GrantAble

GrantAble 2: Setting Up Office in India; Feb '14

PAGE 1: Options • Representative • Liaison Office
PAGE 2: Project Office • Branch Office • Affiliate or Subsidiary • Difficulties • Regularizing Existing Offices • Government Clearance
PAGE 3: Other Registrations • Bank Operations • Fund-raising • Base for South Asia • Control • Hybrid Structures • P E
PAGE 4: Shutting Down

As Indian economy and society has changed, a number of international NGOs (Non-Governmental Organizations) and aid agencies have started setting up base in India. However, Indian laws are not designed to make this easy. There are a number of bureaucratic twists and turns, which often don't make sense to outsiders.

This issue of Accountable tries to demystify the process. It offers an overview of the options. It also discusses some of the difficulties that you might face.

Options

There are at least five ways to establish a presence in India. These are graded for increasing degree of engagement:
1. Post a Representative
2. Open a Liaison Office
3. Open a Project Office
4. Open a Branch Office
5. Promote an Affiliate or a Subsidiary

However, legal and operational implications of each vary. Let us look at these in more detail.

1. Representative

No permission is needed to post an individual as a representative in India.[1] The individual should not set up an office, but work on their own. You can also ask an organization in India to represent you, through a grant or a fee-based arrangement. However, avoid fee-based agreements with Indian NPOs (Not-for-Profit Organizations) as these may create tax complications for them. Service tax will not be attracted, if the client is based outside India.

What happens if the representative is an expatriate? They will need an employment visa. This is quite difficult unless they are employed by an Indian organization or a registered liaison, branch office, etc. The name of the employer is usually endorsed on the visa. Therefore, this option works only if the representative is an Indian national or a PIO (Person of Indian Origin).

Representatives should not take up program activities in India on behalf of their principal. This can lead to violation of FCRA (Foreign Contribution Regulation Act). How? FCRA is now applicable to individuals as well as for-profit organizations with specified program activities. In some cases, this can also result in a Permanent Establishment for the principal, attracting a tax liability.

2. Liaison Office

This allows you to open a physical office in India, and post a limited number of staff. The office can take up only limited activities (see table). You can not raise funds or take up any direct program activities. A number of donor agencies use this option to set up a program coordination office.

FCRA permission is not needed for a liaison office. However, you need Reserve Bank of India's (RBI) permission for each office you set up in India. Permission is granted only for three years at a time. Permission for NPOs has become increasingly difficult over

[1] Under FERA 1973, permission was needed for this also (sec. 28). This requirement has been dropped under FEMA 1999.

the years.

3. Project Office

This option works if you are implementing a project in India and need only a temporary presence.

There is a general permission for foreign companies to set up project offices, if they have an execution contract with an Indian company. The project should also be funded by remittances from abroad or by a bilateral / multilateral financing agency. Alternatively, the project should have been cleared by an authority or a bank, etc.

However, this general permission doesn't work for NPOs or foreign government bodies. They must apply to the RBI for prior permission. FCRA permission may also be needed if the activities are financed with foreign contribution.

4. Branch Office

A branch office is allowed to take up some more activities (see table). You need permission from RBI as well as FCRA for setting up a branch office. However, FCRA Department has now become uncomfortable with this idea, and permission is routinely declined.

Activity	Liaison Office	Branch Office
Acting as a communication channel between the parent entity and Indian organizations	●	
Representing the parent entity in India	●	●
Acting as buying / selling agent (of Parent entity) in India		●
Promoting export / import with India	●	
Export / import of goods (on wholesale basis)		●
Promoting technical or financial collaborations between Indian organizations and parent or overseas group entity	●	●
Rendering professional or consultancy services	●	●
Carrying out research work, in areas in which the parent entity is engaged	●	●
Rendering services in information technology and development of software in India	●	●
Rendering technical support for products supplied by parent/group entities	●	●

5. Affiliate or Subsidiary

You can also float a separate legal entity in India. This can be a trust, society or a non-profit company. It can be set up as an independent organization that subscribes to your vision. Or it can be set up as a subsidiary or controlled entity.

You do not need RBI permission for this. FCRA permission is needed if you want to get foreign contribution (or share capital) into the organization.

If the Indian entity is set up as a for-profit, then FCRA permission may not be needed. However, contribution of share capital must be in line with Foreign Direct Investment (FDI) norms.

Difficulties

All this is not as simple as it sounds. There are a number of complexities and difficulties. Some are discussed below.

Regularizing Existing Offices

A number of liaison and other such offices were set up over the years without RBI permission. In 2011, RBI invited all such organizations to apply for regularizing of their presence. This ended in Oct'11. However, if you missed the boat in 2011, you can still apply for regularization.

Government Clearance

Your application for setting up a liaison, project or branch office is made to the RBI through an authorized dealer. For business organizations, this is usually sufficient – if 100% FDI is permitted in the sector under automatic route.

This automatic route is not available for NPOs and development agencies. RBI clears such applications only after consulting Ministry of Finance and other concerned ministries. This can lead to long delays.

Other Registrations

RBI now allots a Unique Identity Number (UIN) for each liaison, branch or other such offices. A tax Permanent Account Number (PAN) is also mandatory for such offices. If you have to deduct tax at source, then a TAN is required. In some states, a Shops and Establishments registration may be obligatory. Registration for Provident Fund is also required in some cases.

Additionally, if you are a company in your home country, then you have to register the India office with Registrar of Companies in India.

Bank Operations

A representative can not open a bank account in the organization's name. All others (liaison office, project office, branch office) can. Affiliates or subsidiaries open bank accounts in their own name.

Fund-raising

A representative or a liaison office can not raise funds in India. A branch office can, if the RBI permission provides for this. Offering tax rebates to donors through a branch office is possible in theory but very difficult in practice. Therefore, fund-raising is feasible only through a separate entity.

Base for South Asia

If you set up a liaison office, then your liaison activities must be primarily focused on India. The India office should not be used for supporting activities in other countries.

Control

A branch or liaison office remains under direct control of the parent entity. However, if you are setting up an affiliate or a subsidiary, you need to discuss this with your advisers. They will help you ensure that you are able to maintain required degree of control, without FCRA or tax complications.

Hybrid Structures

Sometimes an international NGO may set up a for-profit entity in India for providing support services, or taking up fee-based activities. Three factors should be kept in mind while planning this:

1. FCRA may still be attracted, if the Indian entity takes up any program activities with foreign contribution.
2. Service tax is applicable to a large variety of services, including program management support.[2]
3. You could unwittingly set up a Permanent Establishment of the parent entity. This can lead to income tax complications for the parent entity.

Most development professionals are blissfully ignorant of laws related to for-profits. It is therefore useful to prepare a road-map for your proposed operations and have it evaluated by a person familiar with these laws.

Raising the Drawbridge

Many cultures in Asia have had a fear of foreigners, and have tried to insulate themselves, often with disastrous consequences. In the 19th century, Japan did not want Western missionaries or traders on its shores, though the Dutch had been given a license to trade. This incensed the Americans, who made several attempts to breach the castle. Finally, Commander Perry, at the head of a flotilla, imposed a naval blockade in 1842. He gave the Japanese three days to open their economy to the US, or else! The Japanese blinked and gave in.

However, Japan then embarked on a national mission to regain its self-esteem. People were trained in combat, and infused with a martial spirit. Exactly one hundred years after Commander Perry's blockade, Japan attacked the Pearl Harbor in 1942. The US responded in 1945, with Hiroshima and Nagasaki.

This long-running feud between two great pacific nations appears to have ended with Japan embracing modern economic ideas, and demilitarizing the nation. Its defense is presently guaranteed by the US military.

Permanent Establishment

The concept of Permanent Establishment (PE) is often used to tax some activities of a non-resident. PEs come in different shapes and sizes. An affiliate or subsidiary also runs the risk of being treated as PE of the parent, if it is used to undertake the parent's activities in India. If the subsidiary performs the functions of a liaison office for the parent, this also can result in a PE for the parent.

INGOs should be careful that their liaison office does not result in PE status for tax purposes. If this happens, then grants raised abroad for their work in India can, theoretically, be brought to tax.[3]

[2] Services to clients based abroad are usually exempt from service tax. See AccountAble 150 for more on this.

[3] Legally, grants are generally treated as business income, unless the charity has a valid tax exemption. In practice, however, foreign charities are unlikely to be taxed on account of a PE in India. Still, in a high profile case, the government can throw the book at the INGO! Also, if the grant or program investment involves carrying on sustainable activities or providing fee-based services, then the PE angle must be carefully examined.

What about a virtual office or a web-site? In a recent case, eBay International was able to argue successfully that its web-site for Indian buyers and sellers did not result in a PE in India. However, in a couple of landmark cases, computers provided by a foreign entity to Indian travel agents resulted in a PE.[4]

What happens if an INGO takes up work in India without setting up an office here? The INGO will not be covered by FCRA. However, people coordinating its activities in India could still be covered as individuals with a program. What if these people finalize or sign contracts (or deliver services) on behalf of the INGO? This could result in a taxable PE.

Shutting Down

What happens if you decide to close down your branch or liaison office? Mostly, you can remit back any surplus funds. This is subject to an audit certificate, a tax clearance and some other documentation. You then need to apply to your bank for permission. The bank checks the documents, and then allows repatriation. The bank will then report the closure to RBI.

Beginning Feb-14, you can also transfer your remaining assets to another entity in India. This also is subject to the process outlined above.

[4] Amadeus Global (2007), Galileo International (2007)

What is GrantAble: Each issue of 'GrantAble' covers a different topic related to grant-making and monitoring and is posted/emailed to about 800 persons in Development Agencies, CSR Departments of large companies, and Corporate Foundations. AccountAid encourages re-production or re-distribution of 'GrantAble' in internal workshops or newsletters for non-commercial use, provided the source is acknowledged.

GrantAble by Email: If you are a grant-maker or involved in managing CSR for a corporate foundation, you may be interested in getting GrantAble in your inbox. Please visit www.AccountAid.net to register for this and other publications.

Disclaimer: Interpretation of law given here is of a general nature. To get a deeper idea of how concepts discussed here would apply to your situation, please ask for scheduling a call or meeting with one of our experienced advisers. Law discussed here is up to date as of 1-Jan-15.

Questions and Comments: AccountAid India, 55-B, Pocket C, Siddharth Extension, New Delhi-110 014; Phone: 011-2634 3128; Phone/Fax: 011-2634 3852; e-mail: query@accountaid.net

Printed and published by Ms. Renu Agarwal for AccountAid India, New Delhi (Ph. 26343128) at PRINTWORKS, W-11, Okhla Industrial Area, Phase 1, New Delhi 110 020

Knowledge Partners: M/s Sanjay Aditya & Associates

Content: Shri Sanjay Agarwal; Editing: Ms. Soumyasree Mullick; Design: Ms. Moushumi De

Images: © traffic sign - ryasick; Dollar Rupee jigsaw - alexsl; Cardboard Box on Hand Truck - Tashatuvango at iStockphoto.com

For private circulation only.