily based on the eight digit Harmonized System Code. The excise duty on most consumer goods is charged based on the landed value of the goods.

Abatements are admissible at rates ranging from 20 percent to 50 percent of the MSRP for the purposes of charging Basic Excise Duty (BED). Goods other than those covered by an MSRP assessment are generally charged based on the “transaction value” of the goods sold to an independent buyer.
In addition, the central government has the power to fix tariff values in order to charge ad valorem ("according to value") duties on specific goods. Occasionally, notifications granting partial or complete exemption to specified goods from payment of excise duties are also issued. EC at 2 percent and SHEC at 1 percent are applicable on the aggregate excise duties.

The central excise duty is a modified form of Value Added Tax (VAT) where a manufacturer is allowed credit on the excise duty paid on locally sourced goods as well as on the CVD paid on imported goods. The CENVAT credit can be utilized for payment of excise duty on the clearance of dutiable final products manufactured in India. In light of the integration of the goods and services tax initiated in 2004, manufacturers of dutiable final products are eligible to apply CENVAT credit to the service taxes paid on input services used in or in relation to the manufacture of final products as well as on clearances of final products up until the point of removal. In addition, CENVAT credit is allowed on the following input services:

- Services used in relation to setting up, modernization, renovation or repairs of a factory, the premises of a service provider or an office relating to such a factory or premises
- Advertisement or sales promotion services
- Services relating to the procurement of inputs
- Activities relating to businesses such as accounting, auditing, financing, recruitment and quality control, coaching and training, computer networking, credit rating, share registry and security, inward transportation of inputs or capital goods, and outward transportation

A manufacturer of dutiable and exempt goods, using common inputs or input services and opting not to maintain separate accounts, may choose between reversing the credit attributable to the inputs and input services used for manufacture of the exempted goods, to be worked out in a manner prescribed in the rules, or paying a percentage of the value of the exempted goods.
2.2 India’s Audit Process

2.2.1 Understanding Annual Audit: An Overview

Audit season in India can be a hectic and confusing time for foreign invested enterprises (FIEs) operating in the country. While most foreign executives in India leave auditing to chartered accountants and professional services firms, it is important to maintain at least a basic understanding of the audit process, how to prepare an FIE for audit, and key considerations that should be taken into account.

There are two primary objectives associated with annual audit in India. The first objective is for auditors to report to shareholders and the government whether or not the company’s balance sheet provides a true and fair reflection of its state of affairs and any profit or loss derived during the financial year. The second, an incidental objective, concerns the detection and prevention of fraud and error. Hiring an experienced firm to complete annual audit in a timely and accurate manner is critical to achieving both of these objectives.

The Basics

Audits of company accounts have been compulsory in India since the passing of the first Companies Act in 1913. Since then, the Institute of Chartered Accountants of India (ICAI), a statutory body established under the Chartered Accountants Act, 1949, has regulated the profession of chartered accountants in India and ensured the maintenance of India’s accounting standards. All chartered accountants are members of the ICAI, and must comply with the standards stipulated by the ICAI and the Audit and Assurance Standards Board (AASB).

Essentially, an audit is the inspection of an individual, business or organization’s accounts, and is traditionally completed by an independent individual or firm with specialized skills and knowledge of auditing procedures in the country in question. In other words, accountants verify that a company’s business transactions were recorded accurately, and provide a true and fair reflection of that company’s financial situation.

The importance of the audit process cannot be understated, as the results can be used for the following purposes:

• Helping investors know the financial health of the company
• Assuring the government that the company is properly discharging its legal duties
• Helping lenders evaluate the credibility of the company
• Drawing management’s attention to any shortcomings in the company’s business operations
• Helping management improve business efficiency
Auditing Objectives

As mentioned earlier, there are two key objectives associated with annual audit in India: expressing to shareholders and the Indian government a true and fair view of the company's financial statements, and detecting and preventing instances of fraud and error.

Ensuring a company's balance sheet provides a true and fair reflection of its current state of affairs requires an auditor who, after completing the audit process, will express their opinion of the company's financial statements via an auditor's report. These financial statements should include:

- Balance Sheet
- Profit & Loss Account
- Cash Flow Statement
- Notes to Accounts

A "true and fair view" can only be satisfied if the financial statements are accurate and not misleading. A company can expect the auditor to feel they have provided a true and fair assessment if the following criteria are satisfied:

- The accounts are prepared with reference to the entries in the account books
- Entries are supported by proper vouchers, documents, or other evidence
- No entry in the account book is omitted while preparing the financial statements, and nothing is included in the financial statements that were not in the account books
- The financial statements are prepared in accordance with the relevant accounting standards

An incidental objective associated with annual audit in India is the detection of errors or fraud in a company's financial statements. If an irregularity is detected, the auditor has a duty to report the details to management, who is then expected to remedy such an error.
2.2.2 Types of Audits

Basic audits in India are generally classified into two main types:

- Statutory Audits
- Internal Audits

Statutory audits are conducted to report the current state of a company’s finances and accounts to the Indian government and shareholders. Such audits are performed by qualified auditors working as external and independent parties. The audit report of a statutory audit is made in the form prescribed by the government agency.

Internal audits are conducted at the behest of internal management in order to check the health of a company’s finances, and analyze the organization’s operational efficiency. Internal audits may be performed by an independent party or by the company’s own internal staff.

In India, every company whose shares are registered on the stock exchange must have an internal auditing system in place. A company whose shares are not listed on the stock exchange, but whose average turnover during the previous three years exceeds INR50 million, or whose share capital and reserves at the beginning of the financial year exceeds INR5 million, must also have an internal auditing system in place. The statutory auditor must additionally report on the company’s internal auditing system of the company in the final report.

Statutory Audits

In India, statutory audits are conducted for each fiscal year (April 1 to March 31) and not the calendar year. The two most common types of statutory audits in India are:

- Tax Audits
- Company Audits

Tax Audits

Tax audits are required under Section 44AB of India’s Income Tax Act 1961. This section mandates that those whose business turnover exceeds INR10 million, and those working in a profession with gross receipts exceeding INR2.5 million, must have their accounts audited by an independent chartered accountant. The audit report is made using Form 3CD along with either Form 3CA (for companies) or Form 3CB (for entities not included under Form 3CA). The provision of tax audits are applicable to everyone, be it an individual, a partnership firm, a company, or any other entity. The tax audit report is to be completed by November 30 after the end of the previous fiscal year. Non-compliance with the tax audit provisions may attract a penalty of 0.5 percent of turnover or INR100, 000, whichever is lower. There are no specific rules regarding the appointment or removal of a tax auditor.
Company Audits

The provisions for company audits are contained in the Companies Act 1956 and Companies Act 2013 as applicable. Every company, irrespective of its nature of business or turnover, must have its annual accounts audited each financial year.

For this purpose, the company and its directors must first appoint an auditor at the outset. Thereafter, at each annual general meeting (AGM), an auditor is appointed by the shareholders of the company who will hold the position from one AGM to the conclusion of the next AGM. After the completion of the term, the auditor must be changed.

Only an independent chartered accountant or a partnership firm of chartered accountants can be appointed as the auditor of a company. The following persons are specifically disqualified from becoming an auditor per the Companies Act:

- A body corporate
- An officer or employee of the company
- A person who is partnered with an employee of the company, or employee of an employee of the company
- Any person who is indebted to a company for a sum exceeding INR1,000 or who has guaranteed to the company on behalf of another person a sum exceeding INR1,000
- A person who has held any securities in the company after one year from the date of commencement of the Companies (Amendment) Act, 2000

The auditor is required to prepare the audit report in accordance with the Company Auditor’s Report Order (CARO) 2003. CARO requires an auditor to report on various aspects of the company, such as fixed assets, inventories, internal audit systems, internal controls, and statutory duties, among others. The audit report must be obtained before holding the AGM, which itself should be held within six months from the end of the financial year.

According to the ICAI, audit can be defined as follows:

- Auditing is defined as a systematic and independent examination of data, statements, records, operations and performance (financial or otherwise) of an enterprise for a stated purpose. In any auditing situation, the auditor perceives and recognizes the proposition before him for examination, collects evidence, evaluates the same and on this basis formulates a judgment which is communicated through an audit report. An audit is an independent examination of financial information of an entity, irrespective of its size and form, when such examination is conducted with a view of expressing an opinion thereon.
Audit Reporting

As discussed earlier, audits are conducted to ensure a company’s financial statements present a true and fair view of its financial affairs. Therefore, the auditor’s opinion expressed in the ultimate report is based on the information gathered during the audit and the verification of financial statements. Upon completing the report, the auditor may express one of the following four opinions:

- Unqualified Opinion
- Qualified Opinion
- Disclaimer of Opinion
- Adverse Opinion

Unqualified Opinion

An unqualified opinion is expressed when the auditor concludes that the financial statements give a true and fair view in accordance with the financial reporting framework used for the preparation and presentation of the financial statements. It confirms that:

- Generally accepted accounting principles are consistently applied in the preparation of financial statements
- Financial statements comply with the relevant statutory requirements and regulations
- There is adequate disclosure of all material matters relevant to the proper presentation of financial information (subject to statutory requirements)

Qualified Opinion

A qualified opinion is expressed when the auditor concludes that an unqualified opinion cannot be expressed, but that the effect of any disagreement with management is not so material and pervasive as to require an adverse opinion, or the limitation of scope is not so material and pervasive as to require a disclaimer of opinion. A qualified opinion should be expressed as being “subject to” or “except for” the effects of the matter to which the qualification relates.

Disclaimer of Opinion

A disclaimer of opinion is expressed when the possible effect of a limitation on scope is so material and pervasive that the auditor has not been able to obtain sufficient and appropriate audit evidence and is, therefore, unable to express an opinion on the financial statements.

Adverse Opinion

An adverse opinion is expressed when the effect of a disagreement is so material and pervasive to the financial statements that the auditor concludes that a qualification of the report is not adequate to indicate the misleading or incomplete nature of the financial statements.
IFRS/IAS Convergence

While accounting standards in India differ slightly from the International Financial Reporting Standards (IFRS), Indian Accounting Standards (AS) are likely to converge with the IFRS in the foreseeable future. While a phased convergence of AS with the IFRS was initiated in April 2010 with a target date of April 2015 for full implementation, slow progress has led the Ministry of Corporate Affairs (MCA) to abandon this timeline in favor of a new roadmap for convergence expected to be released soon.

The first phase of the new convergence process will likely require companies with a net worth of more than INR10 billion (US$163 million) to transition to the IFRS from April 2015. This will be followed by companies with an annual turnover of between INR5 and 10 billion (US$82 and 163 million) from April 2016. By converging AS with the IFRS, India will join the more than 100 countries that have already adopted or converged with the IFRS, which aims to improve investor confidence via increased transparency and comparability across firms, industries, and countries.

India’s eventual “convergence” with the IFRS will differ from “adoption” in that AS will be altered to conform with the IFRS rather than requiring full-fledged adoption of the standards outlined by the International Accounting Standards Board (IASB). This will preserve differing terminologies between the IFRS and AS while adding some new concepts and models such as the Acquisition Method in lieu of the Purchase Method.
This chart highlights key differences between the IFRS/IAS and current AS:

<table>
<thead>
<tr>
<th>Topic</th>
<th>IFRS/IAS</th>
<th>Current Indian Accounting Standards</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disclosure of Accounting Policies</td>
<td>• Deals with overall considerations, including presentation, off-setting, comparative information, and format</td>
<td>• Does not deal with these aspects. Refers to Schedule VI of Companies Act 1956 for these aspects</td>
</tr>
<tr>
<td></td>
<td>• Provides for preparing statement of change in equity</td>
<td>• No such account prescribed</td>
</tr>
<tr>
<td>Valuation of Inventories</td>
<td>• Prescribes same cost formula for all inventories having a similar nature</td>
<td>• There is no stipulation for use of same cost formula</td>
</tr>
<tr>
<td></td>
<td>• When inventory is purchased on deferred terms, excess over normal price is treated as interest over the period of financing</td>
<td>• No such provision in AS</td>
</tr>
<tr>
<td>Cash Flow Statement</td>
<td>• Bank overdraft is treated as a component of cash</td>
<td>• Bank overdraft is not treated as a component of cash</td>
</tr>
<tr>
<td></td>
<td>• Provides option to classify interest and dividends either under operating activities or financing activities</td>
<td>• No such option available</td>
</tr>
<tr>
<td>Contingencies and Events Occurring After the Balance Sheet Date</td>
<td>• States that proposed dividends should not be shown as liabilities</td>
<td>• Specifically requires proposed dividends to be shown as liabilities</td>
</tr>
<tr>
<td>Changes in Accounting Policies</td>
<td>• Requires retrospective effect to be given by adjusting opening retained earnings in case of change in accounting policy</td>
<td>• Requires only prospective effect in case of change in accounting policy</td>
</tr>
<tr>
<td>Depreciation</td>
<td>• Change in method of depreciation to have prospective effect, and treated as change in accounting estimate</td>
<td>• Requires retrospective re-computation of depreciation where there is change in depreciation method, and treated as change in accounting policy</td>
</tr>
<tr>
<td>Construction Contract</td>
<td>• Contract revenue is measured at the fair value of the consideration received or receivable</td>
<td>• Contract revenue is measured as the consideration received or receivable</td>
</tr>
<tr>
<td>Revenue Recognition</td>
<td>• Allows only percentage of completion method for services rendered</td>
<td>• Allows option of completed service contract method or proportionate completion method</td>
</tr>
<tr>
<td></td>
<td>• Interest income is recognised on an effective interest rate basis</td>
<td>• Interest income is recognised on a time proportion basis</td>
</tr>
<tr>
<td>Fixed Assets</td>
<td>• Subsequent costs incurred for replacement of a part of a fixed assets are required to be capitalized and, simultaneously, the replaced part has to be de-capitalized</td>
<td>• Only expenditures that increase the capacity of an asset have to be capitalized</td>
</tr>
</tbody>
</table>
2.2.3 Ensuring a Smooth Audit: Key Considerations

Many investors are concerned about India’s reputation for having notoriously unclear rules and procedures, and approach the audit season with no small degree of trepidation. With proper advice and some relevant knowledge of the local operating environment, however, investors will find that India’s legal and financial operational procedures are not as complex as they may have initially thought.

An audit does not need to be a costly and disruptive exercise for businesses, and an audit report can be invaluable in helping companies manage their business better and address problems or loopholes going forward by identifying irregularities and errors. This article explains the processes a foreign-invested enterprise (FIE) in India can expect to undergo during statutory audit, and what companies need to know and prepare to make the audit process go smoothly.

Initial Brief

Auditors should be provided with an overview of a company’s business activities and structure so as to enable them to provide the most thorough and accurate feedback possible. While most auditors have some general industry knowledge, briefing auditors on the specific activities a business conducts, its supply chain and procurement procedures, and existing internal controls can allow the audit process to proceed smoothly. While auditors are expected to perform checks on internal controls independently, it can be beneficial to first explain how these internal controls function.

Purchasing and Procurement Procedures

Auditors will closely examine purchasing and procurement procedures, and will likely request a flow chart during audit proceedings that outlines the specifics of this process. Preparing this flow chart beforehand can save valuable time during the audit process, and providing this to auditors even if they do not request it can enable the provision of thorough feedback that will allow businesses to better understand the efficiencies and deficiencies of their operations.

Businesses can also expect auditors to examine major purchases to ensure the company is not being overcharged for the purchase of raw materials and other supplies. It is not atypical for dishonest employees to elect to purchase from more expensive, lower quality suppliers with whom they may have some personal connection or relationship (i.e. family connections or businesses and suppliers paying them a commission on purchases). By closely surveying purchasing and procurement procedures, these deficiencies can be identified and halted in the aftermath of an audit.

Auditors will additionally compare purchase vouchers with the relevant tax invoices received from the sellers of goods received notes (GRNs) to confirm whether or not the quantities and amounts match. This will allow auditors to check whether the rates of materials on invoices correspond to purchase orders raised by the company, and whether the dates on GRNs relate to the current accounting period. These checks can be time consuming, and it is recommended to have a properly trained accounting team in place to assist with these checks and make it easier for auditors to evaluate a complete paper trail.
The Production Process
An effective auditor will additionally make note of an FIE’s production and manufacturing process, and the various steps a company follows to convert raw materials into marketable goods. It is helpful to prepare a list of the main raw material inputs a business is using in production to facilitate this process. Companies can also expect auditors to check internal controls at this stage, especially those relating to the input of raw materials. In some respects, this aspect of the audit process relates back to the examination of purchasing and procurement procedures.

Journal Vouchers, Tax Expense, and Cash
A company’s auditor will also seek to verify whether the bills supporting journal vouchers and expenditures relate to the current period. While examining journal vouchers, an auditor will ensure that the tax deduction at source (TDS) was in fact deducted, wherever applicable. It is relatively common for companies to neglect to deduct TDS by mistake, and it is essential to ensure internal processes have not made such an oversight.

When claiming travel and other related expenses for tax deductions, companies should always ensure that supporting documentation is retained and provided to an auditor when necessary. It would be prudent to include in executives’ job descriptions and employment contracts that they must provide evidence of expenditure on business trips and other related expenses so as to avoid any doubt or oversight in this respect. Auditors will often seek to confirm that these expenses are within the prescribed limits outlined in the relevant job description.

Auditors are also required to check that any payment in cash or aggregate payments in cash totaling over INR20,000 in one day are not claimed as a deduction (in accordance with Section 40A(3) of the Income Tax Act 1961), and also check other credit balances in cash. A company’s Bank Reconciliation Statement should also be spot-checked by an auditor to verify expenditures.
Inventory
Manufacturing businesses need to demonstrate that they have maintained their RG 23 books and stock registers for manufacturing or processing materials. An auditor will verify that this has been done correctly, and will need to ascertain whether the RG 23A Part II / RG 23C Part II are aligned with purchase registers, and whether input credits have been recorded correctly.

Auditors will also check a company’s Personal Ledger Account (PLA) register to ensure that payments were accurately made through their PLA after considering input credit. Auditors are also expected to perform a physical inspection of stock to confirm that inventory counts match the company’s inventory register.

Other Reconciliations
A company’s auditor will also need to reconcile the following items:

- Excise/VAT returns with purchases and sales
- Provident fund contributions
- Professional tax contributions
- Employee state insurance contributions

These contributions are mandatory under statute and apply to all companies in India.
2.2.4 Miscellaneous

Management Accounts Opening Balances
Businesses should also have management accounts ready in the event that an auditor wants to check that the opening balances in those accounts have been carried forward correctly from the previous year’s audited financial statements. It is not uncommon for some minor adjustments to be necessary.

Rental Agreements
It is a good idea to ensure that the rent for a factory or office has been paid on time in accordance with the rental agreement, and that the rental agreements are up-to-date in advance of an audit.

PANs for Contractors
Companies must also ensure that they are properly maintaining photocopies of Permanent Account Number (PAN) cards for any contractors that come under TDS applicability. If a company has not been provided with a contractor’s PAN but is required to deduct TDS, it is necessary to deduct TDS at the default rate of 20 percent.
2.2.5 Summary

Audits are often seen by companies as annoying and unwelcome disturbances to their normal operations, and an audit in an unfamiliar country can be a particularly dreaded proposition. However, audits perform two vital functions.

First, they ensure that a business is complying with all relevant laws and regulations in India. They are needed to confirm that the business is correctly assessing its taxable income, backing up claimed deductions with the necessary receipts, and making the appropriate TDS deductions when required. Failure by an FIE to fulfill these legal obligations and improper record-keeping can result not only in fines from the Indian government, but also potential penalties imposed by other jurisdictions, such as under the U.S. Foreign Corrupt Practices Act or other similar legislation in Europe.

The second vital function of an audit is to identify any weaknesses or areas of improvement for a business. It is for this reason that many companies opt to conduct internal audits in addition to their legally required annual audit, as auditors often have the independence and experience to give valuable recommendations on how problems might be resolved. Audits can help to improve management practices and a company’s internal controls should be prepared to accommodate and assist with audits.

If a company’s annual audit reveals any deficiencies in its business processes or internal controls, it may be wise to closely examine those processes and controls. This may include assessing the staff charged with carrying out the company’s operations to ensure they are competent in their roles. It is only by having adequate internal controls that a business can perform to its full potential, and an annual audit is an independent and valuable measure of the adequacy of those controls and procedures.

Detecting and Avoiding Fraud

As an incidental objective associated with annual audit, detecting fraud and error can be as important as assessing whether a company’s balance sheet accurately represents its current state of affairs. For companies with operations in India, it is important to maintain an awareness of what constitutes fraud, and the fine line between fraud and error in the eyes of an auditor.

According to KPMG’s 2012 India Fraud Survey Report, 55 percent of organizations surveyed had experienced fraud in the past two years despite efforts by management to establish a robust control environment. While management is inherently the first line of defense against fraud and error, internal and external auditors are often considered the second line of defense.

Fraud refers to the willful and deliberate misrepresentation of financial information with the intention of deceiving others (i.e. shareholders, the government, etc.). This can entail both defalcation
involving the misappropriation of cash or goods, and the fraudulent manipulation of accounts by management or employees.

Defalcation involving the misappropriation of cash or goods can encompass a number of specific activities including, but not limited to:

• Recording fictitious or bogus payments
• Undercasting the receipt side total of a cashbook
• Showing the same payment twice
• Recording more payments than actual amounts paid by altering the figures on vouchers
• Misappropriating undisbursed wages
• Recording personal expenses as business expenses

Fraud through the manipulation of accounts typically implies presenting accounts more favorably than they are in reality, and distorting the profit or loss of a business and its financial state of affairs (also known as "window dressing"). This type of fraud is committed at the management level, and auditors will oftentimes suspect fraud if they encounter:

• Missing vouchers, invoices, checks, or contracts
• Balances that do not add up
• Significant fluctuations in the gross profit and net profit margin ratio
• A difference between the stock as per records and physically counted stock
• When the control account does not agree with subsidiary books
• When parties provide contradictory explanations for inconsistencies

The key difference between “fraud” and “error” often relates back to the intent to deceive, and distinguishing between the two can be challenging. Auditors are charged with exercising judgment when preparing their opinion for the final audit report, but do not make legal determinations of whether fraud has actually occurred. Rather, the auditor’s opinion is persuasive rather than conclusive in nature and based solely upon the information they reviewed and analyzed during the verification of financial statements.

If fraud is suspected by an auditor, this suspicion will be reflected in their opinion and an interested party may subsequently decide to carry out an investigation into the matter in question.
Fraud Risk Management

According to the Association of Certified Fraud Examiners 2012, the median loss caused by perpetrators of fraud in the first year of employment amounts to US$25,000 while those with more than ten years at an organization can cause a median loss of nearly US$230,000.

Mitigating the risk of fraud begins with a robust governance structure that includes the audit of budgeting processes, ethics policies, quality control, monitoring procedures by senior management, and rotation procedures. Any weakness in an organization's governance structure creates vulnerability for fraud.

Aside from ensuring an organization possesses a robust governance structure, providing an anonymous hotline or other channel for whistleblowers to alert management of fraudulent behavior can be an effective mode of fraud detection. The Companies Act 2013 additionally mandates listed companies to establish a mechanism for whistleblowers to alert management of fraud at the director or employee level.
3. Human Resources and Payroll Considerations

3.1 Key Considerations When Hiring Staff
3.2 Payroll and Social Insurance
3.1 Key Considerations When Hiring Staff

3.1.1 Visa Application

When applying for a long-term visa in India, there are a number of procedures and legal frameworks that must be understood.

India provides two kinds of work-related visas: a business visa and an employment visa. For these visas, Indian authorities require documentation from the applicant as well as the applicant’s employer. Applicants and employers should plan to allow at least one week to prepare the required documentation. Meanwhile, applicants applying for a visa by post should allow two to three weeks for visa application processing, despite declared visa processing times.

The documents required by Indian authorities are dependent on the applicant’s nationality; applicants and their employer should verify all required documentation with the Indian consulate in the applicant’s home country. Nevertheless, the majority of the required visa application documents are similar for most developed economies in Europe and North America.

Foreign nationals that intend to visit India for meetings with Indian companies should apply for a business visa. Depending on the applicant’s nationality, a multiple entry business visa can be granted for a period of up to ten years. However, the maximum allowable stay period per visit is determined by the issuing Indian consulate. US applicants, for example, can obtain a multiple entry business visa that is valid for ten years, but each period of stay is limited to six months. To acquire a business visa for India, the application must ordinarily contain the following documents.

From the applicant:

- A completed visa application form
- A valid passport
- A passport sized photo
- Proof of address such as a driver’s license or utility bill
- Documentation detailing the applicant’s financial standing such as a bank statement

“Employment visas are an annual headache for foreign businesses and businesspeople in India – Indian authorities typically issue one-year multiple entry visas that can be renewed for up to five years. To ensure a quick turn-around time on a successful application, applicants and employers should take a collaborative, hands-on approach.”

Adam Pitman
Manager
International Business Advisory
Dezan Shira & Associates
New Delhi Office

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www.dezshira.com
From the applicant’s employer:

- A permission letter that requests approval for the applicant’s visa and details the applicant’s business, planned duration of stay in India, places the applicant intends to visit, as well as a statement pledging responsibility for the applicant’s expenses
- A sponsorship letter from that pledges responsibility for the applicant’s activity in India and promises to repatriate the applicant at company if any adverse conduct comes to notice

From the employer’s Indian partner:

- An invitation letter for the applicant, which should detail the applicant’s business, planned duration of stay in India and places the applicant intends to visit
- A copy of the company’s Letter of Incorporation

Foreign nationals that intend to work for a company or non-governmental organization in India should apply for an employment visa. Applicants’ eligibility for an employment visa is subject to the following conditions:

- The applicant seeks to visit India for employment in an entity registered in India, or for employment in a foreign company engaged in a project in the country
- The applicant is a highly skilled and qualified professional, who is being hired by a company on a contract or employment basis
- The applicant is filling a role that the employer was unable to staff with a qualified Indian employee
- The applicant will not be working in a routine, secretarial or clerical job
- With the exception of language teachers, ethnic cooks, staff working for an embassy or the Indian High Commission, and voluntary workers, the foreign national must have an annual salary in excess of US$ 25,000.

Foreign nationals that meet these eligibility requirements may apply for an employment visa. An employment visa is typically granted for one year and can be extended for up to five years. To acquire an employment visa for India, the application must ordinarily contain the following documents.

From the applicant:

- A completed visa application form
- A valid passport
- A passport sized photo
- Proof of address such as a driver’s license or utility bill
- A detailed resume or curriculum vitae
From the employer:

- A permission letter that requests approval for the applicant’s visa
- A sponsorship letter that pledges responsibility for the applicant’s activity in India and promises to repatriate the applicant at company cost if any adverse conduct comes to notice
- A tax liability letter pledging full responsibility for the applicant’s income tax in India
- A justification letter that confirms that the employer was unable to find a qualified Indian candidate for the job and details the applicant’s unique specialization and professional capabilities
- An appointment letter detailing the job role and salary
- A comprehensive employment contract
- A copy of the company’s Permanent Account Number (PAN) card, an income tax designation
- The company’s Incorporation Certificate

For both business and employment visa applications, each document provided by the employer needs to be drafted on company letterhead, signed by a senior manager, and marked with the company’s official stamp. In addition, each of these documents need to be original copies. The only exceptions to these stipulations are the Incorporation Certificate and the PAN card, which can be scanned or photocopied. Still, these stipulations mean that employers must be prepared to send original copies to the applicant by post.

Companies that have successfully sponsored business and employment visas in the past are often well prepared to organize support documentation. However, companies that have not previously sponsored these visas should consider contracting an India-based visa consultant. Indian consular staff scrutinize and sometimes investigate the language of key documents, such as invitation letters for business visas or permission and justification letters for employment visas. Visa consultants are well acquainted with the application process and can provide form letters and useful advice to mitigate the potential for problems.
3.1.2 Visa Registration

Expatriates first in-country encounter with Indian bureaucracy often occurs at the Foreign Regional Registration Office (FRRO). After obtaining an Indian visa, registering the visa at a FRRO is often an afterthought for expatriates. Unfortunately, however, registering a visa is a cumbersome process.

If the duration of the visa exceeds six months (180 days), the visa holder must register the visa within 14 days of arrival at a FRRO. The only exception to this is for Pakistan nationals, who must register within 24 hours.

Long-term visa holders should plan to register their visa as soon as possible; failing to register a visa within the specified time period can result in a fine, and in some cases, an investigation. An investigation can take several weeks – the visa holder is not permitted to leave the country during this time period. In addition, investigations may complicate any future visa applications or renewals.

Registration Documents

Before visiting a FRRO to register an employment visa, a visa holder needs to prepare the registration documents required by Indian authorities. Like the visa application, both the visa holder and their employer must provide support documents to register the visa. This process requires coordination between the visa holder and their employer; visa holders and their employer should plan to allow 2-3 days to gather and complete these documents.

The visa holder must ordinarily provide:

• A completed visa registration application form
• Six passport size photos of the applicant
• A copy of the photo page within the passport
• A copy of the visa page within the passport
• Proof of address, such as a driver's license or utility bill, from the visa holder's home country
• A notarized copy of a lease deed/agreement or a C-Form from a hotel of residence
• Visa registration fees

The employer must ordinarily provide:

• Two copies of a permission letter that requests approval for the applicant's visa registration
• Two copies of a sponsorship letter that pledges responsibility for the applicant's activity in India and promises to repatriate the applicant at company cost if any adverse conduct comes to notice
• Two copies of a letter confirming the visa holder's residential address in India
• Two copies of an employment contract that specifically states the monthly salary, designation, tenure of employment, etc.
• The company's Incorporation Certificate
All documents, with an exception for the Incorporation Certificate, must be original copies, drafted on company letterhead, signed by a senior manager, and marked with the company’s official stamp.

Visit FRROs
After the registration documents have been completed, visa-holders can register their visa at FRROs located across India. The latest available listing shows that FRROs are located in the following cities:

Indian authorities ask visa-holders stationed outside of these regional centers to register their visa with the local police. However, visa-holders should attempt to register their visa with a FRRO if possible. Local police are often unaware of the visa registration process, which can lead to unnecessary delays and complications. Moreover, local police officers in rural and un-developed areas are often under-resourced.

For these reasons, many visa-holders stationed in rural and un-developed areas register their visa at a FRRO. This ensures that visa-holders receive the swiftest possible service and maintain privacy at their field location. To do so, the applicant must stay at a regional center with an FRRO for several days, listing a local affiliate office – such as a sales office – as a place of business.
Registering Your Visa
To register a visa, the applicant must bring all required documentation and physically visit an FRRO. Visa holders may schedule a visa registration appointment; however, many visa holders simply visit the FRRO at a time of their choosing. Visa holders that have not scheduled a registration appointment should arrive at the FRRO as early as possible to avoid large crowds.

While visa holders will likely need to wait several hours for a registration officer, well-organized applicants will receive a registration certificate from the officer in a matter of minutes. Once the process is completed, the visa holder becomes legally eligible to work and reside in India for the allowed period.

Although visa holders seeking to register their stay in India can successfully do so independently, many companies employ a local visa consultant. These consultants, who are often certified lawyers, can provide form letters and crosscheck registration documents to ensure that registration applications do not invite any undue scrutiny.

In addition, visa consultants can enter the FRRO with the visa holder to provide support during the registration. Visa holders are not allowed to bring local guests into the FRRO; the presence of a visa consultant ensures that the applicant is accompanied by someone who can speak the local language and answer technical questions during the registration.

A Cumbersome but Valuable Experience
Although registering an employment visa can be a burden for freshly arrived expatriates, the experience provides important insights into the Indian bureaucratic process. Expatriates unfamiliar with Indian bureaucracy will learn local practices that are critical for preparing and submitting official documents in India. Moreover, the process can help managers understand the amount of time and energy required for doing business with local government offices.
3.2 Payroll and Social Insurance

3.2.1 Withholding Tax Returns Filing

Similar to China, businesses in India are required to withhold Individual Income Tax (IIT) from an employee's salary on a monthly basis. During the first seven days of each month, employers must deposit the deducted tax from the previous month with the central government. The only exception to this rule involves the month of March, during which tax deducted may be deposited on or before April 30th.

Employers are required to withhold tax on various payments including rent, interest, dividend, royalty, and service income. In this sense, the compliance requirements for employers are more complex in India than in many other countries. Businesses should actively coordinate with employees to understand the details of supplementary income they are receiving and make the relevant calculations and submission of tax before deducting them from the salary.

Quarterly withholding tax return statements must also be submitted by the 15th of the month following the end of a quarter to the central government reporting the tax deducted at source during the quarter. Failure to meet either this deadline or the monthly IIT deposit deadline can result in both interest and penalties being imposed on a company.
3.2.2 Individual Income Tax (IIT)

Liability Determination

For expatriates, the extent to which services rendered in India are taxable is irrespective of whether the salary is received from inside India or outside India. The taxation of individuals is determined by residence status. Under the Income Tax Act, an individual can have the status of Resident and Ordinarily Resident, Non-resident, or Resident but not Ordinarily Resident. A quick guide to residential status is as outlined below:

<table>
<thead>
<tr>
<th>Period of Stay</th>
<th>Residential Status</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Basic Conditions</strong></td>
<td></td>
</tr>
<tr>
<td>Stay in India is 182 days during tax period</td>
<td>Resident</td>
</tr>
<tr>
<td>Stay in India is 60 days during tax period and 365 days in 4 preceding tax periods</td>
<td>Satisfies either condition</td>
</tr>
<tr>
<td>Satisfies neither condition</td>
<td></td>
</tr>
<tr>
<td><strong>Additional Conditions</strong></td>
<td></td>
</tr>
<tr>
<td>Non-Resident in at least 9 of the 10 preceding tax years</td>
<td>Resident and ordinarily resident</td>
</tr>
<tr>
<td>Stay in India is 729 days in 7 preceding tax periods</td>
<td>Resident but not ordinarily resident</td>
</tr>
<tr>
<td>Satisfies neither condition</td>
<td></td>
</tr>
<tr>
<td>Satisfies either condition</td>
<td></td>
</tr>
</tbody>
</table>

It is also important to note that under the following conditions, 60 days is substituted by 182 days for:

1. An Indian citizen or a person of Indian origin who visits India during any tax period
2. An Indian citizen who leaves India during any tax period for the purpose of employment outside India

Income in the form of salaries includes remuneration in any form for personal services provided under an expressed or implied contract of employment or service. Such income is subject to tax on a ‘due’ or ‘receipt’ basis, whichever is earlier, and includes wages, annuity or pension, gratuity, fees, commission, prerequisites, or profits in lieu of salary, advance salary, leave encashment, etc. Except for under provisions dealing with short stay exemptions, no specific expatriate concessions are available under India’s tax laws.

An expatriate can be a resident of two countries at the same time. In such a scenario, there could be double taxation of the same income, but relief from double taxation may be available under the relevant Double Taxation Avoidance Agreements (DTAAs). Taxation relief can be available in the form of a tax credit in the country of permanent residency. Further, submission of a Tax Residency Certificate containing prescribed particulars is a necessary condition for availing of benefits under DTAAs. An application under Form 10FA must be made to obtain a tax residency certificate in India.
3.2.3 Income Tax Returns

As a result of 2014’s tax audit report deadline being moved to November 30, a number of high courts in several key Indian states also ordered an extension of income tax returns from September 30 to November 30, including Gujarat, Chennai and Bombay. However, it has not yet been announced whether this extension will also apply in 2015.

The process for filing income tax returns is a fairly straightforward one. You must:

Acquire a PAN number
A permanent account number (PAN) is absolutely necessary for income tax returns. It is a ten-digit number that is issued on a laminated card, and will be used as your ID when registering on CBDT’s website.

Select the appropriate tax return form
There are several income tax return forms according to your specific situation. These include forms for individuals with a single house, for companies, and for persons who are applicable for special taxation schemes, and can be found on CBDT’s website. Ensure that you select the relevant one.

Work out which rate of tax you are on
The rates of income tax are listed in the country’s Finance Bill, which is reviewed and amended every year. Under current policy, the key rates of tax are:

<table>
<thead>
<tr>
<th>Estimated Yearly Taxable Income (TI) in USD (for comparison only)</th>
<th>Tax Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>3,000 or less</td>
<td>0%</td>
</tr>
<tr>
<td>3,001-6,000</td>
<td>10%</td>
</tr>
<tr>
<td>6,001-8,000</td>
<td>10%</td>
</tr>
<tr>
<td>8,001-10,000</td>
<td>20%</td>
</tr>
<tr>
<td>10,001-15,000</td>
<td>20%</td>
</tr>
<tr>
<td>15,001-18,000</td>
<td>20 - 30%</td>
</tr>
<tr>
<td>18,001-20,000</td>
<td>30%</td>
</tr>
<tr>
<td>20,001-30,000</td>
<td>30%</td>
</tr>
<tr>
<td>30,001-45,000</td>
<td>30%</td>
</tr>
<tr>
<td>45,001-60,000</td>
<td>30%</td>
</tr>
<tr>
<td>60,001-100,000</td>
<td>30%</td>
</tr>
<tr>
<td>100,001-150,000</td>
<td>30%</td>
</tr>
<tr>
<td>150,001 or more</td>
<td>30%</td>
</tr>
</tbody>
</table>
Further, Domestic companies with a total income that exceeds one crore rupees but does not exceed ten crore are taxed at a rate of five percent. If the total income exceeds ten crore rupees, they are taxed ten percent. For non-domestic companies with a total income that exceeds one crore rupees but does not exceed ten crore, the rate is two percent. If income exceeds ten crore rupees, it is five percent.

As mentioned previously, companies and individuals not working in India but earning an income there are still applicable for tax. It used to be that long-term capital gains were waved for taxation, but this is no longer the case. The rates of tax for non-residents are:

- On any investment income, the income tax rate is 20 percent;
- For long-term capital gains, the rate will either be 10 percent or 20 percent, depending on the nature of your operation;
- On short-term capital gains, 15 percent.

**Calculate your income tax-rate**

- You should then calculate your tax returns against the above rates of tax. You can use the tax calculator on CBDT’s website to do this. Make sure that the information you enter is absolutely accurate, otherwise your tax return application will be rejected.
- After using the tax calculator, you can then follow the prompts on CBDT’s website to complete your tax return. Alternatively, you can use a non-government website to perform the tax return for you, but these will invariably charge a fee for doing so.

**Retain your tax documents**

Having completed your tax return, ensure that you retain printouts and statements of your taxable income in the event that you are contacted by the tax authorities.
3.2.4 India’s Provident Fund Scheme

While much of the Indian population does not participate in the country’s social insurance program known as the Provident Fund Scheme, Indian citizens in the organized sector are entitled to coverage.

International workers including expatriates working for an employer in India are also eligible to participate in the Provident Fund Scheme. Employers are required to contribute 12 percent of their employees’ specified salary to the scheme, and contributions must be deposited on a monthly basis by the 15th of the subsequent month.

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Contribution towards Employee Pension</th>
<th>Contribution towards Employee Provident Fund</th>
<th>Medical (Employee State Insurance Corporation)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Company contributions</td>
<td>8.33 %</td>
<td>3.67%</td>
<td>4.75%</td>
</tr>
<tr>
<td>Individual contributions</td>
<td>10%-12%</td>
<td>N/A</td>
<td>1.75%</td>
</tr>
<tr>
<td>Coverage</td>
<td>20+ employees</td>
<td>20+ employees</td>
<td>10+ employees</td>
</tr>
<tr>
<td>Employee Eligibility</td>
<td>All</td>
<td>All</td>
<td>Employees earning up to INR 15,000 a month</td>
</tr>
</tbody>
</table>

Possible Changes for this Year

The Employees’ Provident Fund Organization has recently proposed changes to India’s Provident Fund scheme. Should the changes be accepted and implemented, the mandatory limit for registration will decrease from 20 to 10 employees, and the compulsory contribution of between 10 and 12 percent will be reduced or even waived for a particular period.

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