

Globalization is leading to several U.S. companies to do business beyond the borders of the United States of America. India has become a hot destination for investments. India is the fifth largest economy in the world in purchasing power parity terms with a Gross Domestic Power (GDP) of over US\$ 1 trillion and second largest amongst emerging developing economies. India's dynamic and highly competitive private sector has long been the backbone of its economic activity. Due to the competitive advantages offered, numerous multinational and much smaller companies have established a significant presence in the Indian market through wholly-owned subsidiaries or joint ventures. The opening of capital-intensive infrastructure industries such as power, telecom, oil and natural gas, roads and highways, and ports offers vast opportunities to foreign investors.

In recent years a number of significant policy changes have been introduced to make investments in India an easier and more rewarding proposition. These policy changes by the Indian government have played an important and relevant factor in making investments in India profitable because the policies allow facilities/companies to freely repatriate any capital appreciation, allows free remittance of royalties, technical fees, dividends, interest, etc., after payment of taxes.

Even though India appears to be an attractive destination it has a strong business regulatory environment that covers all aspects of trade, industrial activity, taxes, foreign exchange, competition, intellectual property and social security.

The government of India through the Ministry of Commerce administers policy regulations and procedures through a system of governmental notifications, which requires interested persons to continually keep track of the latest amendments applicable to their business interests.

The regulatory environment in India extends, inter-alia, to the following business aspects:

- Foreign currency regulations;
- Industrial regulations and administrative controls;
- Regulations for managing business enterprises;
- Regulations concerning taxation;
- Regulations covering capital markets;
- Regulation concerning business and trade practice and anti-trust matters;
- Trade regulations - conditions regulating export and import of goods and services; and
- Intellectual Property Regulations.

The provisions, which apply to entry of Foreign Direct Investment ("FDI") in India, emanate from the Foreign Exchange Regulation Management Act (FEMA), 1999. The aim of FDI policies and regulations is to invite and facilitate foreign investments in India. The policy guidelines of the Government of India for FDI in India are reviewed on an ongoing basis. India's foreign investment regulations can be analyzed through two major headings, one related to the authorizations or licenses required by a foreign investor and the other dealing with issues such as, capitalization, profit repatriation, royalties and withholding taxes on investments made in India.

The basic principles regulating possible entry in India by foreign investors are as follows:

- No investment is permitted in a few sensitive sectors, such as Agriculture, Housing and Real Estate, Retail Trading, Lottery Business and General Trading;
- In all other sectors foreign investment is allowed on an automatic basis up to the permissible equity limit set for the sector, i.e. it does not require prior approval of the Government of India, and only required to be notified within a specified period. In this regard, the Government of India has notified "Sector Specific Guidelines for Foreign Direct Investment" ;

- Investments beyond permissible sector limit, investments by foreign companies already having collaborations in India in the “same” or “allied” areas or sectors, as well as investments in existing India companies, may required prior approval of the Government of India, Ministry of Commerce and such approval could be granted on the basis of fulfillment of several requirements. For example, one requirement imposed by the regulation is that a foreign investor should obtain a “No-Objection” of the Indian partner where it has “an existing” joint venture or technology transfer/ trade-mark agreement in the “same” or “allied” field in India ;

Capital and profits of foreign investment in approved sectors are fully repatriable after deduction of applicable withholding taxes;

- Equity participation in other than cash form, import of used capital goods, equity swaps between Indian and foreign entities fall under the purview of “specific approval” route, i.e., requiring prior Government of India, Ministry of Commerce, approval;
- Foreign technology (including technology transfer and licensing agreements and agreements for use of trademark and brand name of the foreign collaborator) are allowed in India. However, payment of Licensing Fees and Royalties for such transfer are subjected to restrictions, such as:

»Payment of lump-sum Licensing Fee not to exceed US \$2 million, and Royalties for technology transfer up to 5% of domestic sales and up to 8% on export sales, subject to a total payment ceiling of 8% of total sales over a ten year period from date of agreement, or seven years from start of commercial production, whichever is earlier. However, payment of royalty by a wholly owned subsidiary to offshore parent companies is allowed without any restrictions on the duration of the royalty payment.

»Payment of Royalty up to 2% for exports and 1% for domestic sales is allowed on use of trademark and brand name of foreign collaborator.

Higher lump sum Licensing Fees or Royalties beyond the above noted ceiling require “specific approval”, i.e., Government of India, Ministry of Commerce approval. Licensing Fees and Royalties payable pursuant to a technology transfer or use of trademark agreement are freely repatriable subject to payment of withholding taxes in India.

Due to India’s dynamic and robust regulations, it is critical for every foreign company planning to set up operations or otherwise to do business in India to comply with all relevant laws of India, including but not limited to FEMA rules and regulations that impact FDI in India. To that end, it is important for a foreign company to develop a legal strategy that supports the company’s business plans and objectives for the activities it plans to conduct in India and absolutely critical to obtain experienced guidance before venturing into the new and exciting market of India. The vast and growing Indian market is a reality. Even so, it is a challenging market that should be entered only with planning and execution that one would perform in any developing market.

US business enterprises in order to sustain, succeed and to be a part of the emerging markets globalization must be flexible and adaptable to the realities of the India market.

For More Information:

Please contact Vinita Bahri-Mehra*
(614) 255-5508
vmehra@keglerbrown.com

* Vinita is licensed to practice law in India and the State of Ohio. Prior to joining Kegler Brown, she worked with a reputed law firm in Mumbai, India.