WHITE PAPER: PRIVATE EQUITY AND VENTURE CAPITAL

1. Bird's Eye View

India is globally recognized as a developing yet highly competitive economy with enormous potential. The Government's commitment and its policy initiatives towards liberalization of foreign investments, growth of service sector, rationalization of regulatory framework, capital market reforms coupled with business opportunities and increased standard of living are the key contributors to the fast paced and robust Indian economy.

Private equity investing is the business of investing in privately-held companies or those that are taken private in the process. Investment strategies of Private Equity Firms ("**PE Firms**") have assumed different forms since its evolution, such as leveraged buyouts, venture capital, growth capital, distressed investments and mezzanine capital. In adherence with the complexity of India's legal environment and corporate governance structure of Indian companies, PE firms have evolved a hybridized Indian private equity model focusing on minority investment structures, investor control rights and exit strategies.

Venture Capital is financial capital provided to early-stage start-up companies with a high potential for growth after the early growth funding round, also known as seed funding. Venture capital are considered to have both high-growth and high-risk potential. As the investment is high risk, most venture capitalists gain significant control over company decisions and a large portion of the company's ownership. These companies generally center on new technology, including e-commerce, software and mobile applications. Healthcare, retail, transportation, food delivery, housing and education are some of the most preferred sectors for venture capitalists in recent times.

India has emerged as an attractive destination for top Venture Capitalists and Private Equity players.

Recent trends in India:

Since its evolution in India, the focus of private equity investments was largely in the high growth sectors such as the information technology **("IT")** and IT-enabled Services, financial services etc. Since then, PE Firms have diversified their interest to other high potential sectors such as manufacturing, consumer technology, real estate, banking, infrastructure, insurance, e-commerce, retail, pharmaceuticals and biotechnology. Despite the dot com bubble bursting during 1991-2001, India has seen a major upswing and interest in the e-commerce

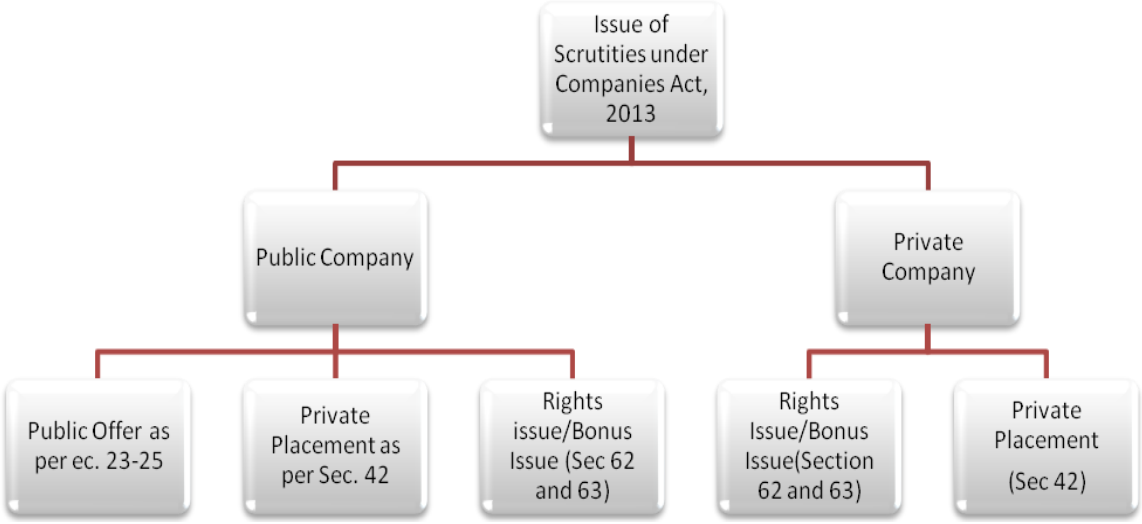
sector, with leading online e-retailers raising funding of almost USD 4 Billion from multiple investors only over the last couple of financial years.

In general, India has received a record USD 22.4 billion in investments the financial year 2015-16, 31.8% more than the previous highest of USD 17 billion in 2007. Consumer technology, real estate and banking, financial services and insurance sectors have witnessed the maximum investments in the previous financial year, thereby making India as one of the most preferred private equity investment destination for the investors around the world.

In the past few years, India's equity market has seen a change in pace. PE Firms have altered their investment strategies, and Private Investments in Public Equity (**"PIPE deals")** have become evident, where shares of the target company are purchased at a discount to the market value, providing capital to the company. PIPE deals have evolved primarily in semi-large and mid-cap companies across sectors. The major upside of PIPE deals is relaxation from the complexity of selling shares through a fresh public issue. Further, there is reduced risk of under subscription and equity dilution as the deal is between the investor and the issuer. However, the mandate to make an open offer, where investment exceeds 24% as per SEBI (Substantial Acquisitions of Shares and Takeover) Regulations, ("**SEBI Takeover Code"**) sometimes disincentivizes PE Firms to delve in the listed space.

2. Legal Framework

Chapter III and IV of the Companies Act, 2013 ("**the Act**") along with the Companies (Share Capital and Debenture) Rules, 2014 governs the issuance of securities by a company. While Chapter III deals with public issues and private placements, Chapter IV deals with the kinds of share capital, rights on shares and issuance of capital. This section provides a broad overview of the aforementioned provisions.



Public Offer (Section 23-25)	➢ *A public company may issue securities through prospectus by way of an initial public offer, further public offer or offer for sale of securities to the public by an existing shareholder of the company.* ➢ *A company making a public offer has to make an application to a recognised stock exchange for listing of the securities being offered.* ➢ *Companies making a public offer of securities are subject to compliance with provisions of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009.*
Private Placement (Section 42)	➢ *Invitation for subscription of securities is made through the issuance of a private placement offer letter.* ➢ *Offer of securities through private placement can be made to a maximum of 50 persons in one financial year. Such computation of the number of persons is towards excluding Qualified Institutional Buyers as defined under SEBI (Issue of Capital and Disclosure Requirement) Regulations and employees to whom stock options have been issued.* ➢ *No subsequent offer can be made by the company unless the previous offer has been completed, withdrawn or abandoned by the company.* ➢ *Any offer or invitation not in compliance with the provisions of Section 42 is construed to be a public offer and is regulated by the provisions of Sections 23-25.*
Rights Issue (Section 62)	➢ *The Companies Act, 2013 does not specifically define the concept of rights issue.* ➢ *Shares are offered through issuance of offer letters to the existing equity and preference shareholders of the company. Shares are offered on a uniform basis to all the shareholders.* ➢ *The Offer has to be kept open for a minimum period of 15 days not exceeding 30 days.* ➢ *Shares are issued pursuant to receipt to acceptance or renunciation letters from the shareholders.*

Indian Contract Act, 1872 ("the Contract Act"):

The investment agreements in a private equity transaction and the rights and remedies available there under are administered in accordance with the provisions of the Indian Contract Act, 1872. Certain clauses articulated in the commercial agreements like the representations, warranties and indemnities provided by the investee company and/or the promoters are enforced as per the provisions of the Indian Contract Act, 1872 only and damages under the said Act can be claimed from the defaulting party in case of any loss arising out of any such breach thereof. Further, the provisions of the Indian Contract Act, 1872 in relation to the *privity* of contracts and third party beneficiaries are relevant in determining the rights and liabilities of the third parties including affiliates to the contracting parties in a commercial contract.

Further, the inception of Companies Act, 2013 established the enforceability of pre-emptive rights and drag/tag rights and settled the position relating to transferability of shares of a public company. Under Section 58(2) of the Companies Act, 2013, share transfer restrictions are enforceable as contract, for which action may be brought by the aggrieved party as stipulated under the provisions of Indian Contract Act, 1872.

3. Regulatory Framework

Although foreign investment has been allowed in India since 1973, it was in 1991 when with the view of liberalizing the economic framework and facilitating external trade, the Foreign Exchange Management Act **("FEMA")** was passed, pursuant to which foreign investors have been allowed to make investments in Indian companies either under the automatic route or the approval route, subject to certain sector specific caps and conditions.

The Reserve Bank of India **("RBI"),** Foreign Exchange Promotion Board **("FIPB")** and the Department of Industrial Policy and Promotion, Ministry of Commerce **("DIPP")** are the nodal agencies for regulating foreign investments in India. The issuance and dealing of shares of an Indian company are administered by the Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulation, 2000 **("TISPRO Regulations").** In addition to this, if the securities are listed or offered to the public, dealings in such securities are regulated by Indian Securities market regulator, the Securities and Exchange Board of India **("SEBI").**

The following are the different routes for permitted foreign investments in India:

Foreign Direct Investment

Foreign Direct Investment ("**FDI**"), as distinguished from portfolio investment, is directed towards establishing a 'lasting interest' in an enterprise that is resident in an economy other than that of the investor.

Consolidated FDI Policy

- *The DIPP, under the Ministry of Commerce and Industry, formulates the consolidated FDI policy annually, to capture and keep pace with the regulatory changes, effected in that particular financial year.*
- *The policy lays down guidelines on the sector specific framework, entry routes for investment and eligibility of investors.*
- *The RBI also issues a Master Circular every year, consolidating the rules governing foreign investments in India.*[1]

Instruments

- ***FDI can be routed through the following instruments:-***

Equity Shares	*CCPS*	*CCD*	*Partly Paid Shares*
- *Participation in governance.* - *Dividend to be declared only out of profits.* - *Ranks last in terms of liquidation preference*	- *Fully and Convertible into equity.* - *Assured dividends on accrued profits and preference over equity shares.*	- *Fully and Convertible debentures* - *Fixed interest payments irrespective of accrual of profits.* - *Ranks higher in terms of liquidation preference.*	- *Atleast 25% of the consideration amount to be paid upfront.* - *The remaining amount to be brought in within 12 months of issue.*

- *Debentures which are not compulsorily or optionally convertible are considered to be more in the nature of debt and are less favored.*
- *Share Warrants issued by an Indian company in accordance with the provision of the Companies Act, 2013 and the SEBI guidelines, as applicable, have been made eligible instruments for the purpose of FDI and FPI.*

Pricing Guidelines:

- *TISPRO regulations lay down the pricing guidelines for divestment of foreign investment in India. While pricing guidelines in case of listed shares have always been based on the price of the share as on the stock*

[1] " RBI Master Circular on Foreign Investment in India", dated July 01, 2015 and updated up to October 30,2015(See:https://rbidocs.rbi.org.in/rdocs/notification/PDFs/96MC7984B235BAB249D5ADCD6277CCD68D0D.PDF)

	exchange, which continues under the present regulations, the policy on pricing guidelines with respect to unlisted shares has been amended over time. ➢ *The RBI in July 2014 announced the withdrawal of all existing guidelines relating to valuation in case of an acquisition/sale of shares of an Indian company and notified that valuations would need to be performed according to any internationally accepted pricing methodology on an arm's length basis.* ➢ *Under the revised pricing guidelines, the valuer would need to apply professional judgment and the applicable valuation methodologies on a case-by-case basis. Accordingly, other valuation methodologies such as the Market Multiple method, Comparable Transactions method, Net Asset Value method, etc., would also will need to be considered while valuing FDI-permissible instruments, including warrants and partly paid shares. Since the new guidelines emphasize on applying the revised pricing guidelines on an arm's length basis, this enables Indian companies to comply with not only the RBI guidelines on pricing but also with transfer pricing regulations.*
Exit Options	➢ *Call options and put options are rights typically provided under various commercial agreements, as exit strategies for the investors. In view of safeguarding their interests in the investee company, option clauses are often inserted by the investors to ensure hassle-free exit with assured returns. These Option clauses have often been less favored by the RBI since these contracts are construed more in the nature of debt as opposed to equity, thereby defeating the spirit of the FDI policy.* ➢ *In the year 2013, SEBI legitimized option contracts and contracts for pre-emption entered into by listed and unlisted public companies. In conformity with SEBI's notification and aligning with the international standards, RBI accepted exercise of call and put options in equity shares and compulsorily convertible preference shares/debentures to be issued to non-residents.* ➢ *The exercise of optionality clauses is subject to a minimum lock-in period of one year or as prescribed by FEMA regulations. Call/put options have to be exercised at the market price prevailing at the recognized stock exchanges or as per any internationally accepted pricing methodology on arm's length basis in case of unlisted companies. As per the notification, the Investors are denied exit from their respective investment with assured returns.* ➢ *RBI in its Monetary Policy statement dated February 3, 2015, relaxed the pricing of instruments/securities, including assured returns at a pre-contracted price to the foreign investors while exercising exit options. The said relaxation ensures greater downside protection to the investors, making India a more lucrative ground for foreign investment.*

Foreign Portfolio Investment ("FPI Regime"):

- SEBI introduced the SEBI (Foreign Portfolio Investment) Regulations, 2014 ("**FPI Regulations**") effective from June 1, 2014, unifying the extant Portfolio Investment Scheme for Foreign Institutional Investor ("**FII**") and the Qualified Foreign Investor ("**QFI**").

- An investor can be registered in accordance with FPI Regulations as Registered Foreign Portfolio Investor ("**RFPI**") through designated depository participants. Existing FIIs/sub-accounts and QFIs can buy, sell or otherwise deal in securities in accordance with these regulations, for a period of three years and one year respectively. Under the FPI regulations, investment made by a single FPI or an investor group is subject to a cap of 10% of the total issued capital.

Categories of FPI

Category I	***Category II***	***Category III***
Government related Investors, Government Agencies, International agencies.	*Broad Based Funds, University Funds, Pension Funds, SEBI registered FIIs and Sub-accounts.*	*FPIs not eligible under Category I and Category II, Charitable societies, trusts, family offices, etc.*

Instruments

- *FPIs can invest in instruments such as listed or to be listed shares, government securities, units of mutual funds or collective investment schemes, treasury bills, corporate debt and Indian depository receipts.*
- *RFPI can purchase/sale shares and debentures on the floor of stock exchange under the FPI Scheme, without being subjected to restrictions under the FDI Scheme.*

Offshore Derivate Instruments ("ODI")

- *An ODI under FPI Regulations is defined to mean any instrument, which is issued overseas by a foreign portfolio investor against securities held by it that are listed or proposed to be listed on any recognized stock exchange in India, as its underlying units.*
- *ODIs allow foreign investors, such as high net worth individuals and hedge funds based overseas, to invest in the Indian market without being registered with the SEBI.*
- *FPIs may issue, subscribe or deal in ODIs provided that they are issued in compliance with KYC norms and only to persons regulated by an appropriate foreign regulatory authority.*
- *Category III FPIs are not permitted to issue, subscribe or otherwise deal in ODIs, directly or indirectly.*
- *The position of the holder of an ODI is usually that of an unsecured counterparty to the FPI as the ownership of the underlying securities, voting rights and other attributes pertaining to ownership vests with the FPI. This is opposed to the international scenario, wherein the ODI*

	holder is perceived to be the beneficial owner.
Non-Convertible Debentures ("NCD")	➢ *Prior to 3 February 2015, under the FPI regime, all categories of FPIs were free to invest in all types of rupee denominated NCDs which are listed or to be listed within 15 days of allotment of the NCDs (except in the case of infrastructure companies, where even unlisted NCDs can be subscribed to by FPIs) as well as commercial papers which are short term in nature (lasting one year or less).* ➢ *RBI and SEBI vide circulars dated February 03, 2015, have amended the FPI regime to prohibit fresh investment by FPIs into corporate debt which has a residual maturity of less than three years. The RBI further explained that fresh investment by FPIs in a debt instrument with a minimum residual maturity period of three years, but with an option to sell such instrument prior to the expiry of the three year duration of residual maturity, would be prohibited.* ➢ *Subject to aforesaid, FPI's are permitted to invest inter alia, in listed or to be listed NCDs in dematerialized form issued by Indian companies, subject to an overall limit of USD 51 Billion of which 90% is available on tap basis.* ➢ *There are no interest caps on NCDs and are usually redeemed at a premium that is typically based on the sale proceeds received by the company.* ➢ *NCDs subscribed under the FPI route are exempted from the terms of pricing under the FDI route.*

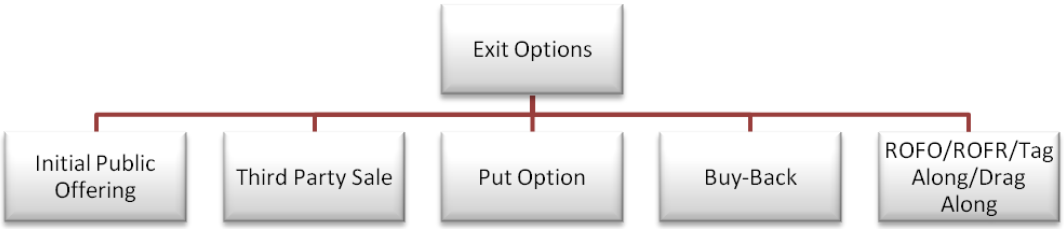
Foreign Venture Capital Investment:

➢ *The SEBI (Foreign Venture Capital Investors) Regulations ("**FVCI Regulation**s") were introduced by the SEBI in the year 2000, to encourage foreign investment into venture capital undertakings.*
➢ *Foreign Venture Capital Investors ("**FVCI**") under the regulations invest either directly or through venture capital fund(s)/alternative investment funds.*
➢ *Under Section 10(23FB) of the Income Tax Act 1961) income received by venture capital funds from their investments in venture capital undertakings operating in all sectors is exempted from tax implications..*

Instruments	➢ *As opposed to the FDI regime, FVCIs can invest into Optionally Convertible Redeemable Preference Shares ("**OCRPS**"), Optionally Convertible Debentures ("**OCDs**") or even Non-Convertible Debenture ("**NCDs**"). at least 66.67% of the investible funds shall be invested in unlisted equity shares or equity linked instruments of Venture Capital Undertakings* ➢ *FVCIs are allowed to invest in the eligible securities by way of private arrangement/purchase from a third party or on a recognized stock exchange, subject to terms and conditions as stipulated in TISPRO and FVCI Regulations as amended from time to time.* ➢ *In terms of the Consolidated FDI Policy of 2016, FVCIs are now permitted to invest in (i) Indian companies engaged in any of the 10 (Ten) sectors listed in*

	Schedule 6 of FEMA 20, including the newly added infrastructure sector; (ii) startups irrespective of the sector in which the startup is engaged; (iii) units of a VCF or of a Category I Alternate Investment Fund (Cat I AIF) or units of a scheme or a fund set up by a VCF or by a Cat I AIF.
Free Pricing	➢ *The entry and exit pricing applicable to the FDI regime do not apply to FVCIs. To that extent, FVCIs can subscribe, purchase or sell securities at any price.*
QIB Status	➢ *FVCIs registered with SEBI have been accorded the status of Qualified Institutional Buyer ("**QIB**") and are accordingly eligible to subscribe to securities at the initial public offering of a venture capital undertaking through the book-building route.*

4. **Exit Strategies**:



Initial Public Offering ("IPO")	➢ *This is the traditionally preferred route for exit under which private equity investors have a right to offer their shares for sale under an IPO and then exit.* ➢ *The benefits of an IPO include higher valuations, which can be achieved so long as the markets are buoyant. Further, there is management co-operation as their operational control is sustained, providing investors with benefits of long and stable shareholding in the company* ➢ *The main downside include: (i) valuation is dependent on prevailing market conditions, (ii) there are considerable transaction costs, (iii) careful planning is required, and (iv) the process takes long to implement, during which period, a drastic change in market changes may warrant abandonment of the IPO.* ➢ *The other drawback is that the IPO may not give large private equity investors a full clean exit. The public generally perceives this as lack of investor confidence in the company which in turn may have downside effects on the market valuation of the company.*
Third Party Sale	➢ *Sale of shares to any third party buyers such as strategic investors,*

	financial investors, competitors, other private equity investors or mutual funds is another exit strategy employed by investors. ➢ *The major upside to this exit strategy is speed, liquidity and control.* ➢ *However, there might be some resistance from the management of the portfolio companies in transferring control to another investor, especially to an existing or potential competitor.*
Put Option	➢ *Shareholders can sell shares to another existing shareholder at a specified price at the time such holder wishes to exit its investments in the investee company.* ➢ *Such other shareholders will have an obligation to purchase those shares at the said predetermined price.* ➢ *The exercise of Put Option may prove to be beneficial for financial investors who make investments to reap benefits and earn profit from the investment.* ➢ *The put option may be vis-à-vis the investee company or the shareholders of the investee company.*
Buy Back	➢ *Private equity investors could agree to exit via a buy-back of shares at a mutually agreed internal rate of return.* ➢ *Such buy-back has to be in conformity to the restriction imposed on buying back the shares for a period of 1 (one) year, profitability, debt equity ratio concept as set out in the Companies Act, 2013 read with the rules framed thereunder.* ➢ *Certain private equity investors use this as a last resort when they know that an enterprise has not had a significant increase in its value.* ➢ *Only one buy back can be conducted in one financial year.*
ROFR/ROFO/Tag Along and Drag Along	➢ *These are standard transfer restrictions/exit mechanisms agreed under investment documentation.* ➢ *Where the promoters have failed to provide the investor with the agreed exit from company, "drag" provisions in favour of the investor are useful.*

5. Taxation Framework:

The tax applications in a private equity transaction are principally governed by The Income Tax Act, 1961 ("**the IT Act**") wherein an entity is taxed on the income generated in India. Furthermore, India has entered into a series of tax treaties with offshore jurisdictions under which a taxes are levied to the extent it is more beneficial for the

taxpayer. A detailed analysis is of the tax reign is set out below:-

Corporate Tax

- *Indian Companies are taxed against profits earned by them during a given taxable period. The company's operating earnings, after depreciation have been deducted from revenues comes within the tax net.*

Sr. No.	***Category***	***Rate of Corporate Tax***
1.	*Resident companies*	*30%+surcharge and educational cess*
2.	*Non-resident companies.*	*40%+surcharge and educational cess*

- *A company is said to be' resident' in India if it is incorporated in India or is wholly controlled and managed in India. A company is said to be non-resident in India if it is not an Indian company and some part of the control and management of its affairs is situated outside India.*
- *Non-resident companies are taxed on income derived from India, including in situations where profits of the non-resident entity are attributable to a permanent establishment in India.*

Minimum Alternate Tax ("MAT")

- *In addition to the corporate tax, MAT is payable by companies at the rate of around 18.5% on the book profits of the Company, where the tax payable by the company is less than 18.5% of its book profits.*
- *With effect from April 01, 2015, FPIs/FIIs have been exonerated from applicability of MAT with respect to capital gains income. This might set up a lucrative tax regime for investment through FPIs/FIIs as most of the income earned by FPI's and FII's are treated as capital gains income.*

Dividends and Share Buy Back

- *Dividends declared or distributed by Indian companies are taxed under distribution tax* ***("DDT")*** *at the rate of 15%, at the hands of the company.*
- *As the tax payable is computed on a grossed up basis under domestic law, shareholders are exempted from any further tax on the dividends received by them.*
- *Any dividend received by an Indian company from a foreign company is taxed at the rate of 15%.*
- *An Indian company is also taxed at the rate of 20% on gains arising to shareholders from distributions made in the course of buy-back or redemption of shares.*

Capital Gains

- *In case of share purchase, the tax issue concerned will be of capital gains tax. The rate of taxation depends on the period of holding of the asset, which determines whether the resulting gain is in the nature of*

a long term capital gain or a short term capital gain. Long term capital gains arise to a company, from transfers of capital assets held for a period of more than 36 months (12 months in the case of shares or any other listed securities). No tax is payable if the share transferred are of a listed company in India and the transaction is completed on the floor of the stock exchange after payment of securities transaction tax.

- *Short term capital gains are ordinarily taxed as part of the total taxable income of the assessee. Short term capital gains arising from transfers of capital assets within a period of 36 months (within 12 months in the case of shares or any other listed securities) from the date of acquisition. Foreign shareholders could also claim adjustment of exchange control fluctuations whilst computing the capital gains.*

Interest

- *Interest earned by a non-resident may be taxed at a rate between 5% to around 40% depending on the nature of the debt instrument.*

DTAAs

- *India has Double Taxation Avoidance Agreements with several countries with the object of minimizing dual tax levy in international transactions. DTAAs often have a lower rate of tax as compared to rates in the Income Tax Act.*
- *Until recently, Indo-Mauritius DTAA was considered as one of the most favorable DTAAs thereby making Mauritius a very tax friendly jurisdiction for the investors to route their investments in to India. However recently India has renegotiated its DTAA with Mauritius and a Protocol dated May 10, 2016 has been entered into towards amending the same. The protocol amends the existing residence based tax regime under the Mauritius DTAA and gives India a source based right to tax capital gains that arise from alienation of shares of an Indian resident company acquired by a Mauritian tax resident. It provides for grandfathering of all existing investments up to March 31, 2017, with the revised position being applicable only to investments made on or after April 1, 2017. A further relaxation in respect of capital gains arising to Mauritius residents from alienation of shares has been provided between April 1, 2017 and March 31, 2019. During this period the tax rate on any such gains will not exceed 50% of the domestic tax rate in India, subject to a 'limitation of benefits' provision proposed to be introduced to the Mauritius DTAA. While capital gains arising out of sale/transfer of shares of an Indian company that have been acquired before April 1, 2017 will not be affected by the protocol, it would appear that convertible instruments (including preference shares and debentures) acquired by a Mauritius resident prior to April 1, 2017 may need to be converted into equity/ordinary shares before April 1, 2017 in order to avail of the capital gains tax exemptions under the Protocol. However clarification on this is still awaited.*
- *Similar amendments have been proposed in Indo-Singapore DTAA as the position on capital gains under the India-Singapore DTAA is co-*

	terminus with the benefits available under erstwhile provisions on capital gains contained in the treaty with Mauritius.
Bilateral Investment Treaties ("BITs")	➢ *Bilateral Investment Treaties proffer better access to treaty benefits through corporate restructuring via intermediate jurisdictions. In view of evading the intricate tax regime of India, Investment is usually brought into India through a holding company from a tax friendly Jurisdiction. India has lucrative BITs with almost all tax efficient jurisdictions including, Mauritius, Netherlands, Switzerland, Cyprus, Singapore etc.*
Indirect Transfer of Shares	➢ *The principle relating to taxability of offshore transfer of shares in India where the underlying assets are situated in India was laid down by the Supreme Court in "Vodafone International Holdings B.V. v/s Union of India & Anr"[2]. Pursuant of the Vodafone Ruling, the Finance Act, 2012 inserted certain clarificatory amendments in the provisions of section 9 of the IT Act, inter alia including an asset or capital asset, being any share or interest in a company or entity registered or incorporated outside India deriving, directly or indirectly, its value substantially from the assets located in India within the tax net.* ➢ *Budget 2015 further clarified that the share or interest would be deemed to derive its value substantially from the assets located in India, if on the specified date, the value of such assets represents at least 50% of the fair market value of all the assets owned by the company or entity. Further, the provision would be applicable on the assets of value more than Rs 10 crore.* ➢ *Income derived from the transfer of P-notes and ODIs deriving their value from the underlying Indian securities is not considered to be income derived from the indirect transfer of shares in India, as the same does not constitute an 'interest' in the Indian securities.*
GAAR	➢ *India first proposed to introduce General Anti Avoidance Rules in 2012, granting discretion to the tax authorities to scrutinize arrangements and invalidate them as impermissible where they lack commercial substance and have been entered into primarily for claiming "Treaty Benefits".* ➢ *GAAR provisions would extend to all taxpayers irrespective of their residential or legal status (i.e. resident or non-resident, corporate entity or non-corporate entity) and would override DTAA's signed by India.* ➢ *The applicability of GAAR is subject to a minimum threshold of INR 3 Crore. However, Foreign Institutional Investors who are not claiming treaty benefits have been exonerated from the ambit of GAAR.*

[2] SLP (C) No. 26529 of 2010, Judgment dated 20 January, 2012.

	Further, GAAR would not be applicable to any investment made by a non-resident that directly or indirectly invests in ODIs. ➢ *The Finance Minister in Budget 2015, has deferred the implementation of GAAR by 2 years, with its prospective applicability from 1st April, 2017.*
Permanent Establishments	➢ *A permanent establishment ("**PE**") under the IT Act includes a fixed place of business through which the business of the enterprise is wholly or partly carried on. In general, the profits of the non-resident entity are taxable in India only to the extent of the profits arising out of activities carried out through its PE in India.* ➢ *Conventionally, India has applied the concept of Place of Effective Management ("**POEM**"), for deciding the threshold of taxing an offshore enterprise. Under the extant laws, POEM has been defined to mean a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance made.* ➢ *Pursuant to Budget 2015, the ambit of foreign company's income being taxed in India has been substantially widened with the change in definition of residential status for offshore companies. Accordingly, foreign companies having effective control and management in India at any time of the year would be liable to tax in India as opposed to having such control and management in India wholly.* ➢ *Further simplifying the tax regime, an India based fund manager or investment advisor is not to be treated as a PE where the offshore fund is broad-based and over 95% investors are non-residents.* ➢ *While this proposal can definitely boost India's fund management industry, it appears that the relief can effectively only be availed by FPIs or hedge funds and may end up excluding private equity or venture capital funds.*

6. How we can assist

Consistent with our reputation as leading Private Equity Attorneys, we provide seamless advice to both domestic and international clients on full breadth of complex, high-value as well as comparatively smaller transactions.

Our team at ARA Law is well versed with all legal aspects associated with both private equity transactions and provides a one-stop solution to its clientele through every leg of the investment process to accelerate the closing of private equity transactions. We advice institutional and private equity investors on a wide range of legal and

regulatory matters that include:

- ***Deal Structures:*** Advising and assisting in deal structuring keeping in mind the client's business objectives and achieving the best possible structure in compliance with domestic and international tax statutes and treaties and relevant exchange control regulations.

- ***Regulatory Approvals, Liaison and Networking:*** Advising and assistance in drafting, filing and coordinating towards procurement of relevant approvals from governmental and statutory authorities, reporting and ongoing monitoring issues and governance in light of the complex regulatory environment under applicable RBI regulations, FDI regulations and SEBI regulations;

- ***Due Diligence:*** Conducting of in-depth legal due diligence with sector focused approach, combining our industry expertise with our private equity transactional capabilities to provide practical solutions to the clients. We also advice on conducting legal audit of portfolio companies and compliances of the existing investment transactional.

- ***Other Aspects of a deal:*** Assisting in review, drafting and execution of the definitive transaction documents; negotiating the transaction documents; closing mechanics of transactions; efficient deal execution and post closing compliances.

- ***Exit:*** Advising and assisting private equity funds and other investors in exiting their investments, whether by way of IPOs, recapitalizations, trade sale, secondary buyout, etc.