



PERMANENT ESTABLISHMENT IN INDIA: BRANCH OR SUBSIDIARY?

DEFINITION OF A PERMANENT ESTABLISHMENT

The Indian Income Tax Act defines permanent establishment as follows: A **permanent establishment** includes a fixed place of business through which the business of the enterprise is wholly or partly carried on and does not include a liaison office.

DEFINITION AND MAIN DIFFERENCES BETWEEN A BRANCH AND A SUBSIDIARY

Definition of Subsidiary

An incorporated entity formed and registered under the Companies Act, 2013. It is a distinct legal entity, apart from its shareholders.

Distinguishing features of a Subsidiary:

1. Company form of organization as separate legal entity.
2. The liability of the Parent company is limited to the extent of its shareholding in the Wholly Owned Subsidiary (WOS). The assets of the foreign company are not subject to any attachments.
3. Minimum two directors are required, one of them being Indian.
4. Quarterly Board Meeting & Annual Meeting of shareholders is compulsory in every year.
5. Subsidiary is not treated as private equity of the foreign company; its income is taxed based on residential status.
6. Transfer of shares is restricted, and deposits may not be accepted from the public.
7. Only activities covered and approved in the Memorandum of Association are permitted.

Definition of Branch Office

Companies incorporated outside India and engaged in manufacturing or trading activities are allowed to set up Branch Offices with specific approval of the Indian Central Regulatory Bank (RBI).

Distinguishing features of a Branch:

1. It is an extension of Head Office with the right to accrue income in India and has no separate legal standing of its own.
2. It can export/import goods, render professional/consultancy and information technology services, carry out research work in line with parent activities, promote technical & financial collaboration, represent the parent company in India, act as buying/selling agent, and render technical support for the products of the parent company.
3. The liability of the Branch is unlimited. The assets of the parent company are at risk of attachment in case the liabilities of the branch exceeds its assets.
4. Branch offices are managed by an Authorized Representative, resident in India (Country Manager).
5. From a taxation perspective, a branch of a foreign company is deemed to be a 'business connection' of its parent, and thereby constitutes a taxable permanent establishment of the foreign enterprise.
6. The entire expenses in India will be met either out of the funds received from head office through normal banking channels or through income generated by it in India.
7. It can not expand its activities or undertake any new trading, commercial, or industrial activity other than that is expressly approved by the RBI.



TAX AND ACCOUNTING OBLIGATIONS

1. A Subsidiary Company incorporated in India is subject to minimum base rate of tax @ 30.9%, whereas a Branch office is liable to pay minimum base rate of tax @ 41.2%
2. Dividends can be paid after payment of Dividend Distribution Tax @ 16.995% by a subsidiary, whereas dividend distribution is free for a branch office.
3. Tax Obligations applicable are: Income Tax, withholding taxes, Service Tax, Professional Tax, custom duty etc. for branches as well as subsidiaries.
4. Provisions of Transfer pricing are applicable for branches as well as subsidiaries.
5. Annual Accounts of Branches as well as subsidiaries are required to be audited by a Chartered Accountant of India.

REGISTRATION FORMALITIES

Branch Office

- (i) Parent company must have a profit making track record during the immediately preceding five years and net worth of not less than USD \$100,000 or its equivalent.
- (ii) Required to Obtain PAN/TAN, Service tax code, Shops and Establishment Act Registration, Importer Export Code, VAT, Registrar of Companies (ROC) Registration.
- (v) Normally registration is allowed for a period of three years.

Subsidiary

- (i) A private company is required to be incorporated with a minimum authorized & paid up capital as may be prescribed and minimum two subscribers. No requirement of track record of parent company as shareholder.
- (ii) Required to Obtain PAN/TAN, Service tax code, Shops and Establishment Act Registration, Importer Export Code, VAT.
- (iii) Once registration is granted it can do business, until the company decides to close down its operations.

STANDARD LEGAL OBLIGATIONS AND FORMALITIES FOR A BRANCH

BRANCH OFFICE

A. Filings:

1. Yearly filings include the filing of audited accounts of Branch Office, World Accounts with Registrar of Companies
2. Yearly submission of Activity Certificate with RBI and AD Bank
3. Annual return with the Income Tax Department
4. Filing of Quarterly/ Monthly TDS returns, VAT, Service Tax Returns

B. Other Legal Obligations/Provisions:

1. The Branch Office will not accept any deposits in India
2. The commission earned by the Branch Office from parties abroad for any agency business will be repatriated to India through normal banking channels.
3. The Branch office shall not undertake any retail trading activity
4. A Branch Office is not allowed to carry out manufacturing or processing activities in India, directly or indirectly.
5. The Branch Office is not allowed to borrow locally unless the prior approval of RBI is given.