

Setting up presence in the country- Liaison office (LO)

Setting up

1. Who can set up a LO in India?

Any foreign entity (a body corporate incorporated outside India, including a firm or other association of individuals) can set up a LO in India in accordance with the Reserve Bank of India ('RBI') guidelines.

2. Is approval under FEMA required to set up a LO?

An LO can be set up in India as per the regulatory framework established by RBI in this regard. Accordingly, a foreign entity may approach Authorised Dealer Bank ('AD Bank') with a request subject to meeting certain conditions:

- a profit-making track record during the immediately preceding three financial years in the home country; and
- net worth of more than USD 50,000 or its equivalent.

Where such condition is not fulfilled then the applicant entity will have to furnish a Letter of Comfort (LOC) from its parent/ group company, which satisfies the prescribed criteria for net worth and profit.

Generally, setting up a LO requires approval from AD Bank. Please note that AD Bank is any commercial bank permitted by RBI to deal in foreign exchange. However, in certain cases prior approval from RBI, in consultation of GOI would be required in the following cases:

- a. A citizen of or entity registered/incorporated in Pakistan.
- b. A citizen of or entity registered/incorporated in Bangladesh, Sri Lanka, Afghanistan, Iran, China, Hong Kong or Macau and the application is for opening a LO in Jammu and Kashmir, Northeast region and Andaman and Nicobar Islands.
- c. The principal business of the applicant is falls in Defense, Telecom, Private Security and Information and Broadcasting and Government approval or license/permission by the concerned Ministry/Regulator has not been granted.
- d. A Non-Government Organisation (NGO), Non-Profit Organisation, Body/ Agency/ Department of a foreign government. However, if such entity is engaged in any of the activities covered under Foreign Contribution (Regulation) Act, 2010, they shall obtain a registration under that Act and shall not seek permission under FEMA.

3. Is the approval under FEMA given by RBI? If yes, which application form is required to be submitted?

The application for establishing LO in India is required to be submitted in Form FNC to an AD Bank along with the prescribed documents and the Letter of Comfort, wherever applicable.

4. What documents are required to be submitted with RBI along with the application?

The following are indicative documents are required to be submitted along with the application:

- a. Copy of the Certificate of Incorporation / Registration; Memorandum of Association and Articles of Association attested by the Notary Public in the country of registration.

[If the original certificate is in a language other than in English, then English translation duly notarized and attested by the Indian Embassy/ Consulate should also be furnished].

- b. Audited Balance Sheet of the applicant for the last five years
- c. Bankers' Report from the applicant's banker in the host country / country of registration stating the length of banking relations with that bank.
- d. Board Resolution passed by the foreign entity approving setting up of an LO in India.
- e. Power of Attorney in favour of authorised signatory in India.

Based on the facts of the case, the AD Bank may request the applicant for additional information.

5. Who is authorized to file such application with RBI?

Any individual authorized by the applicant can sign the application for setting up a LO under appropriate Power of Attorney.

6. Are there any timelines for filing the application with RBI?

As such, no specific timeline is prescribed for the application with the RBI. However, LO can commence its operations only after receiving appropriate communication from the AD Bank in this regard.

7. Can this application be filed and approval be granted online or physical presence in India is required for any meetings?

A duly completed application with all supporting documents must be filed physically with the AD Bank. Generally, all clarifications are requested through post / email. Physical presence is not required as such unless insisted by the AD Bank/ RBI.

8. What happens when an applicant for setting up a LO in India does not fulfil the eligibility criteria laid down by RBI?

In the event prescribed conditions are not fulfilled, the application for setting up LO is likely to get rejected.

9. Can a parent company apply for setting up of a LO on behalf of its subsidiaries?

No, a parent company cannot apply for setting up of a LO on behalf of its subsidiary(ies). However, where the applicant is unable to meet the conditions relating to financial eligibility then the parent entity may offer a Letter of Comfort provided it satisfies the prescribed criteria for net worth and profit track record.

10. Whether there is any time-limit for granting of approval by RBI for setting up of LO in India?

No time-limit has specified for granting approval by AD Bank / RBI for setting up LO in India. Based on past experience, such applications are disposed off within 4 to 6 weeks from the time duly completion application is filed.

11. For how many years is the approval valid?

Generally, permission to establish an LO is given for a period of three years from the date of set up. However, in the case of entities in Non-Banking Finance Companies (NBFCs) and construction and development sectors, validity is for two years.

12. What activities can be carried out by an LO in India?

Permissible activities for an LO include:

- a) Representing the parent company / group companies in India.
- b) Promoting export / import from / to India.
- c) Promoting technical/ financial collaborations between parent / group companies and companies in India.
- d) Acting as a communication channel between the parent company and Indian companies.

13. Whether an application is required to be filed with ROC?

14. Which form is required for filing of such application with ROC?

15. Whether PAN is required to be obtained by an LO? Is any other tax registration required?

Yes, LOs is required to obtain income tax registration number Permanent Account Number (PAN) and withholding tax registration number known Tax Deduction Account Number (TAN). Additionally, depending upon the location of the office address as well as the employees, the LO may be required to obtain registration under the profession tax law.

16. Whether Foreign Banks and Foreign Insurance Companies can set up a LO in India?

Yes, foreign banks can set up a LO in India post examination by the Department of Banking Regulation (DBR), Reserve Bank of India, Central Office. Whereas foreign insurance companies can set up a LO in India post examination by the Insurance Regulatory and Development Authority (IRDA).

17. Whether foreign law firms can establish an LO in India?

No, foreign law firms cannot establish an LO in India

Operating in India

18. Whether an LO is required to open a bank account in India?

An LO is required to open a bank account with an AD Bank to receive remittances from its Head Office and incur operating expenses.

19. Can more than one bank account be opened by an LO?

It may be possible for an LO to open and maintain more than one bank account with the prior permission of RBI.

20. What are the permitted debits and credits in the bank account of an LO?

Permitted debits: Only for meeting the local expenses.

Permitted credits:

- a) Inward remittances from Head Office for meeting the expenses of the office
- b) Refund of security deposits paid from LO's account or directly by the Head Office through normal banking channels
- c) Refund of taxes, duties etc., received from tax authorities, paid from LO's bank account
- d) Sale proceeds of assets of the LO

21. Do LOs require registration with State Police Authorities?

Applicants from Bangladesh, Sri Lanka, Afghanistan, Iran, China, Hong Kong, Macau or Pakistan desirous of opening LO in India shall have to register with the state police authorities.

22. What activities cannot be carried out by a LO in India?

An LO is not allowed to undertake any revenue generating activity in India. Further, an LO cannot practice any legal profession in India.

23. Can the initial approval granted by RBI be extended? if yes, then who grants this extension?

Yes, extension for operating an LO in India can be sought. For this purpose, an appropriate request may be made before the expiry of the validity of the existing approval to the concerned AD Bank. Upon verification the AD Bank may extend the validity for another term of three years from the date of expiry.

24. Whether change/alteration in the document delivered to the ROC for registration is required to be intimated? If yes, which form is applicable and what is the time limit for filing of such change/alteration?

25. Are there any conditions which must be fulfilled before filing an application for extension of LO in India?

Yes, the applicant must ensure that following conditions are fulfilled before filing an application for extension of LO:

- a) The LO should have submitted the Annual Activity Certificates for all the years; and
- b) The bank account of the LO is being operated in accordance with the terms and conditions stipulated in the approval letter.

26. What is the time limit to grant approval for extension of LOs?

Approval for grant of extension of LOs shall be provided within one month from the receipt of the request.

27. Whether an application for undertaking of additional activities or setting-up additional LOs can be filed with RBI?

Request for establishing additional LO may be submitted to the AD Bank. Requests for undertaking additional activities may be submitted to the RBI through the AD bank backed by an appropriate rationale.

28. What is the maximum number of LOs can be established by any foreign entity in India?

There is no restriction on maximum number of LO that foreign entity can set up in India.

29. How are the operations of an LO funded?

Operations of an LO can be funded only by way of remittances from Head Office.

30. Whether an LO can remit funds to its head office?

LO can only remit the excess funds on closure.

31. Whether an LO can purchase immovable property in India?

No, LO cannot purchase any immovable property in India. However, LO has general permission to operate out of leased premises subject to lease period not exceeding five years.

32. What are the requirements for maintaining books of account by an LO?

33. Whether audit of annual accounts of an LO required?

34. Whether audited financial statements are required to be filed with ROC? If yes, which form is applicable?

35. What is the time limit for filing of audited financial statements with ROC? What are the consequences on non-compliance?

36. Are there any reporting requirements on setting up of an LO in India?

LO shall furnish Form 49C with the Indian Tax Authorities along with prescribed documents within 60 days of the end of the financial year.

37. What is an AAC and with which authority is it required to be filed?

Annual Activity Certificate (AAC) is an annual certificate in respect of the activities undertaken by LO during the year are in accordance with the RBI approval letter. It is required to be obtained in the prescribed format from the auditor.

The LO needs to submit AAC each year to the AD Bank as well as Director General of Income Tax (International Taxation), New Delhi.

38. What is the time limit for filing of an AAC? If not filed timely, what are the consequences?

The AAC should be filed within six months of the close of the financial year. In case of non-filing, penal action may be taken against the LO as per relevant FEMA provisions.

39. Is the LO required to file its tax return in India? What are the consequences of non-compliance?

Since LO is not allowed to carry out any business activity in India, it may not earn any income in India. Thus, in absence of any income being generated, it is not liable to file tax return in India.

However, it may be required to file tax withholding return if tax withholding provisions are applicable on local expenses incurred by the LO.

40. What are the tax implications in case LO carries out activities which are not preparatory or auxiliary in nature in terms of the DTAA?

Where the activities carried out by LOs are not in the nature of preparatory or auxiliary, subject to the Indian Tax Regulations read with applicable Double Tax Avoidance Agreement, the LO may constitute a business connection in India. Once it is established that the LO has business presence in India, it would be under an obligation to pay taxes and file tax return in India.

[Section 9(1) of the Income-tax Act, 1961]

41. What are the tax implications in case LO creates a PE? What are the compliances required? What are consequences of non-compliance?

In case LO creates a PE in India, it would be under an obligation to

- Pay taxes at 40% (plus surcharge & cess) in India as if it is carrying out business in India.
- It will also be required to file tax return

[Section 139 of the Income-tax Act, 1961]

42. Whether tax withholding is applicable on remittance made to HO?

Yes, any payment which is chargeable to tax in India (i.e. if it meets the test of income earned from India), LO would be under an obligation to withhold tax and meet other compliances such as filing withholding return, obtaining form 15CA & 15CA.

43. Does the LO need GST registration? What are the compliance requirements and consequence of non-compliance?

Since LOs are not authorized to carry out any business activities in India, they are not required to obtain any registration under GST laws.

However, taxation of LO is a grey area till date, as there are various judicial precedents (including Advance Rulings), which has held otherwise.

Therefore, each of the case has to be evaluated separately, basis the facts of the case and relevant statutory provisions.

44. Whether LOs are required to pay any tax on the amounts received from overseas entity?

Since LO cannot receive or provide any service, hence the reimbursement of expenses received by it, would not be treated a consideration, hence GST would not be applicable

However, as reiterated in the earlier paragraph, taxation of LO is a grey area as of now, due to divergent rulings. In certain rulings, the Authorities have held that LOs are distinct person, and therefore, liable for registration and discharge applicable GST liabilities

Therefore, considering the above, each of the case has to be evaluated separately, basis the facts of the case and relevant statutory provisions.

45. Are TP provisions applicable in case of transactions between HO and LO? What are the compliance requirements and consequence of non-compliance?

A liaison office is not allowed to earn profit in India as per the definition of Liaison office under FEMA. Since LO is not earning any taxable income in India, LO is not subject to tax in India. Hence, charging provisions do not apply and accordingly, transfer pricing compliances are not required.

Further, during any tax assessment, if it is established that LO conducted business in India in form of any activities which is taxable, Transfer Pricing provisions will be applicable, and compliances will be required to be undertaken by such LO.

[Clause 2(e) of FEMA 22R and Section 92 of the Income-tax Act, 1961]

Closure of LO

46. Whether any regulatory approval or FEMA required for closure of an LO in India? If yes, what are the documentation requirements and how long does it take to get such approval?

Yes, requests for closure of the LO may be submitted to the AD Bank along with the following indicative list documents:

- a) Copy of the RBI's/AD bank's approval for establishing the LO.
- b) Auditor's certificate:
 - i. indicating the manner in which the remittable amount has been arrived at and supported by a statement of assets and liabilities of the applicant and indicating the manner of disposal of assets;
 - ii. confirming that all liabilities in India including arrears of gratuity and other benefits to employees, etc. of the office have been either fully met or adequately provided for; and

- iii. confirming that no income accruing from sources outside India (including proceeds of exports) has remained unrepatriated to India.
- c) Confirmation from the applicant/parent company that there are no legal proceedings pending against the LO in any Court in India and there is no legal impediment to the remittance.
- d) A report from the ROC regarding compliance with the provisions of the Companies Act, 2013, in case of winding up of the LO in India, wherever applicable.

The AD bank must ensure that the LO had filed their respective AACs.

There is no time limit prescribed under the RBI guidelines to get the approval for closure of LO. Generally, basis past experience, 4 to 6 weeks from filing of complete set of documents.

The AD Bank will carry out its diligence and seek clarifications, if necessary, post which it may grant a certificate of closure and enable closure of bank account.

47. Whether any approval required from Income tax authorities for closure of LO in India? If yes, what are the documentation requirements and how long does it take to get such approval?

While specific approval is required to be obtained from the revenue authorities, making an application to the authorities informing the same is recommended. Also, a letter intimating surrender of PAN and TAN can be filed.

48. Whether any approval required from GST authorities for closure of LO in India? If yes, what are the documentation requirements and how long does it take to get such approval?

Broadly, LOs are not required to obtain registration under GST laws, the question of seeking approvals on closure does not arise

However, incase it is evaluated that LOs are required to take registration and discharge applicable GST liabilities, then all the formalities which are applicable to a normal registered taxpayer, will squarely apply to LO as well (including filing of Final Returns)

49. Whether transfer of assets on closure of LO permitted?

Proposals for transfer of assets may be considered by the AD Category-I bank only from LOs who are adhering to the operational guidelines subject to conditions prescribed under FEMA.

50. How can the surplus on closure be remitted?

Subject to the approval under FEMA regulation, the surplus money can be remitted to the HO upon obtaining a certificate in form 15CB from an independent accountant along with 15CA generated by the LO through the tax portal.

51. Are there any tax implications on remittance of surplus on closure?

So far, the remittance is of the surplus amount (earlier received from LO for meeting expenses) remaining unspent, there may not be any tax implication.

Reference

- Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016 (Amended up to January 21, 2019)
- Master Direction on Establishment of Branch Office (BO)/ Liaison Office (LO)/ Project Office (PO) or any other place of business in India by foreign entities (updated as on 18 May 2021)