Q4-2016 & Q1-2017

Newsletter

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GM Corporate Solutions

Financial & Strategic Advisors

Foreword

Global M&A Snapshot

The year 2016 witnessed global M&A deal value decline by 16% to USD 3.6 trillion, yet it still managed to become the second highest for deal-making since 2007. The fourth quarter alone contributed USD 1.2 trillion while also posting a 50% increment compared to third quarter. While 2015 was dominated by a large number of megadeals, a more consistent stream of transactions were noted this year. On the other hand, withdrawn M&A climbed to an eight-year high at USD 804.7 billion.

Some of the largest deals in fourth quarter include AT&T's buying Time Warner for USD 85 billion, British American Tobacco's USD 47 billion bid for balance stake of Reynolds American, Qualcomm's USD 39 billion acquisition of NXP Semiconductors and merger of industrial-gas giants Praxair Inc and Linde AG valued at USD 67 billion.

The year 2017 however has had a tepid start with global M&A reaching just shy of USD 1 trillion in first quarter. Some of the largest deals are Cilag Holding's USD 30 billion offer for Actelion, Vodafone India and Idea Cellular's USD 23 billion merger and Reckitt Benciser's USD 18 billion acquisition of Mead Johnson Nutrition Company.

India M&A and private investments snapshot

In India, 1002 M&A deals were struck in 2016 with total deal value of USD 61.4 billion – posting an increment of 2.6 times compared to last year and also the highest in last 5 years. While big ticket deals accounted for only 6% of total deals, they contributed a massive 92% to total M&A value.

Further, private investments in India saw a 25% decline in volume and 44% decline in value terms to close at 1309 deals valued at USD 12.4 billion. Early stage funding also witnessed a significant setback with investors turning extremely cautious and selective.

For India, the year 2017 started on a strong note with deal values surging three-fold in January. While February saw a small decline, March is expected to post a higher volume in the wake of greater certainty on GST rollout and further reforms by the Government.

Snapshot of Key Updates in India

On the regulatory front, the government allowed start-ups issue C-notes and to raise ECB with relaxed conditions. Foreign portfolio investors have now been permitted to invest in unlisted corporate debt securities. The regulations in respect of angel funds have also been relaxed to boost the start-up ecosystem. A new regime for mergers and winding up has been made effective, ushering in simplified and faster processes.

On the taxation front, India signed revised tax treaties with Cyprus, Israel and Singapore. Further, post the demonetization drive by the Government, many changes have been made to provide heavy penalties for undisclosed income. An alternative scheme was also introduced to pay taxes on deposits with penalties.

The period also witnessed substantial progress on GST with fixation of rates and enrolment of dealers. Further, GST bills have also been passed by the Central Government paving the way for its scheduled rollout from 1st July, 2017.

For the first time in independent India, the Union budget was presented on 1st Feb instead of the usual practice of end of Feb. This was done to implement annual spending plans and tax proposals from starting of the new Financial Year. Key highlights of the Finance Act, 2017 with impact on M&A and transfer pricing are captured in the newsletter.

This newsletter aims to capture the key M&A and private investment deals of this quarter and present a brief summary of important tax and regulatory changes. We hope that you find this an interesting read.

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M&A Trends in India

The fourth quarter of 2016 witnessed deals worth USD 21 billion being struck, posting a 163% increment compared to the same period last year. This is attributed to few multi-billion-dollar deals that companies struck either to slash debt or consolidated their market share.

Inbound M&A saw its value treble to more than USD 13 billion while outbound deals slipped by 30%. While the domestic deal volume dropped from 175 to 134 deals, in value terms, it posted an increment of about 28% to tally USD 3.7 bn.

Sector-wise, energy, healthcare, industrials and consumer discretionary sector recorded several high-value deals.

The year 2017 kicked off with USD 2.3 billion deals being struck in January posting a nearly three-fold jump over the year ago period.

Some of the key deals in the above period are:

Vodafone India and Idea Cellular India Ltd have agreed to merge in a transaction creating the country's biggest telecom operator, and world's second largest, valued at USD 23.2 billion. The merger is likely to be completed in 2018 and is subject to approval from Idea shareholders, creditors, SEBI, RBI & other govt. authorities.

In the largest ever infusion of FDI in to India, Russian government-owned energy major Rosneft acquired a 49% stake in Essar Oil. Further, Dutch commodity trading firm Trafigura and Moscow-based fund United Capital bought another 49%. The all cash deal is valued at USD 13 billion, including debt of about USD 6.6 billion.

India's biggest explorer ONGC has agreed to acquire Gujarat State Petroleum Corporation's 80% stake in a gas field off India's east coast for USD 995.26 million. The deal also involves ONGC paying $200 million toward future consideration for six discoveries other than this gas field.

Intas Pharmaceuticals Ltd has acquired Teva Pharmaceutical Industries Ltd's assets and operations of Actavis Generics in UK and Ireland for USD 769 million marking the second largest overseas deal in the Indian pharmaceutical industry.

Wipro Ltd, India's third-largest software services exporter, has agreed to acquire US-based cloud services company Appirio Inc. for USD 500 million in an all cash deal marking its fifth acquisition since July last year.

LafargeHolcim, the largest cement producer in the world, has raised its holding in its two flagship local companies in India - ACC Ltd and Ambuja Cements Ltd by investing USD 320 million.

CK Birla group firm Orient Cement Ltd has struck twin deals totalling USD 300 million with Jaiprakash Associates Ltd to buy the latter's majority stake in its JV with Steel Authority of India Ltd (SAIL) and a cement grinding unit from another group firm to expand to other regions.

Adani Transmission Ltd has signed a binding term sheet to acquire Reliance Infrastructure Ltd's stake in three power transmission projects to strengthen its position as a top private player. The deal value is pegged at USD 294 million.

Bharti Airtel Ltd has acquired the fourth-generation telecom business and airwaves of Tikona Digital Networks Pvt. Ltd for about USD 247 million in cash and debt, as it continues to strike deals to strengthen its position in the wake of growing competition.

Havells India Ltd, the leading maker of branded electrical products in the country, has acquired consumer durables business of Lloyd Electrical and Engineering Ltd for USD 230 million, marking the biggest deal in the industry to date.

Private Investment Trends in India

Private equity investments plummeted by 31% to USD 3.6 billion this quarter compared to Q4 2015. However, compared to Q3 2016, there has been an increase by 29%.

Sector-wise, information technology continues to lead the charts. While there has been a substantial decline across all sectors compared to last year, industrials and financials sectors have witnessed increased investments this year.

The trend continued in Q1 of 2017 with deal value surging by 36% to USD 5.44 billion compared to Q1 of 2016. IT & ITeS accounted for 53% of the investments followed by BFSI and healthcare & life sciences. However, VC investments hit a three-year low this quarter.

Some of the key deals of Q4, 2016 and Q1, 2017 are:

India's largest online retailer Flipkart raised USD 1.4 billion from Tencent Holdings, eBay Inc. and Microsoft. This is the largest funding round for Flipkart. Further, Flipkart is also set to buy eBay's India business as part of the deal.

Leading telecom operator Bharti Airtel has offloaded a 10.3% stake in its tower infrastructure arm Bharti Infratel for USD 952 million to a consortium of global PE firms Kohlberg Kravis & Roberts (KKR) and Canada Pension Plan Investment Board (CPPIB).

Canada's CPP Investment Board has acquired 48% stake in IT outsourcing firm Global Logic from Apax Partners valuing the company at USD 1.5 billion. The transaction is one of the biggest PE exits in the technology sector.

State Bank of India has approved the divestment of its 3.9% stake in SBI Life Insurance Company Ltd. The transaction is subject to regulatory approvals. Buyout firm KKR & Co and Singapore's Temasek Holdings will acquire the stake for USD 265 million.

New York's PE firm Argand Partners that focuses on investments in industrial manufacturers and service providers, has acquired complete stake in Sigma Electric Manufacturing Co. for USD 250 million giving exit to the 10 year old investor, Goldman Sachs's private investment unit.

PE fund True North has acquired 40% stake in Kerala Institute of Medical Sciences (KIMS), a hospital chain providing health care services in India and West Asia (Middle East), held by Ascent Capital and OrbiMed Advisors for USD 200 million.

Homegrown PE firm True North, formerly India Value Fund, has entered into a binding agreement to acquire a majority stake in Home First Finance Company (HFFC) for about USD 100 million, valuing the mortgage firm at USD 150-175 million.

Canadian pension fund manager CPDQ has invested USD 155 million to acquire stake in TVS Logistics Services Ltd., part of TVS Group, giving exit to existing investors- Goldman Sachs and KKR. The transaction is subject to respective board approval and the Competition Commission of India's clearance.

Renewable energy firm Greenko Energy Holdings Pvt Ltd has raised USD 155 million from existing investors, Singapore's sovereign wealth fund GIC and Abu Dhabi Investment Authority (ADIA), marking one of the largest fund-raising exercises in the renewable energy sector.

Key Regulatory Updates

FEMA & FDI

- ***External Commercial Borrowing:*** This quarter witnessed some changes on ECB framework, key highlights are:

ECB by Startups introduced:

  - Entities recognized as startup by Government have been permitted to raise ECB up to USD 3 million
  - ECB can be raised as loans or preference shares (non-convertible / optionally convertible / partially convertible) with minimum average maturity of 3 years.
  - The guidelines also specify freedom for the type of security, mutual agreement for all-in-cost, permission for corporate / personal guarantee, permitted end-uses and hedging in case of INR denominated ECB.

Extension & conversion of matured, unpaid ECB:

  - AD Category I Banks have now been permitted to approve requests from borrowers for extension of tenure and conversion in to equity of matured but unpaid ECB. Besides extant regulations, few additional conditions have also been specified for this.
  - Additional conditions are applicable in case the ECB borrower has availed credit facilities from Indian banking system.

- ***FPI investment in debt:*** As per extant regulations, investment by Foreign Portfolio Investors (FPIs) in unlisted debt securities was permitted only in case of companies in infrastructure sector. Further, investment by FPIs in securitized debt instruments is not permitted.

  To expand the investment basket of FPIs, as was proposed in Budget 2016, FPIs have now been permitted in unlisted corporate debt securities issued by public / private companies with minimum residual maturity of 3 years and certain end-use restrictions. Investment has also been permitted in securitizerd debt instruments without the requirement of minimum 3-year residual maturity.

- ***FDI in LLPs:*** FDI in LLPs was brought under automatic route last year. RBI has recently amended the regulations further relaxing the current provisions:

  - **Conversion of company with FDI into an LLP**: This has now been allowed under automatic route provided that the company is engaged in a sector where foreign investment up to 100 percent is permitted under automatic route and there are no FDI linked performance conditions.
  - **Designated partners**: As per extant provisions, only Indian companies or their nominees who are Indian residents (as per FEMA) could be appointed as designated partners in LLPs with FDI. This condition has now been dispensed with.
  - **ECB**: the stipulation that LLPs are prohibited from raising ECBs has been removed. However, necessary amendments to extant ECB regulations are yet to be introduced for LLPs to avail ECB.

- ***Currency risk for NRIs:*** Currently NRIs are permitted to hedge their Rupee currency risk through 'OTC' (over the counter) transactions with AD banks. With a view to enable additional hedging products for NRIs to hedge their investments in India, it has been provided to allow them access to the exchange traded currency derivatives market.

- ***Convertible notes by Indian start-ups:*** RBI has permitted recognized start-ups to issue convertible notes to person resident outside India. Key highlights are:

  - Minimum investment by investor in a single tranche is INR 2.5 million
  - Convertible note is debt which is:
    - Repayable at the option of the holder, or
    - Convertible into equity shares within a period up to five years from the date of issue of the convertible note, upon occurrence of specified events as per mutually agreed terms and conditions
  - NRIs are also permitted to invest in convertible notes on non-repatriable basis.
  - Investors are permitted to acquire / transfer convertible notes from residents / non-residents subject to pricing guidelines.
  - Government approval would be required for issuing / transfer of convertible notes where start-up is engaged in sector requiring government approval for foreign investment.

Key Regulatory Updates

Companies Law Updates

- ***Incorporating company electronically:*** As a further step to simplify and expedite integrated incorporation process of a company, the MCA has introduced e-Form INC-32.

  The new form provides for e-versions of charter documents of a company. Unlike its predecessor, it can also be used to incorporate a not-for-profit company. It further dispenses the requirements of having to take physical printouts of documents.

  MCA has made it mandatory to use this form only for incorporating a company up to seven subscribers. In case of more than seven subscribers, the usual process is applicable.

  Further, the new form also includes application for PAN and TAN. The Certificate of Incorporation has also been amended to include the PAN of the Company, thus reducing the time for initial tax registration substantially.

- ***Winding up proceedings for offices of foreign companies in India:*** Sub-section (2) of section 391 of the Companies Act, 2013 relates to application of winding up proceedings as per Companies Act, 2013 for closure of place of business of foreign company in India, as if it were a company incorporated in India. The MCA has clarified that this is to be read harmoniously with sub-section (1) wherein foreign companies issue prospectus or Indian Depository Receipts and is therefore applicable to only such foreign companies, not every foreign company.

- ***Demonetization and Balance Sheet:*** MCA has amended the format of financial statements requiring companies to disclose details of cash during demonetization last year. It requires them to provide break-up of cash balances between specified bank notes (INR 500 and INR 1000) and other denomination notes, with details on permitted receipts, permitted payments and amount deposited in banks. Further, an obligation has also been casted on statutory auditor to check compliance with the same.

- ***Revised regulations for Angel Funds:*** To further develop startup ecosystem in India, SEBI has made following amendments for Angel Funds, basis the recommendations of expert committee:

  

  - The upper limit for number of angel investors in a scheme is increased from 49 to 200.
  - The definition of start-up for Angel Funds investments will be similar to definition of DIPP as given in their start-up policy. Accordingly, Angel Funds can now invest in start-ups incorporated within 5 years, which was earlier 3 years.
  - Minimum investment amount by an Angel Fund in any venture capital undertaking is reduced from INR 5 million to INR 2.5 million
  - The lock-in requirements of investment made by Angel Funds in the venture capital undertaking is reduced from 3 years to one year.
  - Angel Funds are now allowed to invest in overseas venture capital undertakings up to 25% of their investible corpus in line with other AIFs.

- ***Corporate Restructurings provisions notified:*** The MCA has made 90 sections of the Companies Act, 2013 effective from 15th Dec, 2016 onwards. These provisions usher in a new regime for mergers, amalgamations and winding up of companies. The new provisions introduce fast track merger wherein no approval of concerned authority is required. Further, minimum thresholds of shareholding / claim to outstanding debt have been specified which give right to shareholders / creditors to raise objections. This comes as a big relief as now only serious objections could thwart the M&A proceedings. The adjudicating authority has also been changed from High Courts to National Company Law Tribunal to provide faster turnaround.

Key Tax Updates

Direct Tax Key Updates

- ***India-Cyprus revised tax treaty:*** India listed Cyprus as a notified jurisdictional area on 1st Nov, 2013 for inadequate exchange of information by Cyprus tax authorities. Due to this, all payments made to Cyprus residents attracted 30% withholding tax and Indian entities receiving money from there were required to disclose source of funds.

  A revised DTAA was signed between the two countries on 18th Nov, 2016. Post the revision, Cyprus was removed from the list of notified jurisdictional area retrospectively from 1st Nov, 2013. This comes as a big relief to investors and Indian companies that have raised capital from Cyprus investors.

  Key highlights of the revised DTAA are:

  - Right to source based taxation of capital gains, at par with Mauritius tax treaty
  - Investments before 1st Apr, 2017 are grandfathered

  It is interesting to note that in Mauritius tax treaty, taxes in India will apply at 50% of domestic tax rate on capital gains during transition period of two years. However, this is not applicable in the case of Cyprus.

- ***India & South Korea sign DTAA:*** India has signed an agreement with South Korea for avoidance of double taxation of income and prevention of fiscal evasion on 18th May 2015, which enters into force on 12th September 2016. The provisions of the Agreement shall have effect in India in respect of income derived with effect from 01st April 2017.

- ***India-Israel Tax Treaty Amended:*** India Israel Tax Treaty was amended on 19th Dec, 2016. The amended provisions are applicable from 1st Apr, 2017. Some of the key changes include insertion of Limitation of Benefit article to restrict treaty benefits if principal purpose test is not met and making available such benefits only to beneficial owner of income. Further, the Most Favoured Nation clause has been omitted.

- ***India-Singapore Tax Treaty Amended:*** In keeping with India's recently revised treaties with Mauritius and Cyprus and joint declaration signed with Switzerland, India and Singapore have amended their DTAA which would be effective from FY 2017-18. Key amendments are:

  - Right to source-based taxation instead of transfer of shares
  - Grandfathering of shares acquired before 1st Apr, 2017
  - Concessional tax rate of 50% of applicable tax rate for transition period of 2 years
  - New provision introduced to prevent economic double taxation in case a transfer pricing adjustment arises on a transaction between an Indian and Singaporean entity.

- ***Determining amount received by shareholders in buy-back:*** Tax on buy-back of shares is payable by shareholders. However, where shareholders were located in jurisdictions where capital gains was exempt, certain unlisted companies would resort to buy-back of shares in lieu of dividends to avoid payment of tax. With effect from 1st June, 2013 this loophole was plugged taxing unlisted companies @ 20% on distributed income for buy-back of shares and exempting shareholders.

  CBDT has now notified final rules for the determining distributed income, covering 12 different circumstances. Some of these are shares issued upon - subscription, ESOP / sweat equity, amalgamation, demerger, acquisition of asset, conversion of firm in to company, convertible securities.

  These rules are applicable from 1st June, 2016 onwards – thus, taxability of buy-back of shares executed prior to this date could be a challenge.

Direct Taxes Key Updates continued…

- ***Place for effective management for companies:*** Place of effective management (POEM) is applicable from AY 2017-18 onwards for determining residential status of companies. Thus, it is important for MNCs in India to assess their residential status while filing income tax returns this year.

  POEM guidelines have been introduced by CBDT on 24th Jan, 2017 as guiding principles. Key features are:

  - Foreign company / body corporate with turnover or gross receipts of INR 500 million or less in a Financial Year would not be considered resident in India, since in this case POEM guidelines are not applicable.
  - Determination of POEM / approach
    - Factual, based on 'substance over form', taking a holistic approach and a year to year determination
    - If the foreign company is engaged in active business outside India POEM would be presumed to be outside India provided majority of the meetings of board of directors of the company are held outside India
    - In case company is not engaged in active business outside India, a two stage process would be followed:
      - identifying persons who actually make key management and commercial decisions for conduct of the company as a whole
      - Determining place where decisions are taken: location of head office, place of holding board meetings, location of senior managers if board has delegated its authority
  - Active business outside India: All of the following conditions need to be satisfied
    - Passive income is not more than 50% of total income.
    - Less than 50% of Total assets are situated in India
- Less than 50% of total number of employees are situated / resident in India and payroll expenses incurred on such employees are less than 50% of total payroll expenditure

- ***Highest depreciation @ 40%*:** Income tax act provides depreciation up to 100% of written-down value in respect of certain assets. The Finance Minister in his Budget Speech, 2015 indicated reduction of corporate tax from 30% to 25% over next four years along with corresponding phasing out of exemptions & deductions. In line with the same, Finance Act, 2016 provided for: tax @ 25% for new domestic manufacturing companies and capping the highest rate of depreciation at 40%.

  The same has been made effective from FY 2016-17 for the new domestic manufacturing companies and from FY 2017-18 for all other taxpayers.

- ***New ITR Forms:*** CBDT has released ITR forms which are to be used this financial year for filing income tax return. The number of forms has been reduced from 9 to 7. ITR Form 1 has been redesigned as a one-page simplified form for salaried class taxpayers. Some of the additional information to be disclosed in ITR are*:*

  - Aadhaar number or Aadhaar enrolment ID. Aadhaar is a 12 digit unique identification number for each individual resident in India
  - Details of cash deposited equal to INR 200k or more in the period of demonetization (9th Nov, 2016 to 30th Dec, 2016)
  - Unexplained credit or investments
  - For individuals and HUFs whose total income exceeds INR 5 million, address of immovable property, description of movable assets
  - Interest held in assets of a firm or AOP as partner / member and details of such firm / AOP
  - Dividend income above INR 1 million
  - Royalty income from patents developed and registered in India
  - Disallowance of expense due to default in deduction / payment of equalization levy
  - For trusts, details of amount applied to charitable / religious purpose

Direct Taxes Key Updates continued…

- ***GAAR clarifications:*** General Anti-Avoidance Rules (GAAR) have been made effective from FY 2017-18 onwards. CBDT has issued a clarification on 27th Jan, 2017 to clarify certain queries on implementation. Some of these are

  - Provisions of GAAR and specific anti-avoidance provisions can apply simultaneously
  - If a case of tax avoidance is sufficiently address by Limitation of Benefit clause in tax treaty, there shall not be an occasion to invoke GAAR
  - If jurisdiction of Foreign Portfolio Investor is finalized based on non-tax commercial considerations and the main purpose of the arrangement is not to obtain tax benefit, GAAR will not apply
  - GAAR will not interplay with the right of taxpayer to select or choose method of implementing a transaction
  - Grandfathering as per the rules will be available to compulsorily convertible instruments, bonus issuances or split / consolidation of holdings in respect of investments made prior to 1st April 2017 in the hands of same investor.
  - If an arrangement has been held to be permissible in one year and the facts and circumstances remain the same, GAAR will not be invoked for that arrangement in a subsequent year.

- ***Clarifications by CBDT:***

  - **Profit-linked deduction in eligible business**: In case of eligible businesses, if there is an increment in profit due to disallowances while computing income under business head, the same can be claimed as profit-linked deduction under relevant section. (Eligible businesses are industrial undertakings, cold storage plant, hotels, housing projects, ships, etc u/s 80IB.

  - **Revenue subsidies from Government**: In line with Supreme Court's recent judgment on the issue, CBDT has clarified that subsidies received from Government by eligible industrial undertakings / businesses towards reimbursement of cost of production / manufacture or for sales of manufactured goods are part of business income. These are not 'income from other sources' and can be claimed as profit-linked deduction.

  - **Re-assessment**: Mere increase in sales turnover (as compared to previous years) because of use of digital mode of payment or otherwise is not, per se, reason to believe for reopening of cases u/s 147 of the Income Tax Act, 1961.

  - **TDS on lump sum lease premium**: The lump sum lease premium/upfront premium paid for acquisition of long term lease, which are not adjustable against periodic rent are not payment in the nature of rent within the meaning of section 194I. Hence, TDS is not applicable in such situation. The view is in line with Delhi high court ruling in the case of Indian newspaper Society where it was held that lease premium paid by assessee to acquire lease hold rights for 80 year is capital expenditure.

Indirect Taxes Key Update

- ***Cross-border B2C OIDAR services*:** As per extant provisions, cross border B2B services are taxable under reverse charge. Further, cross border B2C services provided in taxable territory are exempt. Also, cross border OIDAR services received from overseas service provider are outside levy of service tax as per place of provision of service (PoPoS) rules.

  W.e.f. 01st December 2016 cross border B2C OIDAR services have been brought in to service tax net. Below points summarise the amendment:

  - **Services covered**: Online Information and Database Access or Retrieval (OIDAR) services are those which are automatically delivered over the internet, or an electronic network, where there is no or minimal human intervention. For example: website supply, online software, music, games, distance teaching, e-books, digital ads, cloud services, etc.

  - **Persons liable**: The service provider located in non-taxable territory is responsible for charging and depositing service tax. In cases where such services are delivered through an intermediary (aggregator / marketplace like app store, e-tailers, etc.) the intermediary would become liable unless such intermediary satisfies certain conditions:

  - **Registration**: Service provider can either register themselves or appoint an authorized person / agent in India to comply with service tax provisions. A non-PAN based registration process has been introduced for the same.

  - **Determining whether to charge service tax (ST)**: ST would be chargeable if the service recipient is in taxable territory (India, ex J&K) and the services are provided in a B2C transaction.

  - **Small-scale exemption**: This is available to service providers whose taxable turnover does not exceed INR 1 million in preceding financial year. However, in case of services under a brand /trade name, such exemption is not available.

  - **Cross-border B2B OIDAR services**: These would be taxable under reverse charge mechanism whereby service recipient is liable to discharge service tax liability.

- **Hotel & tour operators / aggregators:** Online aggregators for booking hotels, campsites, etc. were earlier allowed an abatement of 90%. Further, service tax law casts obligations on such aggregators to pay the whole of service tax on reverse charge basis vis-à-vis the hotels, campsites.

  

  Due to existing business practices, service tax was being paid by aggregators only on their commission. This was making offline aggregators less competitive as well.

  Service tax rules have been amended effective from 22nd Jan, 2017 to provide that online aggregators would not be liable to pay service tax on such services provided following conditions are satisfied:

  - Hotels, campsites, etc. have service tax registration, and
  - Hotels, campsites, etc. receive amount due to them directly from the customer

  Further, instead of earlier 2 different rates of abatement, a uniform abatement of 40% has been provided for all tour operators. Also, tour operators would no longer be able to credit of input services from other tour operators.

- **Exemptions withdrawn:**

  - Charitable entities registered under Section 12AA of the Income Tax Act were exempted from tax on OIDAR services. This exemption has been withdrawn w.e.f. 30th Jan, 2017.

  - Certain services provided to educational institutions were hitherto exempt. With effect from 1st Apr, 2017 this exemption has been restricted only to institutions providing education up to higher secondary school or equivalent.

- **Transportation of goods up to customs clearance:** Service tax has been introduced on transportation of goods from outside India to customs station of clearance in India. Further, the person-in-charge of vessel / his agent carrying such goods has been made liable to pay service tax on reverse charge basis.

Finance Act 2017 – Impact on Private Investments and M&A

- ***Long term capital gains in case of immovable properties:*** Capital gains are termed as long-term or short-term based on holding period of capital assets. With a view to furthering investment in real estate, the holding period for immovable property has been reduced from 36 months to 24 months. This would be effective from financial year 2017-18.

- ***Notional rental income:*** Currently, unsold inventory in real estate project is deemed to provide developers notional rental income. Due to this, developers were induced to offload units at the earliest possible, even at prices below market prices. This is now being amended to provide that such notional rental income would be considered as nil for up to one year from end of financial year in which certificate of completion is received.

- ***Base year for computation of capital gains:*** As per extant provisions, for computing capital gains in respect of an asset acquired before 1st Apr, 1981, the assessee has an option to take fair market value (FMV) of the asset as on 1st Apr, 1981 or the actual cost as cost of acquisition. This base year has now been revised to 1st Apr, 2001 from the financial year 2017-18. The cost inflation indices would also be accordingly revised.

- ***Neutrality in conversion of preference shares to equity shares:*** Tax neutrality already exists in case of conversion of bond or debenture of a company to share or debenture of the company. This is now being extended to conversion of preference shares into equity shares. Further, cost of acquisition of preference shares & their period of holding shall be respectively considered as cost of resultant equity shares & period of holding of such equity shares.

- ***FMV in case of unlisted shares:*** To ensure that full value of consideration is not understated, the income tax act provides for deeming provisions in certain cases like immovable property. This is now being made applicable for unlisted shares also, wherein FMV would be the full value of consideration if the sale consideration is less than the FMV. This is applicable from next financial year and rules for computing FMV would be specified.

- ***Extension of holiday period for startups:*** Recognized start-ups can now claim tax deduction for any three consecutive years out of seven years from date of incorporation, compared to out of five years earlier.

- ***Carry forward of losses by startups:*** The existing provision of income tax do not permit carry forward of losses of a closely held company if there is a change in shareholding of the company by more than 49%. In case of start-ups, this requirement is being relaxed. It is now provided that losses incurred within seven years from incorporation of start-up can be carried forward for set off if all the shareholders at the end of the year(s) in which such losses were incurred continue to hold those shares in the year of set-off of such loss.

- ***Taxation of foreign portfolio investors:*** Non-resident investors in registered category I and category II Foreign Portfolio Investors as per SEBI regulations are being exempted from indirect transfer provisions. This is being made applicable from FY 2011-12 onwards.

- ***Taxation of income on bonds/ borrowings:*** Applicability of concessional TDS @ 5% is extended as per following:

  - Interest payable to FIIs and QFIs on government securities and rupee denominated bonds, extended to interest payable due on or before 1st July, 2020
  - Interest on ECB and long term bonds extended to ECB and long term bonds issued up to 1st July, 2020. Further, this benefit is also made applicable to rupee denominated bonds from FY 2016-17 onwards.

  Benefit of ignoring gains on account of appreciation of rupee against foreign currency, at the time of redemption of rupee denominated bonds, has been extended to secondary holders as well. Further, transfer of rupee denominated bonds between non-residents is exempted from capital gains from FY 2017-18 onwards.

- ***Abolition of FIPB:*** With successful implementation of e-filing and online processing of FDI applications, Foreign Investment Promotion Board is set to be abolished in coming FY.

Finance Act 2017 – Transfer Pricing

- ***Thin-capitalization rules for related parties:*** Borrowing from BEPS Plan Action 4, thin capitalization norms for associated enterprises have been introduced to prevent base erosion and profit sharing via excessive interest deduction. Key highlights are:

  - Interest payment up to INR 10 million per annum is not covered under this requirement.
  - The interest expenses claimed by an entity to its associated enterprises shall be restricted to 30% of its EBITDA.
  - The interest expense beyond 30% is allowed to be carried forward for next 8 years.
  - Implicit / explicit guarantee to lender or deposits with lender by associated entreprise would also be considered as debt from the associated enterprise.
  - The provision is applicable for interest payment for FY 2017-18 and onwards.

- ***Specified Domestic Transaction:*** Finance Act, 2012 had extended transfer pricing provisions to expenditures under transactions with domestic related parties and inter-company transactions where one of companies involved is enjoying any tax holiday / profit linked deduction.

  With a view to reduce compliance burden, the scope of domestic transfer pricing is being restricted to exclude expenditures under transactions with related parties. Thus, transfer pricing documentation and compliance requirements in such case are now dispensed with. It has been made applicable from FY 2016-17 onwards.

- ***Secondary adjustments introduced:*** In line with OECD transfer pricing guidelines and international best practices, secondary adjustment provisions have been introduced.

  Secondary adjustment means adjustment in the books of accounts of the taxpayer and its associated enterprise to reflect that the actual allocation of profits between the two is consistent with the transfer price determined as a result of primary adjustment. This removes the imbalance between cash account and actual profit of the taxpayer.

  Key highlights are:

  - The provision is applicable where primary adjustment has been made:
    - *Suo motu* by the assessee in ITR, or
    - Made by assessing officer and accepted by assessee, or
    - Determined by an Advanced Pricing Agreement, or
    - Made as per safe harbor rules, or
    - As per settlement under Mutual Agreement Procedure
  - The provision is applicable from FY 2017-18 onwards where the amount of primary adjustment exceeds INR 10 million for the year.
  - Where as a result of primary adjustment, there is an increase in total income or reduction in loss, the excess money available with its associated enterprise (AE) would be required to be remitted to India within a prescribed time. In case of failure to do so, such excess would be deemed as an advance by the assessee to such AE and prescribed interest would be computed on such advance.

Finance Act 2017 - Miscellaneous

- ***Time limit on assessments:*** The existing time limit for assessments is 21 months from end of assessment year (AY). This is being reduced to 18 months for AY 2018-19 and 12 months from AY 2019-20 onwards.

- ***Filing of ITR:*** In case of delay in filing of ITR beyond due date, from AY 2018-19 onwards, instead of penalty, late fee as per following details is being made applicable:

  - Where ITR is furnished on or before 31st Dec of the assessment year, INR 5,000
  - Where ITR is furnished after 31st Dec, INR 10,000

  It has also been provided that where total income is up to INR 500k, late fee up to INR 1,000 would be levied.

  ITR may be revised by an assessee before end of one year from end of AY or completion of assessment, whichever is earlier. This period is being reduced to end of assessment year or completion of assessment, whichever is earlier.

- ***Income tax refunds:*** As per extant provisions, process of ITR and grant of refund is not necessary in case of scrutiny assessments. The Finance Act, 2016 amended to provide that processing of ITR is to be made before passing of assessment order from AY 2017-18 onwards.

  To address grievance in delay of issuance of refund, this provision is now being altogether dispensed with from AY 2017-18 onwards. To protect interest of revenue, a new provision is introduced empowering assessing officer to hold the refund, with prior approval of Principal Commissioner or Commissioner, up to passing of assessment order.

- ***Lower Tax Rates:*** For AY 2018-19, the tax rate for individuals for the income slab of INR 250k to INR 500k has been reduced from existing 10% to 5%.

  The rebate of up to INR 5,000 for AY 2017-18 available to resident individuals whose total income is up to INR 500k is being scaled down to INR 2,500, available where total income is up to INR 350k.

  On the other hand, a surcharge @ 10% of the income tax would be applicable for individuals where total income is above INR 5 million and up to INR 10 million.

  For companies, the Finance Act, 2016 had reduced tax rate to 29% (excluding surcharge & cess) in case of domestic companies whose turnover in FY 2014-15 was up to INR 50 million. Further, in case of new manufacturing companies, the tax rate was reduced to 25% subject to certain conditions.

  In this year's budget, the applicable tax rate is being reduced to 25% for all domestic companies if total turnover of FY 2015-16 does not exceed INR 500 million.

- ***MAT / AMT:*** Presently, credit of MAT / AMT can be carried forward for up to 10 assessment years (AYs) immediately succeeding the assessment year to which it relates. To provide relief to taxpayers, this period has now been extended to 15 AYs.

  Further, it is also being provided that credit of MAT / AMT shall not be allowed to be carried forward to the extent it relates to the difference between Foreign Tax Credit (FTC) allowed against MAT / AMT and the FTC allowable against income tax liability as per regular provisions of income tax.

- ***Restricting / Discouraging cash transactions:***

  - Cash donations eligible for deduction u/s 80G reduced from INR 10k to INR 2k
  - Expenditure for acquisition of capital asset for which cash payment to a person in a day exceeds INR 10k, then such expenditure would be ignored for determining actual cost of such asset. Further, no investment-linked deduction, available otherwise, would be allowed in such case.
  - Limit for tax deductible expenditure via cash payments to a person in a day is being reduced from INR 20k to INR 10k.
  - The minimum presumptive rate of taxation for businesses having turnover up to INR 20 million is being reduced from 8% to 6% for such portion of turnover as is received otherwise than in cash.
  - Prohibition on receipt of more than INR 200k from a person in a day or in respect of single transaction or in relation to one event from a person.

Other Buzz

- ***GST:*** Goods and Services Tax continued to remain the buzzword for the year 2016. After passage of constitutional amendment bill by both the houses of parliament in August, the government had issued model GST law and GST council was also constituted to finalize the same.

  Meanwhile, the Government had already launched a new web-portal for GST wherein dealers registered under various State and Central indirect tax laws such as Central excise, Service Tax, VAT, Entry Tax, Luxury Tax and Entertainment Tax are to enrol under GST Regime.

  Both the Lower House and the Upper House of the Parliament recently passed the four bills of GST on 29th March and 6th April respectively. With the parliament's nod, the implementation of GST from July 1 is quite certain. The final rules and rates would be determined around mid of May. The onus now shifts on to the States to pass GST bill in their respective assemblies.

  The GST would have far-reaching impacts on profitability and across various business functions. It would also bring a larger portion of the unorganized sector into the mainstream changing the business dynamics of several industries.

  Some of the issues which need to be addressed are restructuring supply chain, open customer contracts in certain sectors, analyzing tax impact particularly where substantial VAT / excise incentives are applicable, pricing of products considering also the anti-profiteering clause, etc.

- ***Demonetization*:** In an unscheduled televised address at 8 pm IST on 8th Nov, 2016, the Prime Minister of India announced annulling of legal tender of currency notes of INR 1000 and INR 500 from the midnight of the said date. These notes comprised 86% of the country's overall currency. New currency notes of INR 500 and INR 2000 denominations were issued.

  The old notes could be deposited / exchanged till 31st Dec, 2016 with any Issue office of the RBI or any branches of banks.

  Demonetization has been hailed by the Government as a masterstroke to combat inflation, corruption, and to discourage generation of black money (undisclosed income) and counterfeit currency.

  While this move of the Government has seen mixed reactions, the logistics issues in issuance of new currency haunted the public for quite some time bringing to a halt various business activities for the short run.

  While the jury is still out as to the mid to long term impacts of this move, few sectors like FMCG, real estate have seen a dip in activity. On the other hand, there has also been domino effect on e-commerce which has seen a jump in sales thanks to widespread adoption of digital wallets and online payments. The banking system is also expected to further improve as India heads towards a cashless society.

Glossary

Abbreviation	Description
AD	Authorized Dealer
AMT	Alternate Minimum Tax
CBDT	Central Board of Direct Taxes
CGST	Central Goods & Services Tax
DTAA	Double Taxation Avoidance Agreement
DTAC	Double Taxation Avoidance Convention
EBITDA	Earnings Before Interest Tax Depreciation & Amortization
ECB	External Commercial Borrowing
FIPB	Foreign Investment Promotion Board, India
FMV	Fair Market Value
FPI	Foreign Portfolio Investors
FY	Indian Financial Year
GST	Goods & Services Tax
IGST	Integrated Goods & Services Tax
Ind AS	Indian Accounting Standards
INR	Indian National Rupees
ITR	Income Tax Return

Abbreviation	Description
k	Thousand
LLP	Limited Liability Partnership
MAT	Minimum Alternate Tax
MCA	Ministry of Corporate Affairs
NCLT	National Company Law Tribunal
OECD	Organization for Economic Co-operation & Development
PAN	Permanent Account Number
PE	Permanent Establishment (for International tax)
PE	Private Equity (for investments)
SEBI	Securities and Exchange Board of India
SGST	State Goods & Services Tax
TCS	Tax Collected at Source
TDS	Tax Deducted at Source
u/s	under section
VAT	Value Added Tax
VC	Venture Capital

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