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A study on how to establish
companies in India from a legal
and tax point of view.

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Summary

My graduate thesis handles the problem how Sony Ericsson Mobile Communications AB (SEMC) in the easiest way can establish a market in the south of India, Chennai, relating to accessories. The most relevant accessory that they want to manufacture is portable hands frees.

I have made an analysis of financial and governmental directives and found out what the restrictions are to import and export goods to and from India.

My work also comprehends the possibilities for SEMC to establish a local production of accessories based upon the governmental financial duties, levies and other directives applicable for such business operation.

My key focus has been on inbound and outbound duties and fees as well as financial and legal directives and restrictions to establish local production in India.

First, I have a little summary on how Sony Ericsson Mobile Communications AB work and what their intentions with the new establishment are. The structure of the legal work is also included. After that, a brief description on how India is built, as a country as well as a legal body.

In the middle of the thesis, I have made a description on how one can establish a company in India to receive the most advantages concerning taxes, customs and incentives.

The foreign trade policy of India is discussed at the end of the thesis along with the policy regarding the telecom sector.

Preface

I have finally written my Master thesis here at the Faculty of Law, University of Lund. I cannot believe that my four and a half years here has ended. It has been a terrific journey and the best years in my life so far. I would like to thank a few people that have stood by me and mean so much to me. The first person is my lovely mother and best friend, Charlotte. Without your love and support I would not have made it through, you mean the world to me. I would also give a huge thank you to my father Lennart who has always supported me and helped me through everything. To the rest of my entire family, thank you all for your endless love and support. I would like to say thank you to my closest friends, which have always supported me. Vanessa, Melissa Kristina and Andrea, I love you all so very much! Of course a huge thank you to all of my friends at Juridicum, which have been there for me night and day, especially Martin, John, Sofia and Emil!

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Abbreviations

BTN	Brussels Tariff Nomenclature
CBDT	Central Board of Direct Taxes
CBEC	Central Board of Excises and Customs
CST	Central Sales Tax
DTA	Domestic Tariff Area
DTAA	Double Taxation Avoidance Agreement
DoT	Department of Telecommunications
ECB	External Commercial Borrowings
EOU	Export Oriented Units
EPCG	Export Promotional Capital Goods
EPZ	Export Processing Zones
EXIM Policy	Export and Import Policy
FIPB	Foreign Investment Promotion Board
FTP	Foreign Trade Policy
HS	Harmonised Commodity Description and Coding System
ICD	Inland Container Depots
IEC number	Importer-Exporter Code number
NTE	Net Foreign Exchange
OECD	Organisation for Economic Cooperation and Development
RBI	Reserve Bank of India
ROC	Registrar of Companies
SEMC	Sony Ericsson Mobile Communications
SEZ	Special Economic Zones
TATT	Transfer and Trading in Technology
WTO	World Trade Organisation

1 Introduction

The raising demand for a wide range of telecom equipment, especially in the mobile telecommunication area, has provided fantastic opportunities to domestic and foreign investors in the manufacturing business. This explains why there have been many companies during the last two years that have set up their manufacturing business in India. India has an increasing use of mobile phones and its service is viewed as a mass consumption service. Now the turn has come to Sony Ericsson Mobile Communications (SEMC). The point of the departure of this master thesis is that SEMC wants to establish a manufacturing business in India regarding portable hand frees (phf) and other accessories. Part of the production is meant for export as well provided reasonable commercial terms could be found and agreed. The manufacturing will be set up in the south of India, in an area called Chennai. They do need to increase their knowledge of local regulations and trade prerequisites. Here is where I come in; they want me to examine the different manufacturing possibilities in Chennai.¹

1.1 Purpose and question at issue

The main question at issue is which way is the best way for SEMC, in a legal point of view, to establish their manufacturing in India. I will attempt to answer this question through the following sub-questions:

- Which alternative is the more advantageous/favourable of the following two:
 - establish a new Indian company or
 - the establishment of a foreign company?
- How much foreign equity the new company are allowed to.

If any of the above alternative is attractive, how would this compare to direct import of finished products?

1.2 Method and material

The research focus for my work have been to find out how the legal structure, the taxation system and the custom system of India looks like and how it applies to foreign investors, since I believe that these areas are unknown to most people I have been using the traditional legal method. The material used in this thesis is information from the different public authorities in India. They have a very broad information and fact base on the

¹ See picture in Supplement A.

internet. The different acts of India have been a very helpful instrument finding out how the legal structure of India looks like and works. Björn Savlid at the Swedish Export Council has been very helpful providing me with information on how the EOUs and SEZ works. The conclusion section summarises the findings on this thesis, and provides some personal thoughts.

1.3 Disposition

In the beginning of my thesis, I give a short explanation on what kind of company SEMC is, and what they produce. After that, I provide general information about India to give a better understanding of their way of thinking. An introduction to their taxation system, customs, duties and excise are explained. The thesis also covers the Indian trade policy and how their import and export system works. The biggest part of the thesis covers the different ways to establish a new business in India. There are two ways, either as an Indian company or as a foreign company. When that decision has been made, the other question is where the company should be placed to receive the most benefits and incentives. Regarding this question there are two alternatives. One can either register the company in an Export Oriented Zone or as a unit in a Special Economic Zone.

1.4 Sony Ericsson Mobile Communications AB

Sony Ericsson Mobile Communications is a global provider of mobile multimedia devices, including feature-rich phones and accessories. The products have a large combination of powerful technology with innovative applications for mobile imaging, communications and entertainment. The result is that Sony Ericsson is a very attractive brand. They create business opportunities for mobile operators and exciting and fun products for the end users.

In 2001, telecommunications leader Ericsson and consumer electronics powerhouse Sony Corporation established Sony Ericsson Mobile Communications. Ericsson and Sony equally own the company and their first joint product were announced in March 2002.²

The products of Sony Ericsson have a universal appeal and have a very different approach concerning areas of imaging, design and applications. Sony Ericsson has continually launched products that make the best use of the major mobile communications technologies, such as the 2G and 3G

² Sony Ericsson Mobile Communications corporate profile, p. 1.
http://www.sonyericsson.com/spg.jsp?cc=global&lc=en&ver=4001&template=pc1_1&zone=pc&lm=pc1 . (070530)

platforms, at the same time as they are enhancing its offerings to entry level markets.³

Sony Ericsson Mobile Communications are one of the world leaders regarding design and innovation in mobile communications. They strive to be a good provider applications, foregoing partnerships with application developers and content providers. One way to achieve to be the best and come up with the latest ideas concerning entertainment is their agreement with Sony Music Entertainment.⁴

Sony Ericsson has approximately 7500 employees worldwide. They carry out product research, design and development, marketing, sales, distribution and customer service. They have establishments in over 40 countries around the world and they get inspiration from all the different cultures. The global management is in London and R&D is in Sweden, Japan, China, the Netherlands, the US and UK.⁵

³ Ibid, p. 1.

⁴ Ibid, p. 2.

⁵ Ibid, p.2 and Sony Ericsson Mobile Communications jobs & careers, the Sony Ericsson story p.1

[http://www.sonyericsson.com/spg.jsp?page=pc2_2&cc=global&lc=en&ver=4001&template=pc2_2&zone=pc_\(070530\)](http://www.sonyericsson.com/spg.jsp?page=pc2_2&cc=global&lc=en&ver=4001&template=pc2_2&zone=pc_(070530))

2 Basic facts about India

India is the worlds largest democracy and the population is more than one billion people. They have a large amount of nature resources and a very rich culture. India has grown a lot during the last few years as one of the worlds fastest growing countries, both when it comes to population and industry. A large-scale reform regarding the economy started in 1991. This led to that a big amount of foreign business establishments and a influx of foreign investments.⁶

During the last year, the reform work has been intensified because many governmental companies have been transformed into private companies. A result of the government's intentions was the announcement of the decision to sell out their 50 % share in the country's head car manufacturer, Maruti Udyog. Other Indian companies that are for sale are Air India and Indian Airlines. There is a big chance that the government in a short period will announce the sell out of the two telecom companies, MTNL and VSNL. The focus of the government's priorities is now the infrastructure, which is very important for the development of India. Relating to these areas there are quite big opportunities for business relations with Swedish companies. One of the first reforms that was brought out towards the end of 1999 was that the Indian government opened the once before totally owned governmental insurance industry to both private and foreign operators. At this moment, one can find on the market, new innovative insurance solutions that has not existed before. Because of the attitude of the current government, India's opportunities in growth has risen quite high the last years.⁷

According to its constitution, India is a secular republic. India is a federation, which consists of 29 self-governing States. There are also six "Union Territories". The government has the structure according to the British parliamentary. They have had huge successes with the democratic federal system, which is why all the different people have been able to live according to their own ideals.

For a very long time India has been the most dominating power in the Southeast Asia. This is an example of the size of the country, its fast growing economy, their permanent place in the UN, their possession of nuclear, aircraft carrier and their own space programme. Neutrality and alliance freedom has been the foundation for the foreign policy since their independence in 1949. The alliance free movement acted as an important foundation during the cold war and at the same time, India closed a cooperative scheme with the Soviet Union. The collaboration with the United States of America is a result of the cold war; it is easier for India to have relations with other big-power block of nations than before the war.

⁶ Swedish Trade Council country rapport Asia, India, <http://www.swedishtrade.se/landrapporter/?objectID=4331> (070530) p. 1.

⁷ Ibid, p. 2.

Maybe an even greater new relationship that has improved is the collaboration with China.⁸

During its first 40 years as an independent nation, India had a planned economy with an annual growth of a few percent. This all changed because of a crisis in 1991, when India had no other choice than to change course to a market economy. The results of that was that the growth had a remarkable rise and the economy of India has since then grown with approximately 5 to 8 %.

India has a very small percentage share of the world trade, only 0, 8 %.

Their goal for 2007 is to have reached 1 %. The export of India has expanded with more than 10 % a year. India has a potential to expand their external trade with up to 80 %.⁹

2.1 The Indian taxation system

Indian tax legislation is enacted both at the Central level and at the State level. The power to levy almost all direct and some indirect taxes have been given to the Central Government. Taxation of income is in accordance with the provisions of the Income tax Act, 1961. The bodies that empower the right to implement and administer direct tax laws are the Ministry of Finance (Department of Revenue) through the Central Board of Direct Taxes (CBDT). The CBDT is an apex tax authority. The judiciary decides the interpretation of tax laws, which is independent of the legislature. The circulars, notifications and clarifications that are issued by the CBDT supplement the Act.¹⁰

The Indian tax year runs from 1 April to 31 March of the following calendar year for all taxpayers. Taxable income must be ascertained separately for different classes of income and is then aggregated to determine total taxable income. Income tax is levied on “taxable income”, which consists of the following categories: salaries, income from house property, profits and gains of business or profession, capital gains and income from other sources.¹¹

For most of the times domestic companies, partnerships and local authorities are subject to tax at flat rates, whereas individuals and specified taxpayers are subject to progressive tax rates. The tax system in India is self-assessment¹². All taxpayers are required to file their tax returns and pay the tax. The tax Officer has the right to make a scrutiny assessment to estimate officially the correct amount of tax by requiring further information and details.

The expenses that businesses take on for their purposes are deductible from taxable income. To be able to deduct as expenses, the expenses themselves has to be wholly and exclusively paid during the previous year and

⁸ Swedish Trade Council, country rapport Asia, India, p. 2.

⁹ Ibid, p. 5.

¹⁰ Ministry of External Affairs Government of India, India in business, <http://www.indiainbusiness.nic.in/investment/taxation.htm> (070530) p. 1.

¹¹ Ibid, p. 1.

¹² It means an evaluation and judgement of one’s own abilities, action, attitudes.

supported by relevant papers and records. The expenses of a personal or a capital nature are not deductible. It is not allowed to make income tax a deduction.¹³

2.1.1 Direct taxation in India

When discussing corporate income tax the definition of a company is important. The definition of a company in India is one that is a juristic person having an independent and separate legal entity from its shareholders. The income of the company is calculated and assessed separately in the company. A company is resident in India during the relevant previous year if it is an Indian company, but if it is not an Indian company, the control and the management of its affairs have to be situated wholly in India. If a company is not an Indian company and some part of the control and management of its affairs is situated outside India, the company is said to be non-resident in India.¹⁴

India has signed Double Taxation Avoidance Agreements with 65 countries including the United States of America, the United Kingdom, Japan, France, Germany and Sweden. These agreements provide a relief from double taxation in respect of incomes in the form that they provide exemption and credits for taxes paid in one of the countries. The base of these treaties is the general principles laid down in the model draft of the Organisation for Economic Cooperation and Development. There are of course some modifications so that the agreements are suitable for the other contracting countries.¹⁵

The most common DTA agreement between India and another country only covers the residents of India and the residents of the contracting country. It is only the residents of India and the residents of the contracting country that can claim any benefit under the relevant DTA agreement. The tax treaties are meant to be beneficial and not intended to put the contracting states taxpayers to a disadvantage. In the Indian Tax Act 1961, a beneficial provision under the Indian Income Tax Act will not be denied to residents of a contracting state simply because the corresponding provision in the tax treaty is less beneficial.¹⁶

2.1.2 Indirect taxation in India

2.1.2.1 Sales Tax

The definition of Sales Tax is a tax that is levied on the sale or purchase of goods. Sales tax is levied under the authority of both Central Legislation¹⁷

¹³ Ministry of External Affairs Government of India, India in business, <http://www.indiainbusiness.nic.in/investment/taxation.htm> (070530) p. 2.

¹⁴ Ministry of External Affairs Government of India, India in business, http://www.indiainbusiness.nic.in/investment/corporate_incometax.htm (070530) p. 1.

¹⁵ Ministry of External Affairs Government of India, India in business, http://www.indiainbusiness.nic.in/investment/double_tax.htm (070530) p. 1.

¹⁶ The Indian Tax Act 1961, section 90.

¹⁷ Central Sales Tax.

and State Governments Legislations¹⁸. The Central Sales Tax Act 1956 is the framework for the Central Sales Tax and it covers inter-state transactions of sale of goods as well as transactions of import of goods into or export of goods out of India. The Local Sales Tax is governed by the respective State Sales Tax Acts under which tax is levied on intra-state transactions of sales.¹⁹

Central Sales Tax is to be paid on the sale of all goods by a dealer in the course of the interstate trade or commerce or, outside a State or, in the course of import into or, export from India. If the sale and purchase are the reason for the movement of goods from one State to another or when the sale is effected by a transfer of documents of title to the goods during their movement from one State to another, the sale or purchase shall be believed to take place in the course of interstate trade or commerce.²⁰

The Sales Tax is to be paid to the sales tax authority in the state from which the movement of goods begins. The person that has to pay the Sales Tax is every dealer on the sale of any goods effected by him in connection to the inter-trade or commerce, although that no liability to tax on the sale of goods arises under the tax laws of the appropriate state. If a sale or purchase takes place outside the state and in the course of import of goods into or export of goods outside of India, there is no way that a state can levy sales tax on those goods or purchases. The only one that can levy tax on inter-state sale or purchase of goods is the parliament.²¹

There are some principles regarding the state sales tax laws. A sale or purchase is being made when the transfer of property in the existing goods or future goods takes place for consideration of money. The goods are divided into different categories and different rates of sales tax. Regarding the sales tax cases, the tax on the sale or purchase is made at a single point. Every dealer that sell or purchase goods should apply for registration and obtain a registration certificate to that effect.²²

2.1.2.2 Value Added Tax

This tax is a general consumption tax assessed on the value added to goods and services. It applies to all the commercial activities that involves the production and distribution of goods and the provision of services. The fact that it is borne ultimately by the final consumer makes it a consumption tax. The actual tax is not charged on companies but as a percentage of prices. The result is that the actual tax burden is visible at every stage in the production and distribution chain.²³ The collection of the VAT happens fractionally, via a system of deductions so that the taxable persons can deduct from their VAT liability the amount of tax they have paid to other taxable persons on purchases for their business activities. Since the system

¹⁸ Local Sales Tax.

¹⁹ Ministry of External Affairs Government of India, India in business, http://www.indiainbusiness.nic.in/investment/indirect_tax.htm (070530) p. 1.

²⁰ The Central Sales Tax Act 1956, chapter 2, 3a.

²¹ India Mart <http://finance.indiamart.com/taxation/salestax.html> (070530) p. 2-3.

²² Ibid, p. 3.

²³ To get more information about VAT, Buckett Alan "VAT in the European Community".

works this way, it ensures that the tax is neutral regardless of how many transactions are involved. The construction of VAT is such that when it concerns goods that are imported and consumed in a particular state, the first seller pays the first point tax and the next seller pays tax only on the value-addition done. The result is a total tax burden exactly equal to the last point tax.²⁴

India introduced VAT in its Indian Taxation System on April 1, 2005. The Value Added Tax Act administrates the VAT levy. There are three ways to compute VAT. The first one is the subtraction method, which means that the tax rate is applied to the difference between the value of output and the cost of the input. The second is the addition method which means that the value added is computed by adding all the payments that is payable to the factors of production and the last one is the tax credit method which entails set-off of the tax paid on inputs from tax collected on sales. India chose the tax credit method.²⁵

2.1.3 Why India needed VAT

India needed a taxation system that would close the avenues for traders and businesspersons that evaded paying taxes. VAT made them to be compelled to keep accurate records of their sales and purchases. There is no room for any exemptions under the VAT system and a tax is levied at each stage of manufacture of a product. At every stage of value-addition, the tax that is levied on the inputs can be claimed back from the tax authorities.²⁶

VAT is a multi-point sales tax with set-off for tax paid on purchases and capital goods. The dealers can deduct the amount of tax paid by him for different purchases from the tax collected on sales. This way they only pay the balance amount to the Government.

Even though India needed VAT, a few sales are not covered in the VAT Act because the VAT Act only applies to sales within a state. The VAT Act does not cover Sale in the course of inter-state trade or commerce, which shall continue to be liable to the Central Sales Tax Act 1956, sale that takes place outside the state and sales in the course of export or import.²⁷

²⁴ India Mart, http://finance.indiamart.com/taxation/meaning_of_vat.html (070530) p. 1.

²⁵ India Mart, http://finance.indiamart.com/taxation/vat_in_india.html (070530) p. 1

²⁶ India Mart, http://finance.indiamart.com/taxation/necessity_of_vat_in_india.html (070530) p. 1

²⁷ India Mart, http://finance.indiamart.com/taxation/vat_faqs.html (070530) p. 1

3 Introduction to Indian customs

The Indian customs have quite a lot of important tasks. The five most important tasks are:

1. the collection of customs duties on imports and exports as per basic customs laws,
2. the enforcement of the various provisions of the Customs Act governing imports and exports of cargo, baggage, postal articles and arrival and departure of vessels, air crafts etc.,
3. discharge of various agency functions and enforcing various prohibitions of the Customs Act and other allied enactments,
4. prevention of smuggling including prohibition of narcotics drug trafficking and
5. international passenger processing.

The basic statute is the Customs Act 1962 and it empowers that “duties of customs shall be levied at such rates as may be specified under the Customs Tariff Act 1975 or any other law for the time being in force, on goods imported into or exported from India”.²⁸ The rates at which duties of customs shall be levied under the Customs Act 1962 are specified in the First and Second Schedule.²⁹ The legislature has prescribed different rates of duties on different commodities that are mentioned in the first Schedule. The duties are levied on both specific and ad valorem basis³⁰ but sometimes are specific-cum-ad valorem³¹ duties collected on imported goods. When the collection of ad valorem duties happens, the value of the goods has to be determined for customs duty purposes as per provision in the Customs Act. “For the purpose of the Customs Tariff Act 1975 or any other law being in force where under a duty of customs is chargeable on any goods by reference to their value, the value of such goods shall be considered to be the price at which such or like goods are ordinarily sold, or offered for sale, for delivery at the time and place of importation or exportation, as the case may be, in the course of international trade, where the seller and the buyer have no interest in the business of each other or one of them has no interest in the business of the other, and the price is the sole consideration for the sale or offer for sale”.³² In addition to this, there are some rules that shall apply to imported goods where a duty of customs is chargeable by reference to their value; they are called the Customs Valuation (Determination of price of imported goods) Rules 1988.³³ All of the requirements have to be very carefully studied and applied by the

²⁸ The Customs Act 1962, section 12 (1).

²⁹ The Customs Tariff Act 1975, section 2.

³⁰ Duties that depend upon its value, with reference to value, in proportion to the value.

³¹ Duties are levied upon imports with a fixed amount per unit.

³² The Customs Act 1962, section 14.

³³ To get more information about customs, Thompson, Edward Palmer, ”Customs in common/E.P. Thompson”.

importer as well as the assessing officer so that the duties as due after proper valuation as per law are discharged before the goods get out of customs control.³⁴

3.1 The valuation of customs

The basis valuation of import and export goods in the country can be found in section 14 of the Customs Act 1962. For the products that are called tariff values, the Central Government has the power to fix values. If the tariff values are fixed for any goods, the ad valorem duties will be calculated with reference to such tariff values. These tariff values can be fixed for any class of imported or export goods, having regard to the trend of value of such or similar goods, and where any such tariff values are fixed, the duty shall be chargeable with reference to such tariff value, and has to be notified in the Official Gazette.³⁵

The definition of “value, in relation to any goods, means the value thereof determined in accordance with the provision of sub-section (1) of section 14”.³⁶

When it concerns export goods, the provisions in section 14 provides a complete code of valuation by itself. As for imported goods, the value is required to be determined in harmony with rules made in this behalf.

The customs value should, according to the Customs Valuation Rules 1988, be the transaction value. Concerning imported goods, the value shall be the transaction value. This is the price actually paid or payable of the goods when sold or exported to India.³⁷ The meaning of the price actually paid or payable is the total payment made or to be made by the buyer to the seller or for the benefit of the seller for the imported goods. All payments that are made as a condition of sale of the imported goods by the buyer to the seller or by the buyer to a third party to satisfy an obligation of the seller is included in the actual paid price.³⁸

3.1.1 The rights of appeal concerning the valuation matters

Principles concerning the justice in valuation matters have to be followed. If the customs authorities do not accept the declared value and have to re-determine the customs value, the importer or the one that represent him are required to be given a written notice and a personal hearing. If the importer is aggrieved with the re-determination of value, a judicial decision giving in detail the basis of the determination of value can be given. At the Commissioner Appeal as a first instance, an importer can appeal against a

³⁴ Central Board of Excise and Customs Manual, S.No. 1 section 2.

³⁵ The Customs Act 1962, section 14 (2).

³⁶ Ibid, section 2 (41).

³⁷ The Customs Valuation Rules 1988, rule 3 and 4.

³⁸ Central Board of Excise and Customs Manual, S. No. 6 section 9.

decision on valuation. The second appeal is to be given to the Tribunal that consist of administrative and judicial members. If one will take the appeal further, the third appeal lies to the Supreme Court of India. Each of the adjudicating and appellate authorities informs the importer regarding his rights of appeal.³⁹

3.2 The most important customs acts, rules and regulations

India has many different acts concerning customs. The most comprehensive and important is the Customs Act 1962. This act was formulated in 1962 to prevent illegal imports and exports of goods. All imports are sought to be subject to a duty with the view to affording protection to native industries and to keep the imports to the minimum in the interest of securing the exchange rate of Indian currency.⁴⁰

Duties of customs are levied on goods imported or exported from India at the rate that is specified in the Customs Tariff Act 1975. Concerning the unloading of the imported goods and loading of the exported goods, the Central Government has the power to notify the ports and airports. The places for clearance of imported or to be exported goods, the routes by which the goods mentioned above may pass by land or inland water into or out of India and the ports which by themselves shall be coastal ports. This power is to exercise proper surveillance over imports and exports.⁴¹

The Central Board of Excises and Customs (CBEC) periodically bring out a book called the “Indian Customs Tariff Guide”. This book contains different tariff rulings issued by the CBEC. The “Indian Customs Tariff Guide” is published to give a road guide as to classification of goods for the purpose of duty liability.

The Customs Tariff Act 1975 is an act to consolidate and amend the law relating to customs duties. The rates, at which duties of customs shall be levied under the Customs Act 1962, are specified in the First and Second Schedules in the Act of 1975.⁴²

India has quite a lot of rules concerning customs. The Customs valuation (Determination of Price of Imported Goods) 1988 shall apply to imported goods where a duty of customs is chargeable by reference to their value. The Customs, Central Excise Duties and Service Tax Drawback (Amendment) Rules 2006 concerns the drawback in relation to any goods manufactured in India and exported. Drawback means the rebate of duty or tax, as the case may be, chargeable on any imported materials or excisable materials used or taxable services used as input services in the manufacturing of such goods.⁴³

³⁹ The Customs Act 1962, section 128-129.

⁴⁰ India Mart, http://finance.indiamart.com/taxation/custom_duty/index.html (070530) p. 1.

⁴¹ Ibid, p. 1.

⁴² The Customs Tariff Act 1975.

⁴³ The Customs, Central Excise Duties and Service Tax Drawback (Amendment) Rules 2006, section 2 (a).

The Accessories (Condition) Rules 1963 say in the exercise of the powers conferred by section 156 of the Customs Act 1962 that “accessories of and spare parts and maintenance or repairing implements for, any article, when imported along with that article shall be chargeable at the same rate of duty as that article, if the proper officer is satisfied that in the ordinary course of trade, such accessories, parts and implements are compulsory supplied along with that article and not separate charge is made for that supply, their price being included in the price of the article”.⁴⁴ How to make an application for obtaining an advance ruling⁴⁵ is regulated in the Customs (Advance Rulings) Rules 2002. How the Authority for Advance Rulings shall operate are regulated in the Authority for Advance Rulings (Customs, Central Excise and Service Tax) Procedure Regulations 2005.

3.3 The Customs Act control and regulatory provisions

To properly and effectively handle growing international traffic and to make it administratively possible that goods imported into India or exported out of the country by sea, air, land or rail routes are checked by the Customs, to ensure that they are abided with all the related laws before entry into or exit from India. Unrestricted freedom of access into the country or exit out of the country is therefore not permitted. This is regulated in India by law and the basic statute is the Customs Act 1962. It governs the entry and exit of different categories of goods and passengers into or outside the country.⁴⁶ The government is given the power to assign customs ports and airports where alone the imported goods can be brought in for unloading or export goods loaded on ships and aircrafts. Alike powers that also has been given to the government are that they are able to notify the places, which alone shall be the Land Customs Stations for clearance of imported goods or goods to be exported by land or by inland water. There is a possibility that the routes of passage by land and inland water into or out of the country can be controlled. These provisions have been very useful especially when it comes to regulating traffic for adjacent countries like Nepal.⁴⁷

3.3.1 The role of the custodian

The Customs have authorized and appointed custodians when it concerns imported goods by both sea and air. All the imported goods that are unloaded in a Customs area will remain in their custody until these are ready for either home consumption or are warehoused or transhipped as the laws have provided. Since the traffic with containers has grown the facility of

⁴⁴ The Accessories (Condition) Rules 1963, section 2.

⁴⁵ The determination, by the authority, of a question of law or fact specified in the application regarding the liability to pay duty in relation to an activity which is proposed to be undertaken, by the applicant.

⁴⁶ Central Board of Excise and Customs Manual, S.No. 1 section 4.

⁴⁷ Ibid, section 5.

customs clearance at the interior centres in the country has been provided by opening various Inland Container Depots (ICD), they have the function as Dry Ports. All the goods are transferred to the internal Dry Ports where they are kept with the appointed custodian until the customs are cleared. When the custodian has taken the goods from the carrier, he arranges its proper storage and safety. After that he then allows clearance to the importers but only after they have fulfilled all the customs formalities, paid the necessary duties and other charges, discharge other obligations before they are allowed to take their goods into the country and the customs have given a clear permission for clearance out of the customs area.⁴⁸

3.3.2 The handle of import and export cargo

The different port trust and other authorities in the public and private sectors handle the import and export cargo when it is kept in their custody at various ports, international airports, ICDs. All the cargo handling and the custody at the international airports is mostly entrusted to International airport authority of India. To make it easier for the cargo that waits for pending customs clearance, a few cargo complexes with appropriate storage facilities have been set up at most international airports. A few new ICDs have opened at various industrial centres as a facilitation measure.⁴⁹ Most of the import and export cargo are handled at different seaports. There are a lot of guarding and looking after at the seaports. The custodians have the important task to ensure safe custody of the goods until they will be delivered.⁵⁰ The customs authorities have enough office space and necessary facilities in the dock area to carry out their functions in relation to imports and exports, they have the possibility to inspect and examine the goods, which are imported or presented for exportation before customs clearance facilities.

3.3.3 The procedure for imported and exported goods

If the goods are imported in a vessel or aircraft, it attracts customs duty. Unless the goods are not meant for customs clearance at the port or airport of arrival by particular vessel or aircraft and are intended for transit by the same vessel or aircraft or transshipment to another customs station or to a place outside India, the importers have to give detailed customs clearance formalities of the landed goods.⁵¹ Regarding transit goods, the customs allows transit without payment of duty if these are mentioned in import report for transit to any place outside India.⁵² Goods brought in by particular vessel or aircraft for transshipment to another customs station do not need to

⁴⁸ Central Board of Excise and Customs Manual, S.No. 1 section 7.

⁴⁹ Ibid, section 8.

⁵⁰ The Customs Act 1962, section 45.

⁵¹ Ibid, section 54.

⁵² Ibid, section 53.

have detailed customs clearance formalities at the port or airport of landing. In contrast to this, the carrier and the concerned agencies have to follow a simple transshipment procedure. After the arrival of the goods at the other customs station, the customs clearance formalities have to be in accordance with by the importer. Transshipment of goods could occur after unloading to a port outside of India, simpler transshipment procedure is prescribed, and there is no requirement to pay duty.⁵³

Regarding the offloaded goods, the importers can make a choice. They can either clear the goods for home consumption after payments of the duties leviable or they can clear them for warehousing without immediate discharged of the duties leviable in terms of the provisions concerning the warehouse in the Customs Act. Regarding the consumption or warehousing, every importer is required to file in the terms of an entry, called the Bill of entry.⁵⁴

SEMC has to consider what kind of custom duties they may be obliged to pay. They have to decide how they want to import their goods as well.

3.4 Classification system for goods

Importation of goods is charged with customs duties. Regarding some goods, customs duties are also charged on the act of exportation. There is no single rate of customs duty by the importing or exporting country, when it enter the international trade they are grouped into exclusive similar categories or class of goods and calculated on a basis of well defined criteria. The sub division and calculation of all the goods that enter international trade together with well defined rules of interpretation, form the term nomenclature of goods. The nomenclature is utilised by the government as the basis for prescribing appropriate duty on goods imported or exported. The nomenclature in combination with the duty rates is called the Tariff. Since the tariff normally is a part of the Tariff Act in a country, it is called the “Tariff Schedule”.⁵⁵

“A good nomenclature of goods should make sure that;

1. that every manufactured product will get covered under a code number uniformly applied the world over.
2. that a set of rules is a available for interpretation.
3. that the nomenclature is accepted internationally as a technical and legal basis for improving trade relations amongst countries.
4. that a statistical base, suitable for computerisation is available”.⁵⁶

Brussels Tariff Nomenclature, evolved by the world body, Customs Cooperation Council, fulfilled the need of the nomenclature. With the aim to facilitate trade flow and analysis of trade statistics in a more coordinated manner, the Customs Cooperated Council⁵⁷, developed the Harmonised Commodity Description and Coding System in 1986. India adopted this nomenclature in 1986. The Customs Tariff is totally united with the HS. The

⁵³ The Customs Act 1962, section 54 (2).

⁵⁴ Ibid, section 46.

⁵⁵ Central Board of Excise and Customs Manual, S. No. 4 section 1.

⁵⁶ Ibid, section 2.

⁵⁷ Renamed as World Customs Organisation WCO.

Central Excise Tariff is also very united with the HS at the four-digit level. Regarding the six-digit level, the proper enumeration and subdivision of products is done keeping in view the goods that enter the trade.⁵⁸

To uniform the interpretation of the HS, the World Customs Organisation has published a detailed Explanatory notes to different headings to explain their scope. This is the basis for the interpretation of the HS.⁵⁹ The WCO are discussing the classification of individual products in its committees. They also give classification opinion on them. Even though this kind of information is not binding in nature, it provides a useful guide for the classification of goods.⁶⁰

Since different products have different digits, it is crucial for SEMC to know which product they want to import and export. The most interesting products for SEMC are the products made of plastic and rubber, since they want to import these from Asia.

3.5 The restrictions regarding import and export

In sections in the Customs Act, it is regulated that any goods, which are imported or attempted to be imported and exported or attempted to be exported, are liable to confiscation.⁶¹ If the importation is carried out improperly and if there are any attempts to export goods improperly the Customs Act provides for penalty. Concerning goods that are prohibited, the Adjudicating Officer can impose penalty up to five times the value of the goods. Since there is a possibility that this can happen, it is extremely necessary that the trade know what kind of prohibitions and restrictions that are in force before they consider importing or exporting any goods.⁶²

The definition of prohibited goods is any goods where the import or export of such is subject to any other prohibition under the Customs Act or any other law for the time being in force.⁶³

Export or import of goods can be declared as absolute or conditional prohibited by the Central Government.⁶⁴ The purposes referred to in the first sub-section are listed in section 11 (2). There have been a lot of notifications from the Central Government to prohibit import of sensitive goods.

The Ministry of Commerce has placed certain goods under restricted categories for import and export. The Central Government are empowered to make provisions for prohibiting, restricting or otherwise regulating the import and export of goods.⁶⁵ Some goods are strictly prohibited regarding import and export while some can be imported or exported with a licence.⁶⁶

⁵⁸ Central Board of Excise and Customs Manual, S. No. 4 section 2-3.

⁵⁹ To get more information about the HS-system, Moëll Christina "Harmoniserade tulltaxor. Införlivande, tolkning och tillämpning av internationella regler för varuklassificering".

⁶⁰ Ibid, section 4.

⁶¹ The Customs Act 1962, section 111 and section 113.

⁶² Ibid, section 112 and 114.

⁶³ Ibid, section 2 (33).

⁶⁴ Ibid, section 11.

⁶⁵ The Foreign Trade (Development and Regulation) Act 1992, section 3 and 5.

⁶⁶ Ibid, section 9 (2).

4 Indian duty

4.1 Basic duty

Under the customs laws there are a few various types of duties that are leviable. One is the basic duty; it is levied under the Customs Act. The rate can vary from 5% to 40%, depending on different items.

4.2 Additional Duty (Countervailing Duty-CVD)

The additional duty is levied under section 3 (1) of the Customs Tariff Act 1985, it is equal to excise duty levied on a product manufactured or produced in India. In a situation where a like product is not manufactured or produced in India, the duty payable is the excise duty that would be leviable on that product if it had been manufactured or produced in India. In the case where the product is leviable at different rates, the rate applicable is the highest rate among them. That kind of duty is leviable on the value of goods plus basic custom duty payable.⁶⁷

Additional duty is used to compensate duty on inputs that are being used by Indian manufactures. It is levied under section 3(3) of the Customs Tariff Act and this duty can be charged on all the goods by the Central Government to counter balance excise duty leviable to raw materials, components and other inputs similar to those used in the production of such goods.

Up until the 30th of April 2007, there was an exemption notification concerning additional duty. The exemption covered part, components and accessories of mobile handsets including cellular phones.⁶⁸

4.3 Anti-dumping duty

Foreign sellers abroad may export into India goods at prices below the amounts charged by them in their domestic markets, in turn to capture Indian markets to the disadvantage of Indian industry. This is called dumping.⁶⁹ If goods have been sold at less than normal value, the Central Government may levy additional duty equal to the margin of dumping on that kind of articles. This is done to prevent dumping. Pending determination of margin of dumping, such duty may be provisionally

⁶⁷ India Mart, http://finance.indiamart.com/taxation/custom_duty/index.html (070530) p. 1.

⁶⁸ Custom Tariff 2006-2007, chapter 85 section XVI.

⁶⁹ To get more information about anti-dumping, Li Wenxi, "Anti-dumping Law of the WTO/GATT and the EC. Gradual Evolution of Anti-Dumping Law in Global Economic Integration".

imposed. The duty is finally determined after the exact rate of dumping. The Central Government may vary the provisional rate of dumping duty.⁷⁰ Even though goods are imported indirectly or after changing the condition of goods, the dumping duty can be imposed. There are a few restrictions on imposing dumping duties concerning countries that are signatories to the GATT⁷¹ or on countries given “Most Favoured Status” under an agreement. If the Central Government can prove that imports of such goods in India at that kind of low prices causes material injury to Indian industry, the dumping duty can be levied on imports concerning those countries.⁷²

4.4 Protective duty

The Central Government may levy protective antidumping duties at the rate recommended on specified goods to protect the interest of Indian industry. These duties levy notification must be introduced in the Parliament in the next session by way of a bill or in the same session if Parliament is in session. The notification ceases to have force if the bill is not passed within six months of introduction in Parliament, but the action already undertaken under the notification remains valid. This kind of duty will be payable up to the specified date in the notification. There is a chance that protective duty may be cancelled or varied by notification. This special notification must also be placed before the Parliament for approval.⁷³

4.5 Duty on bounty feed articles

If a foreign country subsidises its exporters for exporting goods to India, the Central Government may then import additional duty equal to the amount of such subsidy or bounty⁷⁴. Additional duty can be collected on a provisional basis, if the amount of subsidy or bounty cannot be clearly determined immediately. Difference may be collected or refunded after a final determination.⁷⁵

4.6 Export duty

This kind of duty is levied on export of goods. There are only a few articles like skins and leather that are subject to export duty. This duty's main purpose is to restrict exports of certain goods. The need to increase import and export duties has granted the Central Government emergency powers to

⁷⁰ India Mart, http://finance.indiamart.com/taxation/custom_duty/index.html (070530) p. 2.

⁷¹ The General Agreement on Tariffs and Trade is a multilateral trade agreement that regulates trade with goods across countries.

⁷² India Mart, http://finance.indiamart.com/taxation/custom_duty/index.html (070530) p. 2.

⁷³ Ibid, p. 2.

⁷⁴ Reward, price.

⁷⁵ India Mart, http://finance.indiamart.com/taxation/custom_duty/index.html (070530) p. 3.

do so, if the need arises. This increase in duty must make its way to the Parliament through a notification within the session. If it, at the time, is not a session, the notification has to be placed within seven days when the next session starts. The approval time for the notification is 15 days.⁷⁶

⁷⁶ India Mart, http://finance.indiamart.com/taxation/custom_duty/index.html (070530) p. 3.

5 Central excise in India

Central excise duty is an indirect tax that is levied on goods manufactured in India. The Central Government administers the tax. The terms that regulate the central excise duty are levied in the Central Excise Act 1944. The rates of duty are not regulated in the same act; they are prescribed under the Schedule I and II of the Central Excise Tariff Act 1985.

The event that is taxable under the central excise law is manufacturing and the liability of central excise duty will arise as soon as the goods are manufactured. The duties that are levied under Additional Duties Act are also collected by the Central Excise Officers.⁷⁷

Up until 1969, a physical control system existed wherein each clearance of manufactured goods from the factory was done under the supervision of the Central Excise Officers. The self-removal procedure introduction was a partition in the excise procedures. After the change of procedure the assessors were allowed to quantify the duty based on approved classification list and the price list, they also had the power to clear the goods on payment of appropriate duty.⁷⁸

The invoice-based system came into force in 1994 and all the clearances are now effected on manufacturer's own invoice. In 1996 came the self-assessment system, which means that the assessor himself assesses his tax return and the Department scrutinise it, or conducts selective audit to ascertain accuracy of the duty payment. The assessor has to declare the classification and value of the goods, instead of obtaining approval of the same from the Department.⁷⁹

The Central Board of Excise and Customs administers the central excise law through its field offices the Central Excise Commissionerates. The country is divided into ten zones and a Chief Commissioner of Central Excise controls each zone. At most, there are 61 Commissionerates in these zones controlled by the Commissioner of Central Excise. The following formations are Divisions and Ranges that are controlled respectively by Deputy or Assistant commissioners of Central Excise and Superintendents of Central Excise.⁸⁰

The Central Excise Department follows two types of procedures for the enforcement of the central excise law and collection of central excise duty. They are:

- a) Physical control – only applicable to cigarettes.
- b) Self-Removal Procedure – applicable to all the other goods produced or manufactured within the country. The assessor can determine himself the duty liability on the goods and clearance of the goods.⁸¹

⁷⁷ Central Excise Manual, chapter 1 part II, section 1.1-1.2.

⁷⁸ Ibid, section 1.3.

⁷⁹ Ibid, section 1.4.

⁸⁰ Ibid, section 2.1.

⁸¹ Ibid, section 2.2.

5.1 The tax payers assistance

The taxpayers in the Commissionerates of Central Excise and Divisional Offices have instructions from the CBEC regarding their assistance. These offices are duty bound for providing necessary guidance to the public in all matters concerning Central Excise Law, procedure, tariff and exemptions.⁸² One of the Commissioners of Central Excise tasks is to position officers with knowledge of appropriate rank, like senior inspector or superintendent to be in charge of Taxpayers Assistance Unit in each of the Commissionerate and Divisional headquarter. This means that the officers will have access to the Deputy and Assistant Commissioners, Additional and Joint Commissioners and Commissioner to seek their advice and guidance when any genuine doubts may arise. Besides helping the taxpayers with offering advice to the assesses, the Taxpayers Assistance Unit help them in meeting the officer concerned for necessary guidance and clarification where it may be needed.⁸³

To have such a responsive tax administration as possible, the Board has decided that all intimations, declarations and queries received from the Members of trade and industry should be handled within a special time limit and with a sense of responsibility and accountability. Certain directions have been issued to the central excise field formations to be able to achieve the above-mentioned directions.

1. All the declarations and intimations, if sent by fax, e-mail, post or by Courier, have to be accepted by the fields' formations.
2. Appointments should be given on e-mail on request from the trade.
3. All queries and replies that are sent by e-mail should be accepted.
4. If a query are received from the trade, it must be answered within a maximum of four weeks from the date of receipt.
5. The best way to make an e-mail an effective mode of communication between the Department and the public, is to get e-mail connectivity to all offices in the field formations and to keep them properly maintained. A wide publicity of the e-mail address should also be given.⁸⁴

⁸² Central Excise Manual, chapter 1 part II, section 3.1.

⁸³ Ibid, section 3.2-3.3.

⁸⁴ Ibid, section 3.4.

6 Indian foreign trade policy

For India to become a major player in the world trade, there need to be an encompassing comprehensive view for the overall development of the country's foreign trade. Even though increase of export is of vital importance, India has to facilitate those imports, which are required for the stimulation of the Indian economy.

The Minister of Commerce and Industry has a goal for India with their Foreign Trade Policy 2004-2009. It is to double India's percentage share of global merchandise trade within the next five years and to act as an effective instrument of economic growth by giving a trust to employment generation. It is important to have coherence and consistency among trade and other economic policies to be able to maximize the contribution of such policies to development. During the incorporation of the existing practice of enunciating an annual Export and Import Policy, it is necessary to go further and take an integrated approach to the developmental requirements of India's foreign trade.⁸⁵

Trade can be seen as a means to economic growth and economic development. The primary purpose has to be the stimulation of greater economic activity. The base of the Foreign Trade Policy is exactly the primary purpose and it is built on the two main objectives mentioned above. To achieve these two objectives India has to adopt a few strategies. A couple of them are

- to simplify procedures and to bring down the transaction costs, neutralize occurrence of all levies and duties on inputs used in export products⁸⁶,
- make the development of India as a global centre for manufacturing, trading and services much easier,
- make the technological and infrastructural upgrade of all the sectors of the Indian economy easier and at the same time attaining internationally accepted standards of quality⁸⁷,
- try to both physically and virtually upgrade their infrastructural network to international standards, which are related to the Foreign Trade chain,
- the Board of Trade shall be revitalised by redefining its role and give it due recognition and educate experts on Trade Policy⁸⁸.

The Foreign Trade Policy is a roadmap for the development for India's foreign trade. It holds the most basic principles and points India to the right direction. India is hoping for partnerships with business and industry to make this Policy work out the way they want.

⁸⁵ The Foreign Trade Policy 2004-2009, preamble p. 1.

⁸⁶ Based on the fundamental principle that duties and levies should not be exported.

⁸⁷ The best way to make it are through import of capital goods and equipment and at the same time increase value addition and productivity.

⁸⁸ The Foreign Trade Policy 2004-2009, preamble p. 1.

It is therefore very important for India to give SEMC the best options so that they want to establish a new business there. It will raise a lot of new opportunities and gain them both.

6.1 The new tasks of the Board of Trade

The Board of Trade has been given a clear and dynamic role in advising the Government on issues related to the Foreign Trade Policy. Since India want to increase their export there will be a rather large interaction between the Board of Trade and the Government.⁸⁹

Some terms of reference for the Board of Trade are to advise the Government on policy measures for preparation and implementation of both short and long-term plans for increasing exports in the light of emerging national and international economic scenarios. They will also examine the issues that are considered as relevant for promotion of India's foreign trade and strengthen the international competitiveness of Indian goods and services.⁹⁰

6.2 Provisions regarding imports and exports

If the imports and exports are regulated in the provisions of this policy or any other law that are in force they are not free. The item concerning the import or export shall be specified in ITC(HS)⁹¹ and published and notified by the Director General of Foreign Trade. All the importers and exporters have to obey the provisions of the Foreign Trade (Development and Regulation) Act 1992, the Rules and Orders made there under and also the provisions of the FTP and the terms and conditions of any licence, certificate or permission that have been granted to them. In addition to that, all the imported goods shall be subject to domestic laws, rules, orders, regulations, technical specifications, environmental and safety norms as applicable to domestically produced goods.⁹²

If a question or doubt arises concerning the interpretation of any provision in this Policy, the question or doubt has to be referred to the Director General of Foreign Trade. The Director General of Foreign Trade will also deal with any question or doubt arising from whether a licence, certificate or permission have been issued in accordance with the FTP and questions and doubt concerning the scope and content of such documents.⁹³

The Director General of Foreign Trade has the power to grant permission to an exception of the provisions of the FTP or of any other procedure, if the

⁸⁹ The Foreign Trade Policy 2004-2009, chapter 1C.1.

⁹⁰ Ibid, chapter 1C.2.

⁹¹ Explanation are given in Supplement D.

⁹² The Foreign Trade Policy 2004-2009, chapter 2.1-2.2.

⁹³ Ibid, chapter 2.3.

ground is a valid burden to the applicant or that a strict application is likely to have an adverse impact on trade.⁹⁴

Every import and export has to be made with an Importer-Exporter Code number if it is not specifically exempted. This number shall be granted by application by the competent authority.⁹⁵ The goods that are imported in agreement with this Policy, may be exported in the same or significantly the same form even though a licence, certificate or permission has not been issued, on the condition that the item to be imported or exported is not mentioned as restricted for import or export in the ITC(HS).⁹⁶

⁹⁴ The Foreign Trade Policy 2004-2009, chapter 2.5.

⁹⁵ The Foreign Trade Policy 2004-2009, chapter 2.12.

⁹⁶ Ibid, chapter 2.35.

7 The import policy in India

Some basic factors influence India's import policy. Those are the economic needs of the country, effective use of foreign exchange and industrial as well as consumer requirements. The policy on the import side has three objectives, which are:

1. to make necessary imported goods more easily available, including essential capital goods for modernizing and upgrading technology;
2. to simplify and streamline procedures for import licensing;
3. to promote efficient import substitution and self-reliance.

India has only four prohibited goods and they are tallow fat, animal rennet, wild animals and unprocessed ivory. They have a restricted list but most of the restrictions on there are on security grounds, health and environmental protection or because the goods are reserved for production by small or tiny enterprises. They are home based or village based and only require low skills and therefore employ a large number of people.⁹⁷

India allows import free of duty for export production under a duty exemption scheme. There are input-output norms specified for over 4200 items. These norms specify the amount of duty-free import of inputs allowed for specified products to be exported.

Imports of capital goods and intermediates do not have any quantitative restrictions. Importation of capital second-hand goods is permitted if they have a minimum lasting life of five years. There is a special scheme that allows exporters to import capital goods including computer systems, at concessionary customs duty, subject to fulfilment of specified export obligations.⁹⁸ The scheme is called the Export Promotion Capital Goods Scheme.

7.1 Regulations and procedures regarding importation

All of the imported goods fall into one of the four categories:

1. Freely imported items; most of the capital goods fall into this category. These items do not require import licences and have the possibility to be freely imported by any individual or entity.
2. Licensed imports; some items can only be imported if they have licences and only by actual users.
3. Canalised items; items under this category can only be imported by specific public-sector agencies.

⁹⁷ India Mart, http://finance.indiamart.com/exports_imports/importing_india/index.html (070530) p. 1.

⁹⁸ Ibid, p.1.

4. Prohibited items; the items that are completely prohibited from importation are tallow fat, animal rennet and unprocessed ivory.⁹⁹

When a company import different goods they have to pay duty, the rate is the same in every state. The rate depends on what the company wants to import. To find out what the exact rate for the relevant good is one have to look in the Custom Tariff 2006-2007.¹⁰⁰

Regarding goods that SEMC would import it would concern electronics from adjacent countries and the rate would probably be around 12, 5%.¹⁰¹ It is therefore once again important to know exactly what goods or products SEMC wants to import.

⁹⁹ India Mart,
http://finance.indiamart.com/exports_imports/importing_india/regulations/index.html
(070530) p. 1-2.

¹⁰⁰ Information provided by Björn Savlid, Exportrådet mail Tuesday February 13th 2007 11:56.

¹⁰¹ Custom Tariff 2006-2007, part II chapter 85.

8 The export policy in India

The major focus of India's trade policy is exports and a thrust area is exports involving higher additions. Most items can be freely exported from India. To avoid shortages in the domestic market, to conserve national resources and to protect the environment, a few items have been subject to export control.¹⁰²

Export profits are exempted from income tax. The inputs that are required to be imported for export production are exempted from the basic customs duty. Export Oriented Units and Export Processing Zones have the benefit of special incentives like duty free import of capital goods and raw materials for the purpose of export production. A special fund, the Brand Equity Fund, has been set up with the purpose of popularize high quality India brand in the world market.¹⁰³

8.1 General and regional incentives

The Central and State Governments offer several no tax incentives in the shape of capital subsidies and concessional credits, in the interest of developing backward areas, export or some specific industries. A distinction between domestic and foreign investors is not being made.¹⁰⁴

Special incentives for export is given in the form of cash assistance or cash compensatory support on exports of certain items, duty drawback.¹⁰⁵

If industrial units are set up in specific backward districts they become eligible for a Central Government subsidy on their fixed capital investment and for concessional financing from national financial institutions. In certain selected areas, the Central Government also provides a transport subsidy. In addition to all of this, the State Governments offer a variety of incentives and facilities, such as land on concessional terms, water and power at reduced rates, concessions in sales tax and octroi¹⁰⁶ and other subsidies.¹⁰⁷

¹⁰² India Mart,

http://finance.indiamart.com/exports_imports/exports_from_india/index.html (070530) p.1.

¹⁰³ Ibid, p. 1.

¹⁰⁴ India Mart, http://finance.indiamart.com/exports_imports/incentives/index.html (070530) p. 1.

¹⁰⁵ A refund of central excise and customs duties levied on different materials.

¹⁰⁶ A municipal levy of duty on entry of goods into a specified local area for consumption or sale. The rate of Octroi Duty varies from local area to local area.

¹⁰⁷ India Mart, http://finance.indiamart.com/exports_imports/incentives/index.html (070530) p. 1.

8.2 General tax incentives regarding export

The investors in India are offered many incentives from the Government; it is done to stimulate industrial growth and development. The offered incentives are often given in coherence with the Government's economic philosophy and are revised on a regular basis to accommodate new areas of emphasis. Some of the most important incentives that significantly reduce the effective tax rates for the beneficiary companies are:

1. Five year tax holiday for:
 - Power projects.
 - Firms engaged in exports.
 - New industries in states and for new industrial units established, in electronic hardware/software parks.
 - Export Oriented Units and units in Free Trade Zones
2. Tax deductions of 100% of export profits.
3. Deduction of 30% of net (total) income for ten years for new industrial undertakings.
4. Deduction of 50% on foreign exchange earnings by construction companies, hotels and on royalty, commission etc. earned in a foreign exchange.
5. Deduction in respect of certain inter-corporative dividends to the extent of dividend declared.¹⁰⁸

8.3 The Department of Scientific and Industrial Research (D.S.I.R.)

The D.S.I.R. has a scheme called the Transfer and Trading in Technology (TATT), this scheme can grant assistance for technology exports. The prospective technology or service exporters can identify the possible export opportunities, apart from financial assistance, by studying the technology profiles of various developing countries that have been prepared with the support of D.S.I.R. to identify the technology needs of those countries. To finance efforts for technology exports, the D.S.I.R. is providing support by grant. How large a grant is and its eligibility is determined case to case, but grant can extend to 100% of the eligible expense.¹⁰⁹

¹⁰⁸ The High Commission of India in Singapore, http://www.embassyofindia.com/doing_business_india_investincentive.asp#central (070530) p.1.

¹⁰⁹ India Mart, http://finance.indiamart.com/exports_imports/incentives/dsir.html (070530) p. 1.

9 Tax incentives for Indian companies

There are many incentives that Indian tax laws provide, especially for industrial growth and development in specific areas, subject to the fulfilment of specified conditions. A few of these incentives are:

- If certain conditions are fulfilled, companies that are engaged in telecommunication service have the right to a tax deduction of 100 % of the profits for the first five years and 30 % of the profits for the next five years. This is a deduction in addition to the deduction of expenses that the companies have brought on themselves for business purposes.
- If specified conditions are fulfilled, 100 % of the profits and gains from an undertaking located in any Free Trade Zone or Export Processing Zone or 100 % Export Oriented Unit from the export of articles or things are tax deductible for ten consecutive years. It is not allowed to make any deduction in respect of any year commencing after 1 April 2010 and thereafter.
- If specified conditions are fulfilled, a tax deduction of 100% for the first five years and 50% for the next two years is accepted concerning the profits and gains derived from an undertaking in a Special Economic Zone. After that, for the next three years, the deduction will be restricted to 50 % of the amounts credited to a special reserve created for this purpose.
- If specified conditions are fulfilled, profits and gains derived by an undertaking located in any Export Processing Zone are tax deductible. Deduction is either 100 % for 10 consecutive years or 100 % for the first five years and 30 % after that, which depends on the time of starting the manufacturing activities.¹¹⁰

These are some of the incentives that SEMC could receive if they set up a business in India.

9.1 Incentives offered by States

India is a federal country that consists of States and Union Territories. Even the States are partners in the economic reforms that are being undertaken in the country. To simplify the rules and procedures for setting up and operating the industrial units, most of the States are making serious efforts for that to become a reality. In most of the States, a Single Window System is in existence, for granting approval for setting up industrial units. With an aim to attract foreign investors in their states, many of them are offering

¹¹⁰ Ministry of External Affairs Government of India, India in business, <http://www.indiainbusiness.nic.in/investment/taxation.htm> (070530) p. 6-7.

incentive packages in the form of various tax concessions, capital and interest subsidies and reduced power tariff.¹¹¹

¹¹¹ Foreign Direct Investment Manual 2003, p. 36.

10 Doing business in India

A foreign company have two options when they are planning to set up a business in India. They can either do it as an Indian company or as a foreign company.

After the foreign company has registered either as a wholly owned subsidiary or as a joint venture, they can continue their registration in the relevant Special Economic Zone (SEZ) to receive certain tax reductions and other advantages that the SEZ can offer.

The above-mentioned information concerns the Export Oriented Units (EOU) as well. The foreign company must first register and then it can apply for an EOU-status to be able to get access to the advantages that are associated with that status.¹¹²

10.1 As an Indian company

By incorporating a company under the Companies Act 1956, through either wholly owned subsidiaries or a joint venture, a foreign company can commence operations in India.¹¹³ The foreign equity in this kind of Indian companies can be up to 100% depending on the requirements of the investor, subject to equity caps and in respect of the area of activities under the FDI policy. By forging strategic alliances with Indian partners, the foreign company can set up their operations in India.¹¹⁴

A foreign investor may get the following advantages by setting up a joint venture:

- Established distribution/marketing set up of the Indian partner
- Available financial resource of the Indian partner
- Established contacts of the Indian partners which help smooth the process of setting up operations

The three most common types of joint venture companies are:

1. Two parties that can be either individuals or companies, both of them residents or one of them non-resident, incorporate a company in India. One parties business is transferred to the company and shares are issued by the company and subscribed by that party. The second part subscribes for the shares in cash.
2. As an alternative, the two parties, mentioned above, starts a new business. In the new business, they subscribe to the shares, in cash, of the joint venture company in agreed proportion.
3. The promoter shareholder of an already existing Indian company and a third party, which have the possibility to be either individual or a company, either non-resident or both residents, can collaborate to

¹¹² Information provided by Björn Savlid, Exportrådet mail Friday March 30th 2007 08:22.

¹¹³ To get more information about joint ventures, Tomlinson, James W.C., "The joint venture process in international business: India and Pakistan, James W.C. Tomlinson".

¹¹⁴ Department of Industrial Policy & Promotion, Investor guidance, entry strategies for foreign investors, p. 1. <http://siadipp.nic.in/policy/entry.htm> (070530).

jointly take the business of that company forward. The third party takes on that parts shares through payment in cash.¹¹⁵

There is a possibility for a foreign company to set up a wholly owned subsidiary in a sector where 100% FDI is permitted under the FDI policy. As soon as a company has been duly registered and incorporated as an Indian company, it is subject to all the Indian laws and regulations that apply to a domestic company.¹¹⁶

The alternative that I think would give SEMC the most benefits is as an Indian company as a joint venture. It would fit their requirements for a new establishment.

10.2 As a foreign company

If a company chooses to set up a business in India as a foreign unincorporated company, there are three ways to approach it:

1. Liaison office/Representative office
2. Project office
3. Branch office

These kinds of companies can undertake any sort of permitted activities. They have to register themselves with the Registrar of Companies within 30 days of setting up a place of business in India.

Liaison office acts as a channel of communication between the principal place of business or head office and entities in India. These kinds of offices cannot undertake any commercial activity directly or indirectly and cannot therefore earn any income in India. The role of a liaison office is to collect information about possible market opportunities and providing information about the company and its products to prospective Indian customers. They can promote export and import from and to India and facilitate technical and financial collaboration between parent company and companies in India. It is the Reserve Bank of India (RBI) that grant approval for the establishment of a liaison office in India.¹¹⁷

The foreign companies that are planning to execute specific projects in India can set up temporary project offices in India. First, now, the RBI has granted general permission to foreign entities to establish project offices subject to specified conditions. These offices do not have the power to undertake or carry on any activity relating and incidental to execution of the project. If the RBI has granted general permission, the project offices may remit the surplus of the project on its accomplishment outside India.¹¹⁸

Foreign companies engaged in manufacturing and trading activities abroad are allowed to set up branch offices in India. This is only allowed if the prospective branch office has one of these purposes:

1. export/import of goods
2. rendering professional or consultancy services

¹¹⁵ Seth Associates, setting up a joint venture in India, p. 1
http://www.sethassociates.com/setting_up_a_jont_venture_in_india.php (070502).

¹¹⁶ Ibid, p. 2.

¹¹⁷ Department of Industrial Policy & Promotion, Investor guidance, entry strategies for foreign investors, p. 2.

¹¹⁸ Ibid, p. 3.

3. carrying out research work, in which the parent company is engaged
4. promoting technical or financial collaborations between Indian companies and parent or overseas group company
5. representing the parent company in India and acting as buying/selling agents in India
6. rendering services in Information Technology and development of software in India
7. rendering technical support to the products supplied by the parent/group companies
8. foreign airline/shipping company¹¹⁹

Since a branch office is not allowed to carry out manufacturing activities on its own, they are permitted to subcontract these to an Indian manufacturer. Branch offices that have been established with the approval of RBI may remit the profit of the branch outside India.

There are certain branch offices that are on a so-called stand-alone basis, which mean that these offices are isolated and restricted to the Special Economic Zone and no business activity or transaction will be allowed outside the SEZs in India. This restriction includes branches and subsidiaries of its parent office in India. There is no need for approval from the RBI for a company to establish a branch or a unit in SEZ to undertake manufacturing and service activities subject to specified conditions.¹²⁰

Foreign companies that operate in India through a branch are allowed to deduct management and general administrative expenses that the companies have brought on themselves by the head office outside of India. These expenses are restricted to the lower of: 5 % of adjusted total income and expenses linked to the Indian business.

The expenses are restricted to 5 % of the average total income, when the adjusted total income for a year is a loss. A few incentives are available for specific types of earnings in foreign exchange. At present, 50 % of the profits from the export of select goods and software are deductible while computing taxable income. There is also a possibility for deductions regarding other different items of income earned in a foreign exchange.¹²¹

If SEMC would like to establish their new business as a foreign company the best way for them would be as a branch office since they are interested in importing goods.

¹¹⁹ Ibid, p. 3.

¹²⁰ Department of Industrial Policy & Promotion, Investor guidance, entry strategies for foreign investors, p. 4.

¹²¹ Ministry of External Affairs Government of India, India in business, <http://www.indianbusiness.nic.in/investment/taxation.htm> (070502) p. 3.

11 Trade zones in India

11.1 Free Trade Zones - FTZ

There are many free trade zones in India. No excise duties are payable on goods manufactured in these zones if they are made for export purposes. All goods brought into these zones from different parts of the country are brought without the payment of any excise duty. There are also no customs duties on imported raw material and components used in the manufacturing of such goods being exported. If the unit's entire production is not sold outside the country, the unit has the provision of selling 25% of their production in India. Regarding that sale, the excise duty is payable at 50% of basic duty plus additional customs or normal excise duty payable if the goods were produced elsewhere in India, whichever is the highest.¹²²

11.2 Export Oriented Units – EOU

There are two ways to establish production facilities in India. If the company is export oriented, they can register as an Export Oriented Unit. The advantages with this kind of units are that one can pay lower excise/customs duty, or in some cases, do not pay at all. These companies also pay a lower tax.¹²³

Export Oriented Units can be established anywhere in India, they are exporting 100% products. There are a permissible certain fixed percentage of sales in the Domestic Tariff Area. The EOU can be set up at any place that is declared as a warehousing station.¹²⁴ There are more than 300 of these kinds of warehousing places in India. A separate unit can be set up even within the factory of manufacturing and as a result, they will save considerably in administrative costs.

An EOU can carry out many activities besides manufacturing. They can import goods for service activities, reconditioning, repairs of imported goods and return to foreign suppliers, destruction of waste and rejects with permission of Assistant Commissioner outside the premises and undertaking job work of repairs and maintenance.

In case of the export orders should dry up, the conversion of EOU to DTA unit by exit or de-bonding is quite easy.¹²⁵

If a company enter into an EOU zone, the foreign company would save/have:

¹²² <http://www.indianindustry.com/trade-information/export-incentives.html> (070530) p. 2.

¹²³ Information provided by Björn Savlid, Exporträdet mail Tuesday February 13th 2007 11:56.

¹²⁴ The Customs Act 1962, section 58.

¹²⁵ <http://www.dateyvs.com/custom06.htm> (070530) p. 3.

- Exemption from excise duty on goods procured from indigenous sources/local markets.
- Full reimbursement of the Central Sales Tax (CST) paid on the purchase from the DTA for production of goods and services as per the EOU scheme. The reimbursement of CST shall be admissible only to those units who get them registered with the Sales Tax authorities.
- Tax holiday to EOU – 100% tax holiday on exports until 2009. The tax exemption is provided to the EOU beginning with the assessment year relevant to the previous year in which the undertaking begins to manufacture. However, no deduction shall be available after the assessment year 2009-2010.

For a company to be able to enter the EOU zone, the foreign company must:

- Have a proposal that focus more on export than imports.
- Should bring export proceeds to India only within 360 days of its export.
- Have positive Net Foreign Exchange (NFE) for a period of five years from the start of the commercial production. Positive Net Foreign Exchange means that the export and DTA sales must be larger than the imports from abroad or other SEZ/EOU.¹²⁶

A 100% Export Oriented Unit is an industrial unit offering for export its entire production, the permitted levels of domestic tariff area sales are excluded. It is a possibility to set up an EOU with a foreign equity participation of up to 100%. To be able to do this, the following conditions are applicable:

1. The entire production and operation of 100% EOUs must be carried out in a customs bonded factory, if not specifically exempt from physical bonding. Goods will be imported into the customs bonded factory.
2. The unit shall start its manufacturing in the bonded area and export its entire production for a period of 10 years ordinarily and 5 years in case of the products are liable to rapid technological change.
3. An approved EOU will execute a bond or legal undertaking with the Development Commissioner concerned. If the EOU will not fulfil the obligations stipulated in the letter of approval or intent, then the unit will be liable to penalty.
4. EOUs have to adhere to the minimum value addition conditions incorporated in the letter of permission/letter of intent/industrial licence given to them.
5. EOUs have to maintain a proper account of the imports, consumption and utilization of the imported materials and exports made by the unit. The Develop Commissioner will receive these accounts on a periodically basis. If an existing industrial unit is operating as both a domestic unit as well as an approved 100% EOU, it is best if it have two distinct identities with separate accounts.
6. EOUs have the permission, with certain limits, to sell parts of the production in the DTA.

¹²⁶ Information provided by Björn Savlid, Exportrådet mail Tuesday February 13th 11:56.

7. To attain export house, trading house or star trading house status for the parent company, the free on board value of export of an EOU can be clubbed with the free on board value of exports of its parents company in the DTA.
8. The supplies that are produced in the DTA under global tender conditions, against payment in foreign exchange, against advance licenses and other licences, and to other EOUs with the permission of the Development Commissioner, will be counted towards the fulfilment of export obligations.¹²⁷

This alternative is the best if SEMC wants to concentrate on export. They will gain a lot if they register their new business as an EOU.

11.2.1 Policy for EOUs

Units that decide to undertake their entire production of goods and services may be set up under the Export Oriented Unit Scheme, Export Processing Zone Scheme, Electronic Hardware Technology Park Scheme or Software Technology Park Scheme. These units may be engaged in manufacture, production of software, agriculture, animal farming, floriculture, poultry and sericulture, to mention a few. Even units that are engaged in service activities may also be considered.¹²⁸

An EOU have the right to import free of duty all types of goods, which includes capital goods. The capital goods are required by it for manufacture, processing or in connection with one of these, all of this has to happen under one condition. That is that these goods are not prohibited items in the Negative List of Imports.

The importation of second hand goods, other than capital goods, is restricted for imports and may only be imported in accordance with a Public Notice or a licence. If those goods do not have any age limit, they may be imported duty free.¹²⁹

An EOU have the possibility to source capital goods from a domestic or foreign leasing company without payment of customs or excise duty, if a firm contract between the two parts exists. If a situation like this occurs, the EOU and the domestic or foreign leasing company jointly have to file the documents to enable import or gain of the capital goods without payment of duty.¹³⁰

A Letter of Permission or a Letter of Intent has to be issued by the Development Commissioner or the designated officer to the EOU. The letter has to have an initial validity period of three years by which the unit has to have commenced production. The competent authority may extend its

¹²⁷India Mart,
http://finance.indiamart.com/exports_imports/export_financing/export_units/index.html
 (070530) p. 1-2.

¹²⁸ India Mart,
http://finance.indiamart.com/exports_imports/export_financing/export_units/procedures.html
 (070530) p. 1.

¹²⁹ The Foreign Trade Policy 2004-2009, chapter 6, section 6.3.

¹³⁰ Ibid, chapter 6, section 6.4.

validity further up to three years. As soon as the unit has commenced its production, the issued Letter of Permission or Letter of Intent shall be valid for a five-year period for the relevant activities. This period may be extended for an additional five-year period at a time.¹³¹

It is only the projects that have a minimum investment of rupees 1 crore¹³² in plant and machinery that are considered for establishment as EOUs under the scheme.¹³³ The applications for setting up units under the EOU scheme, other than proposals for setting up of unit in the service sector, shall be approve or rejected by the Units Approval Committee within 15 days.¹³⁴

EOU are able to sell finished products that are freely importable under the Policy in the DTA, against payment of full duties provided they have achieved positive NFE. An EOU also have the possibility to export goods manufactured by it through another exporter or any other EOU.¹³⁵

If an EOU want to exit the scheme, it may do so with the approval of the Development Commissioner.¹³⁶

11.3 Special Economic Zone – SEZ

The other way to establish production facilities in India is to register a company in a so-called Special Economic Zone (SEZ). These zones are spread out all over India and specialize in special industries. Companies that register in these zones get almost the same advantages like the EOUs, but they also get access to the infrastructure that is available within the zone. These zones accept 100% foreign ownership.¹³⁷

A SEZ is a geographical region where the economic laws are more liberal than a country's typical economic laws. The best way to describe a SEZ is by using the meaning trade capacity development tool. Its goal is to promote rapid economic growth by using tax and business incentives to attract foreign investment and technology.

An appropriate description to a SEZ is by saying that it is a specifically duty free enclave, it shall be deemed foreign territory for the purpose of trade operations and duties and tariffs. All the goods and services that enter the SEZ area from DTA shall be treated as exports and goods coming from the SEZ area into DTA shall be treated as if they are imported.¹³⁸

The SEZ unit has the privilege to import from the DTA without payment of duty, all types of goods and services, capital goods included, whether they are new or second hand, required by it for its activities or in connection therewith, provided they are not prohibited items of imports in the ITC(HS).

¹³¹ The Foreign Trade Policy 2004-2009, chapter 6, section 6.6.

¹³² In India, the sum of ten million especially of rupees.

¹³³ The Foreign Trade Policy 2004-2009, chapter 6, section 6.6 (d).

¹³⁴ Ibid, section 6.7.

¹³⁵ Ibid, section 6.8 (h) and section 6.10. .

¹³⁶ Ibid, section 6.18.

¹³⁷ Information provided by Björn Savlid, Exportrådet mail Tuesday February 13th 11:56.

¹³⁸ The Foreign Trade Policy 2004-2009, chapter 7 section 7.1 (a) (b).

If there are any other law that require permission for import, that law is applicable.¹³⁹

If a firm contract exists between the SEZ unit and a domestic or foreign leasing company, the SEZ unit may source the capital goods from the leasing company. The two companies shall jointly file the documents to enable import and procurement of the capital goods without payment of duty.¹⁴⁰

Every SEZ unit must be a positive Net Foreign Exchange Earner. The calculation of the NFE shall be cumulatively for a period of five years from the commencement of the production.¹⁴¹

The Development Commissioner must approve the applications for the set up of a SEZ unit within 15 days.¹⁴² The SEZ unit have possibility to export goods that are manufactured through a merchant exporter recognised under the Foreign Trade Policy 2004-2009 or any other EOU or SEZ unit.¹⁴³

Another privilege a SEZ unit has is that they can subtract a part of their production or production process through units in the DTA or through other SEZ or EOU, if there is an annual permission of Customs authorities.

Subcontracting a part of production process can be made abroad if the Development Commissioner has given its approval.¹⁴⁴

If a SEZ unit wants to get out of the scheme, they have to have the permission of the Development Commissioner. That kind of exit shall be subject to payment of applicable customs and excise duties on the imported goods. If the unit has not achieved a positive NFE, the exit has to be subject to penalty, which may be imposed by the adjudicating authority under the Foreign Trade (Development and Regulation) Act, 1992.¹⁴⁵

SEZ offers a lot of different employment and have the power to boost the development of improved technologies and infrastructure. The three distinguishing features of a SEZ are that the zones are proposed to be setup by private sector or by State Government¹⁴⁶ in association with the private sector. The private sector has been invited to develop infrastructure facilities in the existing SEZ. The State Government has a leading role in the setup of SEZs and the last one; there is a framework that has been developed by creating special windows under the already existing rules and regulations of the Central Government and State Government for the SEZ.¹⁴⁷

In India, there are 13 functional SEZs and about 61 SEZs that were approved and are under the process of establishment in India.¹⁴⁸

Almost every developing country in the world has realized the need of facilitating international trade for the sustained growth of the economy. The

¹³⁹ Ibid, section 7.2 (b).

¹⁴⁰ The Foreign Trade Policy 2004-2009, chapter 7 section 7.3.

¹⁴¹ Ibid, chapter 7 section 7.4.

¹⁴² Ibid, chapter 7 section 7.7.

¹⁴³ Ibid, chapter 7 section 7.10.

¹⁴⁴ Ibid, chapter 7 section 7.12.

¹⁴⁵ Ibid, chapter 7 section 7.13.

¹⁴⁶ The Special Economic Zone Act 2005, section 2 (zb).

¹⁴⁷ Ministry of Commerce and Industry, Department of Commerce regarding Special Economic Zones, <http://www.sezindia.nic.in> (070530).

¹⁴⁸ Seth Associates, Special Economic Zones – an Indian perspective, http://www.sethassociates.com/special_economic_zones.php (070530) p.1.

way India has tried to commit to liberalisation is through the Government of India. They have adopted a multi-pronged approach to promote foreign investment in India; they have pushed ahead with second-generation reforms and have made several policy changes to achieve this objective. The first time the SEZ policy was introduced in India was in 2000 as a part of the EXIM Policy of India. Since the Government of India realised the need to enhance foreign investment, promote exports from the country and the need that level playing field must be made available to the domestic enterprises and manufacturers to be competitive globally, they announced the introduction of SEZ policy in the country. This was deemed foreign territory for the purposes of trade operations, duties and tariffs.¹⁴⁹

For India to provide an internationally competitive and hassle free environment for export, they allowed units¹⁵⁰ to be set up in SEZ for manufacturing of goods and rendering of services. Operations regarding import and export of the SEZ units are on a self-certification basis. All the units in the zone have to be a Net Foreign Exchange earner. Nevertheless, because of this they would not be subjected to any pre-determined value addition or minimum export performance requirements.¹⁵¹

The setting up of SEZs can happen in the public, private and joint sector or by the Government, according to the policy. In the Special Economic Act 2005, the definition of how a SEZ can happen are either jointly or severally by the Central Government, State Government or any other person for manufacture of goods or rendering services for both or as a Free Trade or a Warehousing Zone.¹⁵²

There is a minimum setup size for a SEZ that handle multi product. It should have a contiguous area of one thousand hectares or more.¹⁵³ The Central Government have the right to prescribe some requirements for the establishment of a SEZ. One is regarding “the minimum area of land and other terms and conditions subject to which the Board shall approve, modify or reject any proposal received by it”. The second requirement is that “the terms and conditions subject to which the Developer¹⁵⁴ shall undertake the authorised operations and his obligations and entitlements”.¹⁵⁵

One of the EXIMS’s features is that the designated duty free enclave to be treated as foreign territory only for trade operations and duties and tariffs. Manufacturing, trading or services are allowed and there is no requirement for licence regarding import.¹⁵⁶

To be able to provide a stable economic environment for the promotion of export and import of goods in a quick and hassle-free manner, the Government of India enacted the Special Economic Zone Act 2005. The

¹⁴⁹ Seth Associates, Special Economic Zones – an Indian perspective, p.1.
http://www.sethassociates.com/special_economic_zones.php (070530)

¹⁵⁰ The Special Economic Zone Act 2005, chapter I section 2 (zc).

¹⁵¹ Seth Associates, Special Economic Zones – an Indian perspective, p.2.
http://www.sethassociates.com/special_economic_zones.php (070530)

¹⁵² The Special Economic Zone Act 2005, chapter II section 3 (1).

¹⁵³ The Special Economic Zone Rules 2006, chapter II section 5 (2) subsection (a).

¹⁵⁴ The Special Economic Zone Act 2005, chapter I section 2 (a).

¹⁵⁵ Ibid, chapter II section 3 (8) sub-sections (a) and (b).

¹⁵⁶ Seth Associates, Special Economic Zones – an Indian perspective, p.2.
http://www.sethassociates.com/special_economic_zones.php (070530).

SEZ Act was enacted to provide for the establishment, development and management of the SEZs for the promotion of exports and for matters connected to that or incidental to it. The export and the foreign direct investment inflows into India were expected to get a big thrust from the SEZ Act. The act itself is considered one of the finest pieces of legislation that represent the future of the industrial development strategy in India. The policy frameworks for SEZs are enacted in the SEZ Act 2005 and the supporting procedures are handled in the Special Economic Zones Rules 2006.

The administrative setup for SEZs is based on a three level basis. The first one is the Board of Approval; it is the apex body in the Department. The second is the Unit Approval Committee at the Zonal level dealing with approval of units in the SEZs and other related issues. The last one is the Development Commissioner¹⁵⁷, which control each zone.

A proposal to set up a SEZ in the private, joint or state sector has to go through the concerned State Government. In turn the concerned State Government send forward the proposal to the Department of Commerce with its recommendations for consideration of the Board of Approval.¹⁵⁸

The Approval Committee, consisting of Development Commissioner, Customs Authorities and representatives of State Government, approves all the proposals for setting up of units in the SEZ.

The SEZ unit has to be located at the specific locations where such zones are developed. If the export orders stops, the conversion of a SEZ to DTA unit is a bit more difficult than from EOU to DTA. The unit have to physically move out of the zone after exit or de-bonding.

I think that this is the most favourable alternative for SEMC. They will receive the most benefits, have access to the infrastructure and a SEZ unit will provide many new jobs for the people that already live in the country. The new business of SEMC will have an extremely good chance of growing into something very profitable, for both India and SEMC.

11.3.1 Benefits to SEZ Units

The goods and services that are exported out of or into India or procured from the DTA by a unit in a SEZ or a Developer shall be exempt from the payment of taxes, duties or cess.¹⁵⁹ A Developer or an entrepreneur in a SEZ unit has many fiscal provisions regarding exemptions, drawbacks and concessions.

When entering into a SEZ, the foreign company would save/have:

- Exemption from customs duty on goods/services imported or exported by SEZ unit.
- Exemption from excise duty on goods produced from DTA by a SEZ unit.
- Exempted of service tax, on taxable services to a SEZ unit, to carry on authorized operations in a SEZ.

¹⁵⁷ The Special Economic Zone Act 2005, chapter I section 2 (h).

¹⁵⁸ Ibid, chapter III section 9 (2) sub-section (a).

¹⁵⁹ The Special Economic Zone Act 2005, chapter III section 7.

- Central Sales Tax exemption on the goods produced from DTA.
- Drawback on goods brought or services provided from the DTA into a SEZ or unit services provided in a SEZ or unit by the service providers located outside India to carry on the authorised operations by the Developer or the entrepreneur, are exempt from any duty of excise¹⁶⁰
- Tax holiday for SEZ units that are engaged in manufacturing, a deduction of:
 - “hundred per cent of profits and gains derived from the export, of such articles or things or from services for a period of five consecutive assessment years beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be, and fifty per cent of such profits and gains for further five assessment years, and thereafter”¹⁶¹,
 - “for the next three consecutive years, so much of the amount not exceeding fifty per cent of the profit as is debited to the profit and loss account of the previous year in respect of which the deduction is to be allowed and credited to a reserve account (to be called the Special Economic Zone Re-investment Reserve Account) to be created and utilized for the purposes of the business of the assessee in the manner laid down in sub-section (1B)”¹⁶².

The sub-section (2) requires that two conditions will be fulfilled for the deduction to be realised. “The amount credited to the Special Economic Zone Re-investment Reserve Account is to be utilised for the purposes of acquiring machinery or plant, which is first put to use before the expiry of a period of three years following the previous year in which the reserve was created. The second condition is until the acquisition of the machinery or plant as aforesaid, for the purposes of the business of the undertaking other than for distribution by way of dividends or profits or for remittance outside India as profits or for the creation of any asset outside India”¹⁶³.

All the domestic sales by SEZ units will be exempt from Special Additional Duty. Domestic sale of finished products is permitted on payment of applicable customs duty.¹⁶⁴

11.3.1.1 State Taxes

To be able to get effect to the provisions of the SEZ Act, the respective State Government may notify policies for Developers and SEZ units. They also have the power to take suitable steps for the enactment of any law for granting exemption from state taxes, levies and duties to a Developer or an entrepreneur.¹⁶⁵

¹⁶⁰ The Special Economic Zone Act 2005, chapter III section 7 and chapter VI section 26.

¹⁶¹ The Income Tax Act 1961, section 10A sub-section (1A) (i).

¹⁶² Ibid, section 10A sub-section (1A) (ii).

¹⁶³ Ibid, section 10AA sub-section (1B) (a) (i) (ii).

¹⁶⁴ See picture in Supplement B.

¹⁶⁵ Seth Associates, Special Economic Zones – an Indian perspective, p. 5.

11.3.2 Net Foreign Exchange – NFE

Every EOU and SEZ units only have to be foreign exchange positive. There are foreign exchange inflows and foreign exchange outflows. The foreign exchange inflows include the export earnings from direct exports, exports through third parties, inter-unit sales and exports to EOU and SEZ. The foreign exchange outflows have an outgo on import of raw materials/consumables, foreign payments of commission/royalty/fees/dividends/interest on External Commercial Borrowings (ECB) and share of amortised value of imported capital goods. The imported capital goods are amortized over ten years and it is only the amortized amount that is included in NFE calculation. Even though the imports are actually not paid for, the values are included in the calculation.¹⁶⁶

To be able to enter the SEZ, the foreign company must:

- have positive NFE for a period of five years from the start of the commercial production. The meaning of Positive Net Foreign Exchange is that the exports and DTA sales must be larger than the imports from abroad or other SEZ/EOU.¹⁶⁷

11.4 The different schemes that encourages exports

India is giving the export the highest priority in the country, since India needs foreign exchange to adverse balance of trade. Almost all the nations are following in the practise of giving encouragement to exports. The Government gives encouragement to exports through different schemes. The main support and supervision comes from the Commerce Ministry of Government of India. Export Promotion Councils have been formed for different categories of products.

The main export incentives for manufactures are:

- Indigenous inputs without payment of excise duty
- No excise is charged on final product
- Imported inputs without payment of customs duty
- No export duty on export of final product
- Bank finance on priority basis and at concessional rate of interest
- Exemption from income tax, sales tax and on final product

Schemes like EOU and SEZ are suited to use when the undertaking is predominantly export oriented and when the requirement of imported capital goods and imported raw materials are high.

The World Trade Organisation (WTO) have restricted that no country can give export incentives as such. The reason for this is that WTO intends to encourage free competition among nations. If some incentives are given for exports, there will not be free competition. It is because of this income tax

¹⁶⁶ Information provided by Björn Savlid, Exportrådet mail Tuesday February 13th 11:56.

¹⁶⁷ Ibid.

incentives are being faced out. On the other hand, some goods can be made tax free for export purposes and this is permitted under WTO stipulation. Because of the facts mentioned above, all the export promotion schemes are directed towards ensuring that inputs as well as final products are made tax free.¹⁶⁸

The Ministry of Commerce, Government of India, handles the control of the EOU and SEZ. There is a close connection with the EOU units and customs law and excise law. They have to follow the prescribed procedures and statutory exemption that these laws give. In addition, the Income Tax Act and the Foreign Exchange Management Act are very relevant for the EOU units.

The basic provisions of scheme of EOU and SEZ are identical even though there are a few minor variations.

11.5 The links between central excise and EOU and SEZ

An EOU unit can sell their production in India at the rate applicable on imports of that kind of goods. This means that excise duty is equal to customs duty leviable on imported goods. Nonetheless, a part of their production can be sold within India at a lower rate of duty. The EOU units have to follow central excise procedures in respect of their domestic sale. They have the possibility to, without payment of central excise duty; obtain inputs and capital goods from Indian manufacturers.¹⁶⁹

The Indian manufacturer's supply to EOU and SEZ are treated as deemed exports and the supplier are qualified to avail benefits available to deemed exports. The supplier has the privilege not to pay excise duty on the final products that are supplied to the EOU and SEZ.

The supplies that other manufacturers in India provide to the units in SEZ are treated as exports and eligible benefits are given to the suppliers.¹⁷⁰

11.6 Duty Drawback Scheme

The different schemes like EOU and SEZ are available to obtain inputs without payment of customs duty or excise duty or obtain refund of duty paid on inputs. Concerning central excise, the manufactures can benefit from Cenvat credit¹⁷¹ of duty paid on inputs and utilise the same payment of

¹⁶⁸ <http://www.dateyvs.com/custom06.htm> (070530) p. 1.

¹⁶⁹ Ibid, p. 14.

¹⁷⁰ Ibid, p. 16.

¹⁷¹ A manufacturer or a producer of final products or a provider of taxable service shall be allowed to take credit of different duties that are specified in the Excise Tariff Act, Additional Duties of Excise (Textile and Textiles Articles) Act 1978, the Additional Duties of Excise (Goods of Special Importance) Act 1957 and the Finance Act 2004.

duty on other goods sold in India, the other option is that they can obtain refund. Schemes relating to manufacturing under bond are also available for customs. Those manufacturers or processors that are unable to avail any of these schemes can avail duty drawback. In this case, the excise duty and customs duty paid on inputs is refunded to the exporter of the finished product by way of duty drawback.¹⁷² Materials that are used in manufacture or processing of export product are provided with drawback. The materials that are granted duty drawback are the ones that when they are imported, used in the manufacture of the goods which are then exported.¹⁷³ Other kinds of materials are granted duty drawback if the imported goods are re-exported as it is and the articles are easy to identify.¹⁷⁴ The meaning of drawback is the rebate of duty chargeable on any imported materials or excisable materials used in manufacture or processing of goods, which are manufactured in India and exported. Even the supply of stores for usage in vessel or aircraft proceeding to foreign port is covered, because it is treated as export as well.¹⁷⁵

Duty drawback is equal to customs duty paid on imported inputs including Special Additional Duty and the excise duty that are paid on indigenous inputs. In those cases that inputs are obtained without payment of customs or excise duty, no drawback will be paid. If customs or excise duty has been paid on part of input or if refund is obtained, it will only be that part on which duty is paid and on which refund is not obtained will be eligible for drawback. There are no other taxes that drawback is available. According to the Customs Act 1962, drawback is available if any manufacture, process or operation is carried out in India.¹⁷⁶ This is not the only ground where duty drawback is available, it can also be applied on processing and job work where goods may not change its identity and no manufacture has taken place.

11.7 The All Industry Rate – AIR

An exporter can opt for either All Industry Rate of Duty Drawback Scheme or brand rate of Duty Drawback Scheme, under the Duty Drawback Scheme. A large portion of Duty Drawback is paid through AIR duty. This rate is set through the consideration of the average quantity and value of each class of inputs imported or manufactured in India.¹⁷⁷ The Duty Drawback Scheme tries to compensate the exporters of different export commodity for average incidence of customs and Central Excise duties that have risen from the inputs used in their manufacture.¹⁷⁸

¹⁷² <http://www.dateyvs.com/custom07.htm> (070530) p. 1.

¹⁷³ The Customs Act 1962, section 75.

¹⁷⁴ Ibid, section 74.

¹⁷⁵ <http://www.dateyvs.com/custom07.htm> (070530) p. 1.

¹⁷⁶ Ibid, section 75 (1).

¹⁷⁷ The Customs and Central Excise Duties Drawback Rules 1995, rule 3.

¹⁷⁸ Ieport Customs Manual, [http://www.ieport.com/Customs_manual/manual_22\(a\).htm](http://www.ieport.com/Customs_manual/manual_22(a).htm) (070530) p. 1.

The AIR rate is fixed as a percentage of the Free On Board price of export products. Since there are so many export products, a duty drawback cap or ceiling has been prescribed. The meaning of this cap is that if an exporter gets high price, his duty drawback eligibility cannot go above the ceiling prescribed.

The table has the power to give allocation of the drawback allowed under primarily two names, Customs and Central Excise. The customs cover basic customs duty, surcharge and Special Additional Duty. The parts that are covered by the excise duty are basic and special duty and CVD.¹⁷⁹

The AIR is fixed based on weighted averages of consumption of imported inputs of a representative cross section of exporters and average incidence of duties. This leads to that the individual exporter is not required producing any evidence in the respect of actual duties paid by him on inputs.

There is a possibility to fix AIR for only some standard products, it cannot be fixed for special types of products. In these cases, a brand rate is fixed under rule 6.¹⁸⁰ An application has to be sent to the Commissioner at Central Excise by the manufacturer. In some cases, the manufacturer may find that the actual duty paid on inputs is higher than AIR fixed for his product. When this happens the manufacturer can apply for a fixation of Special Brand Rate, for his product. This has to be done within 30 days from export.¹⁸¹

¹⁷⁹ <http://www.dateyvs.com/custom07.htm> (070530) p. 2.

¹⁸⁰ The Re-export of imported goods (drawback of customs duty) Rules 1995.

¹⁸¹ The Customs and Central Excise Duties Drawback Rules 1995, rule 7.

12 Foreign Direct Investment – FDI

Foreign Direct Investment has a very important role in the long-term economic development of a country. It acts not only as a source of capital but also for enhancing the competitiveness of the domestic economy through transfer of technology, strengthening infrastructure, raising productivity and generating new employment opportunities.

The policy of the Government of India is to strive to maximize the developmental impact and spin-offs of FDI. The Government is also looking for large FDI inflows in the development of infrastructure, technological upgrading of Indian industry through a certain specific investments in manufacturing and in those projects that have the potential for creating employment opportunities on a large-scale basis. They also happily invite investments setting up SEZ and establishing manufacturing units therein.¹⁸² Foreign corporate and individual investment in India, termed collectively as FDI, when it relates to control or ownership of a company in India, takes one of two routes. It is either the automatic route or the Foreign Investment Promotion Board (FIPB) approval. The first one requires no prior approval required for FDI. Post-facto filling of data relating to the investment made with the RBI is for record and data purposes. The availability of this route is all sectors or activities, which do not have a sector cap i.e. where 100% foreign ownership is permitted, or for investments that are within a sector cap¹⁸³ and where the automatic route is allowed.¹⁸⁴

The FIPB have the authority to approve investment proposals where the proposed is above the prescribed sector caps or where the activity belongs to that small list of sectors where FDI is either not allowed or where it is mandatory that proposals be routed through the FIPB. For the investment and acts, the FIPB ensures a single-window approval as a screening agency. The approvals and rejections of the FIPB are normally received in 30 days. In some cases, there might be absence of stated policy or lack of policy clarity, and then some foreign investors use the FIPB applications route.¹⁸⁵ India is among the countries in the world that has the most liberal and transparent policies on FDI among the emerging economies. It is a possibility to have FDI up to 100% under the automatic route in almost every activities or sectors except a few. They are:

1. sectors prohibited for FDI
2. activities/items that require an industrial licence
3. proposals in which the foreign collaborator has an existing financial or technical collaboration in India in the same field

¹⁸² The Foreign Direct Investment Policy 2006, p. 4.

¹⁸³ E.g. less than or equal to 26% share of an Insurance company.

¹⁸⁴ Investment Commission of India, policies and laws, FDI policy overview, http://www.investmentcommission.in/policies_and_laws.htm (070530) p.1.

¹⁸⁵ Ibid, p. 1.

4. proposals for acquisitions of shares in an existing Indian company in financial service sector and where Securities and Exchange Board of India
5. all proposals falling outside notified sectoral policy under sectors in which FDI is not permitted

These exceptional activities or sectors require prior approval of the Government.¹⁸⁶

The most part of the sectors fall under the direction for FDI. Investment could be made without approval of the Central Government in these sectors. Concerning the sectors that are not in the automatic direction, investment requires prior approval of the Central Government. The FIPB is the body that approves all the approvals.

The most prominent factors that attracts the FDI are manufacturing, automobiles, engineering, telecom, electronics and chemicals. Many agreements have been signed to make it easier to facilitate investment with various countries; they are bilateral investment treaties, double taxation avoidance agreements and comprehensive economic cooperation agreements.

The above mentioned is another reason for SEMC to establish a new business in India regarding mobile phones. The goal of the FDI is to attract as many foreign companies as possible to gain the most out of them as possible. This will benefit India as well and will give them a better position as an important country in the world.

12.1 The FDI Policy in the telecom sector

Regarding the basic fact about cellular mobile, international long distance, national long distance, basic telephone service, global mobile personal communication and other value added services, the FDI is limited to 49% under the automatic route. This is subject to grant of licence from Department of Telecommunications (DoT) and devotion by the investing companies and the companies in which investment is being made, to the licence conditions for foreign equity cap and lock in period for transfer and addition of equity and other licence provision. The FDI up to 49% is also permitted in an investment company that wants to make investment in the telecom companies licensed to operate telecom services. The investments that these companies do is treated as a part of domestic equity and is therefore not set off against the foreign equity cap.¹⁸⁷

FDI up to 74% is permitted concerning licensing and security requirements regarding internet service, infrastructure providers and radio paging service. FDI up to 100% is permitted for manufacture of telecom equipment under automatic route, internet service, infrastructure providers, e-mail service, voice mail service and call centres and IT-enabled services.

¹⁸⁶ Seth Associates, policy on foreign direct investment in India, http://www.sethassociates.com/policy_on_foreign_direct_investment_in_india.php (070530) p.1-2.

¹⁸⁷ Department of Telecommunications, the FDI policy in the telecom sector, p. 1. <http://www.dotindia.com/osp/Brochure/Brochure.htm> (070329)

12.1.1 Fiscal incentives and concessions for the telecom sector

The telecom sector has amortization of licence fee, tax holiday, an enhanced limit of external commercial borrowings, a rebate on subscription to shares and scope for tax exemption on financing through venture. The telecom services sector is allowed the benefit of carry forward losses on mergers and is exempt from excise duty on cellular phones and its components, pagers, radio trunking¹⁸⁸ terminals and parts. They have a reduced central sales tax of 2% and a reduction of custom duty on populated Printed Circuit Boards for transmission from 15% to 10%. Delicensing of telecom equipment manufacturing sector and that 100% FDI is allowed in the sector under the automatic route are the last incentives concerning the telecom sector.¹⁸⁹

According to the Department of Telecommunication of India, there is a reduction of customs duty on mobile phones of 5%.

The reduction of customs duty is very good news to SEMC, that will make it easier for them to start a manufacturing of mobile phones in India.

¹⁸⁸ In a communication network, a single transmission channel between two points, which are the switching centers or nodes or both.

¹⁸⁹ Department of Telecommunications, the FDI policy in the telecom sector, p. 5-6. (070329).

13 Conclusions

After a lot of reading and searching for information regarding India and which way is the best for Sony Ericsson Mobile Communications (SEMC) to establish a market in Chennai, I have found out what I think is the best way for them.

I am going to start with an explanation of the benefits of joint ventures and branch offices, the alternatives that suit SEMC the best. After that, I am going to make a comparison to find out which alternative is the best.

The next question that needs to be answered is what kind of trade zone is the most favourable for the new company to be set up in. There are two choices, Export Oriented Units (EOU) or Special Economic Zone (SEZ).

When I have found out which final alternative is the best, I am going to make a short comparison if SEMC would make a bigger profit and save more money if, instead of starting a manufacture in India, they only imported different material from nearby countries.

Another aspect to consider is the Indian customs. There are a lot of different facts to consider when importing and exporting goods to and from India and I am going to discuss some of the premier aspects of that.

The two best ways to establish a company for SEMC in India are either as an Indian company as a joint venture or as a foreign company as a branch office.

The first alternative is a joint venture. I think that would be the most favourable way for SEMC to establish a new business in India. It attracts lower rate of tax than a foreign company does as a branch office. The liability of the parent company is also greater in case of a branch office. SEMC would receive the best advantages if they choose a joint venture set up. They would get a foreign equity of up to 100 %, depending on the requirements of the investor, subject to equity and in respect of the area of activities under the FDI policy.

Choosing the joint venture alternative would give them a very established distribution set up of the Indian partner, available financial resource of the Indian partner and established contacts of the Indian partners. These advantages would help smooth the process of setting up the business. As an incorporated Indian company, all the Indian laws will apply. It will make it easier to know what is allowed or not for the new company. The best type of joint venture would be that two parties incorporate a company in India.

Since the automatic route dealing with cellular mobile would cover the business, they have to get the approval of the Reserve Bank of India (RBI).

The second alternative is if SEMC want to stay a foreign company and set up a branch office. A requirement is that SEMC are engaged in manufacturing and trading activities abroad. Since a branch office is not allowed to carry out manufacturing activities on their own, they have the option to subtract these to an Indian manufacturer.

I think that if SEMC can find a good local partner, discuss and work out the understanding of the cultural and legal opinions of the parties, they have their key to their success of a joint venture.

When they have decided what type of company to establish, they have to decide how and where they can get most advantages concerning taxes and incentives.

Earlier in the thesis, I have described the two different ways to establish production facilities in India. If the company is export oriented, they can register as an EOU. The advantages with this kind of units are that they can pay lower excise/customs duty, or in some cases, they do not pay any at all. These units also pay a lower tax.

The other way is by register the company in a SEZ, becoming a unit in the SEZ. The advantages are almost the same as the EOUs but they also get access to the infrastructure that is available within the zone. A SEZ is very trade operations positive; it wants to promote rapid economic growth by using tax and business incentives to attract foreign investment and technology. The establishments of a unit in a SEZ are very favourable for India as well, since the benefit from a SEZ are the investment, employment, export and infrastructural developments. It is a win win-situation.

My opinion is that the joint venture of SEMC should register as a SEZ in Chennai. Chennai is a very good place for cellular mobile manufactures. It is regarded as the “Gateway to the South”; it is a strong educational technological base with both a modern harbour and an airport. This makes it a very attractive place for SEMC’s new business.

The other option and proposal that SEMC thought of was if they would make more profit if they only imported goods from adjacent countries and not had their own manufacture in Chennai. This is not a very beneficial alternative for them since they would have to pay duty on their imported goods. They would save this expense if they chose to set up a new business in a SEZ and they would get all the benefits that a SEZ offers.

If SEMC rather wants to import they have to consider the customs and its rates. The most comprehensive and important statute concerning customs is the Customs Act 1962. Duties of customs are levied on goods imported or exported from India at the rate that is specified in the Customs Tariff Act 1975. To properly and effectively handle growing international traffic and to make it administratively possible that those goods imported into or exported out of the country, different routes are checked by the Customs to ensure that they are abided with all the related laws before entry into or exit from India. This means that unrestricted freedom of access into or exit out of the country is not permitted.

Since SEMC also has an interest in import different goods from adjacent countries, it is important for them to know that importation of goods is charged with customs duties. In some cases, even the act of exportation of goods is charged with customs duties. When the goods enter the international trade they are grouped into exclusive similar categories or class of goods and calculated on a basis of well defined criteria. The nomenclature of goods, as the correct term is, is utilised by the government as the basis for prescribing appropriate duty on goods imported or exported. The nomenclature in combination with the duty rates is called the Tariff and is a part of the Tariff Act. If SEMC wants to import they have to make sure that their goods are covered under the nomenclature and that every

manufactured product will be covered under the Harmonised Commodity Description and Coding System (HS).

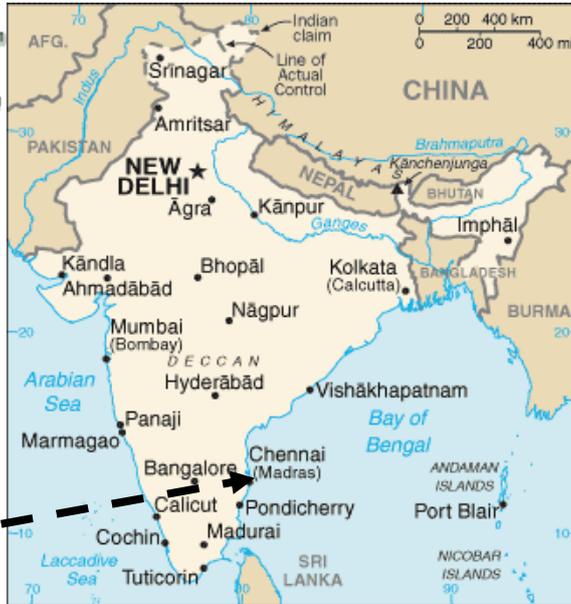
Many other cellular mobile manufacturers have an establishment in a SEZ in India and many more are following their example. It is time that SEMC does that too.¹⁹⁰

¹⁹⁰ See picture in Supplement C.

Supplement A

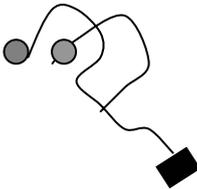


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SEMC wants to set up a phf-manufacturing business in India

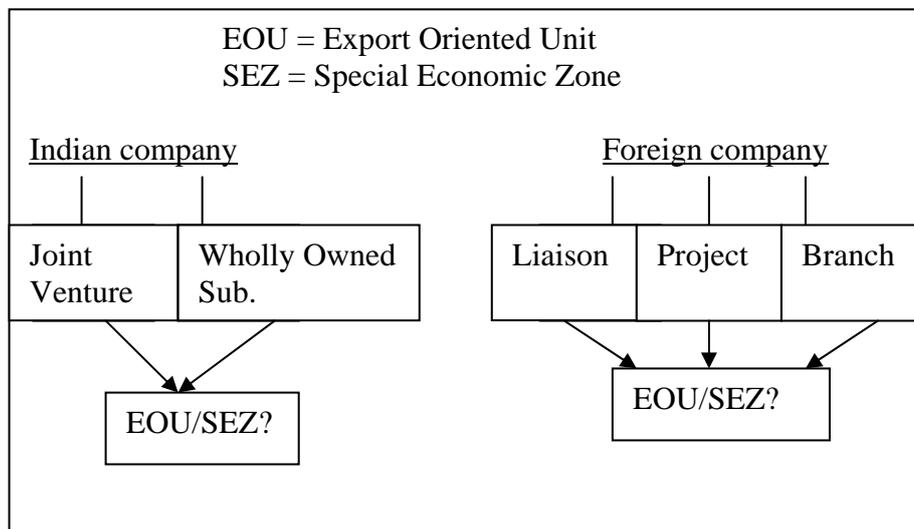


PORTABLE HANDS FREE

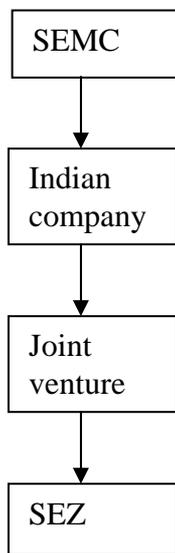
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Supplement B



Supplement C



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SEMC manufacturer of phfs in Chennai

The best way for SEMC to establish a new business in India is through an Indian company as a joint venture in a SEZ.

Supplement D

The definition of ICT goods:

ICT goods are those that are either intended to fulfil the function of information processing and communication by electronic means, including transmission and display, OR which use electronic processing to detect, measure and/or record physical phenomena, or to control a physical process. ICT goods are defined by the OECD in terms of the United Nations Harmonised System.

The guiding principle for the delineation of ICT goods is that such goods must either be intended to fulfil the function of information processing and communication by electronic means, including transmission and display, OR use electronic processing to detect, measure and/or record physical phenomena, or to control a physical process.

Another guiding principle was to use existing classification systems in order to take advantage of existing data sets and therefore ensure the immediate use of the proposed standard. In this case, the underlying system is the Harmonized System (HS). The HS is the only commodity classification system used on a sufficiently wide basis to support international data comparison. A large number of countries use it to classify export and import of goods, and many countries use it (or a classification derived from or linked to it) to categorise domestic outputs.

The application of the ICT product definition to selection of in-scope HS categories is a somewhat subjective exercise. The fact that the HS is not built on the basis of the functionality of products makes it much more difficult. The distinction between products which fulfil those functions and products that simply embody electronics but fundamentally fulfil other functions is not always obvious.

It is possible to adopt a narrow or broad interpretation of the guideline, though the OECD chose a broader interpretation, an approach which is consistent with that adopted to develop the ICT sector definition.

ICT goods are defined by the OECD in terms of the HS are presented in the Annex to the Source Publication.

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