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Vern Krishna: The pluses and minuses of business in India



VERN KRISHNA | May 25, 2011 10:40 AM ET
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Purushottam Sakhare types an affidavit outside a city court in Mumbai. India's common law legal system may be familiar to Canadians, Vern Krishna notes that the pace of dispute resolution is purely Indian. Photo: INDRANIL MUKHERJEE/AFP/Getty Images

The election of Stephen Harper with a majority Conservative government virtually assures a free trade agreement between Canada and India – a project supported by the prime ministers of both countries.

Canadian multinational corporations will welcome the agreement as opening new opportunities for business.

Recent studies forecast India's labour force to increase by 110 million in the next 10 years, compared with only 11 million for the United States. The incremental gross domestic product growth rate attributable to the increased demographics alone is estimated at 4% per year, which compares with a total annual GDP increase of about 3% in Canada and the United States.

There are many pluses to doing business in India. Unlike some other emerging markets, India has a legal structure that fits well with Canada. India is the world's largest democracy with 64 years of stable government. The country also inherited the English legal model and judicial system. In addition to a middle class of 350 million, India is English-speaking with a well-educated professional and technical class.

New opportunities, however, also bring new challenges. Multinationals will need to adapt as they expand into the subcontinent. The legal system may be English in origin, but the speed and manner in which it functions is entirely Indian. Commercial disputes, particularly those involving the government, can easily take 30 years to resolve. Disputes involving land can take two generations! It is difficult to go through the dispute resolution process without some meditative serenity. Attention to details by Canadian and Indian legal counsel is imperative to avoid falling into the molasses of the Indian court system.

Canadian companies will also have to adapt to a political culture that relies on bribes to government officials and politicians. Bribery of public officials – from the lowest bureaucratic level to Ministerial heights – is a must if a company is to secure appropriate approvals and licences in a timely manner.

To be sure, unlike Russia and China, India's free press shows off its dirty laundry. Nevertheless, recent revelations of scams over mobile phone licences and the Commonwealth Games illustrate only a fraction of the graft in the country. As foreign countries enact and enforce stricter anti-corruption laws, multinational companies are becoming increasingly concerned about corruption.

Graft is a form of tax that adds to overhead costs that reduce overall return on equity. Some simply consider it as a cost of doing business and build it into their cost structure. Multinationals, however, must consider their own domestic and international rules prohibiting bribery of foreign officials. Under Canada's Corruption of Foreign Public Officials Act, for example, bribery of foreign public officials is a criminal offence with serious tax implications. Fortunately for Canadian companies, we do not enforce the statute because of esoteric legal concerns about its extra territorial jurisdiction.

Our southern neighbour enforces its Foreign Corrupt Practices Act with pit-bull enthusiasm. Under American law, it is an offence for any company that trades on a U.S. exchange to bribe foreign government officials to gain a business advantage in any country. The Americans prosecute zealously.

For example, the Securities & Exchange Commission settled charges against Alcatel-Lucent that it bribed Latin American and Asian officials for telecom contracts. The firm agreed to pay US\$137-million: US\$45-million in disgorged profit, plus a US\$92-million criminal fine.

The newest challenge in India is its decision to enact a general anti-avoidance rule (GAAR) that gives the tax department substantial discretion to assess taxes and reclassify any transactions that they consider to be contrary to the spirit of the tax code. Though modeled on the Canadian GAAR, the Indian version is administered in a different environment of graft culture. The effective administration of any GAAR requires an efficient tax department that is untarnished and supervised by a judicial process that is speedy and committed to the rule of law. Multinational businesses will face interesting challenges dealing with the [Indian Revenue Service](#), which does not enjoy a reputation for being as untarnished as it should be.

The Indian Revenue Service is also zealous in the extreme. For example, it recently assessed a British company, Vodafone Group PLC, US\$2.6-billion taxes on capital gains that the company triggered on a share sale of a non-resident company between two non-residents on some tenuous theory that there were corporate assets in India. Multinationals going into India should be prepared for a bumpy ride and have appropriate legal counsel.

To achieve the level of economic growth that India desires, it will need to attract foreign capital investment and promote an inviting business climate. Multinationals will need to observe their own domestic rules while also trying to navigate through foreign cultural business practices and legal systems.