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By

**SBS and Company LLP**
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## CONTENTS

INTERNATIONAL TAXATION

## CBCR IMPLEMENTATION GUIDANCE

Contributed by CA Suresh Babu S

**Country By Country Reporting – Implementation Guidance:**

Currently, CBCR compliances has become a matter of concern for all multinational enterprises (MNE). The Organization for Economic Cooperation and Development (OECD) as part of the BEPS project has been issuing guidance to the action points specified by it. Recently on 6 April 2017, the OECD released an updated version of the Guidance on the Implementation of Country-by-Country Reporting ('the Guidance') which has addressed five new issues:

- The definition of terms "related party revenues" & "revenue" used in the CbCR;
- The definition of total consolidated group revenue;
- The accounting principles for determining the existence of and membership in a group;
- Treatment of major shareholding; and
- Transitional filing options for MNE groups.

### 1. Definition of related party and revenues

The Guidance clarifies that the revenue referred to in Table 1 of CbCR shall include extraordinary income and gains from investment activities. While this may not necessarily reflect just the operating results of the constituent entities, it would at least do away with the ambiguity on what constitutes 'extraordinary income' and varying yardsticks that MNE groups would apply.

The Guidance further mentions that "related parties" in Table 1 of CbCR, which are defined as "Associated Enterprises" in the Action 13 report should be interpreted as 'Constituent Entities' listed in Table 2 of the CbCR. In the Indian context, this is defined in section 286 of the Income Tax Act 1961 ('the Act') largely aligned to the OECD definition in the Action 13 report which includes permanent establishments and does not give any leeway in terms of materiality of a company in terms of the group size.

### 2. Definition of the total consolidated group revenue

The Guidance clarifies that for determining the total consolidated group revenue (to see if the threshold of EUR 750 million is breached by a MNE group), all of the revenue reflected in the consolidated financial statements should be used. Further, in line with the definition of revenues for Table 1, the Guidance also provides that the jurisdictions are allowed to require inclusion of extraordinary income and gains from investment activities in the total consolidated group revenue if such inclusion is called for under the applicable accounting rules.

The applicable accounting standard therefore could either push companies into the realms of CbCR or save it from having to comply with CbCR filing.

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The applicable accounting standard therefore could either push companies into the realms of CbCR or save it from having to comply with CbCR filing.

The Guidance also specifically recognizes that in the case of financial entities, gross amounts from transactions may not be recorded in their financial statements, the item(s) considered similar to revenue under the applicable rules should be used in the context of financial activities. The Guidance captures a specific example of interest rate swap wherein revenue is reported on a net basis and the same is what would be used to determine the total consolidated group revenue.

**3. Accounting principles/ standards for determining the existence of and membership of group**

For the purpose of determining the constituent entities of a group, the Guidance recommends companies having their shares listed in a public stock exchange to follow the consolidation rules in the accounting standards already used by the group. For other companies, the OECD has provided an option to either use local GAAP of the jurisdiction of the ultimate parent entity or IFRS unless the jurisdiction of the ultimate parent entity mandates the use of a particular accounting standard.

The choice of a particular accounting standard becomes important in terms of the following;

- Which entity/ group would an entity be considered as part of for determining the group revenue.
- Whether an investment fund company would be required to consolidate its financial statements.

**4. Treatment of major shareholding**

The Guidance leaves it to the prevailing accounting standard to determine how much of the revenue of the entity is to be included in the groups consolidated financials where minority interest exists. A pro-rata basis or 100 % of the entities revenues could be used for the revenue threshold reporting revenues in the relevant Tables.

**5. Transitional filing options for MNE**s

OECD recommends that countries implement CbCR for periods commencing January 2016 for which the last day of filing the CbCR is 12 months from the end of the fiscal year ('Applicable Deadline'). For countries that are not aligned with these dates, transitional issue arises. To overcome this, jurisdictions may accommodate voluntary filing of CbCR in their jurisdiction of tax residence ('parent surrogate filing'). The Guidance also lists out countries which have already enabled the parent surrogate filing for fiscal periods commencing on or after 1 January 2016 in their jurisdictions which inter alia include countries such as China, United States of America ('US') and Japan.

The Guidance also provides that, inter alia, where the CbCR filing has been undertaken by the ultimate parent entity ('UPE') or surrogate parent entity ('SPE') resident in a particular jurisdiction before the Applicable Deadline, and there exists a qualifying competent authority agreement between UPE/ SPE tax jurisdiction and that of the constituent entities' tax jurisdiction, then there ought to be no filing obligations in the constituent entities' jurisdiction.

An issue that Indian MNE Groups may have to immediately grapple with is what happens with respect to constituent entities resident of tax jurisdictions which are yet to sign the MCAA but have CbCR filing obligations which fall before the Indian filing deadline of 30 November 2017 (one such example could be China).

**Updated -UN TP Manual:**

On 7 April, 2017, United Nations (UN) has published updated TP Manual that contains new chapters on intra-group services, cost contribution arrangements and on the treatment of intangibles; the updated UN TP manual incorporates developments relating to Base Erosion and Profit Shifting (BEPS) project including revised guidance on documentation and business restructuring. The updated version has been divided into 4 parts for better clarity –

A) Transfer pricing in a global environment,
B) Substantive guidance on arm's length principle,
C) Practical implementation of TP regime and
D) Country practices;

The following are the new chapters that are incorporated as part of the updated UN TP Manual:

**Intra-group services**

The chapter is based on the rationale that if specific group members do not need the activity and would not be willing to pay for it if they were independent, the activity cannot justify a payment, and further, any incidental benefit gained solely by being a member of an MNE group, without any specific services provided or performed, should be ignored.

The concept of benefit test is explained under various situation such as services are provided to meet specific need of AE and when centralized services are provided along with examples. The Chapter states the 4 situations where charge is not justified as benefit test is not met viz. shareholder activities, duplication of services, benefit arising only out of passive association with MNE group and incidental benefit giving appropriate examples.

The chapter also elaborates upon various method to determine arm's length price, direct and indirect charge mechanism and allocation keys. The Chapter provides for 2 safe harbour mechanisms for low value services and minor intra-group expenses.

**Cost contribution arrangements**

The Chapter covers issues such as value of CCA contributions, treatment of government subsidies, predicting expected benefits, CCA entry, withdrawal and termination and CCA guidelines and

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FEMA

## OVERVIEW OF IFSC - FEMA AND SEBI REGULATIONS

Contributed by CA Murali Krishna G

The last decade has seen unprecedented growth in India's financial services sector. It employs over 3 million people, constitutes about 5% of the GDP and has an estimated market capitalization of over US$ 200 billion. As India experiences continued economic growth, the financial sector could generate about 10-11 million jobs and a GDP contribution of US$ 350 to US$ 400 billion by 2020[1] . With a sustained growth and rapid development in technology and infrastructure, an increasing share of financial services would get centralized. McKinsey & Company's market assessment report estimates potential of about 6 million centralized jobs across multiple service roles.

Several developed countries have successfully established high-tech financial hubs, which over time have catered as international financial services centers. These centers provide suitable regulatory regimes and create a business environment to promote talent and increase capital flow. As they develop they create significant economic value for their respective domestic economies, e.g. financial services in London and New York account for 10% of the GDP and about 5% of jobs. Emerging financial services centers like Singapore and Hong Kong have achieved similar levels of concentration of economic activity over short periods of time.

With the above background the author has made an attempt to analyze the present status of IFSC Regulations and how India is positioned itself to capture the Global opportunities.

### What is IFSC?

An international financial services centreprimarily caters to customers outside the jurisdiction of domestic economy, dealing with flows of finance, financial products and services across borders

Section 2(q) of Special Economic Zones Act, 2005 has defined "International Financial Services Centre" means an International Financial Services Centre which has been approved by the Central Government under sub-section (1) of section 18

The provisions of Section 18 of the SEZ Act, 2005 is been reproduced for ready reference

**Setting up of International Financial Services Centre**

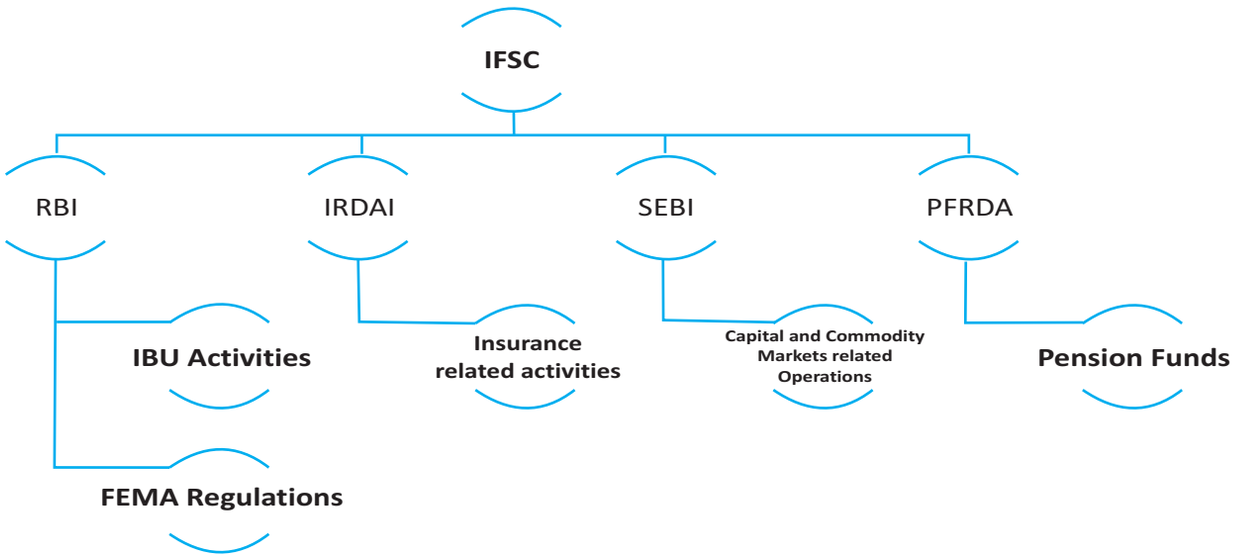
*18. (1) The Central Government may approve the setting up of an International Financial Services Centre in a Special Economic Zone and prescribe the requirements for setting up and operation of such Centre :*

***Provided** that the Central Government shall approve only one International Financial Services Centre in a Special Economic Zone.*

*(2) The Central Government may, subject to such guidelines as may be framed by the Reserve Bank, the Securities and Exchange Board of India, the Insurance Regulatory and Development Authority and such other concerned authorities, as it deems fit, prescribe the requirements for setting up and the terms and conditions of the operation of units in an International Financial Services Centre.*

[1]Source: http://giftgujarat.in/genesis

## Present Regulatory Architecture




It can be observed from the above diagram that the IFSC related activities are governed by several Regulators based on the nature of activities being undertaken.

Reserve Bank of India **(RBI)** regulates the IFSC Banking Units (IBU) as a Banking Regulator and also regulates the Foreign Exchange control Regulations.

Insurance Regulatory and Development Authority of India **(IRDAI)** regulates the activities of Insurance companies in IFSC

Securities and Exchange Board of India **(SEBI)** regulates the operations of intermediaries dealing in Securities and Commodities and their derivatives

Pension Fund Regulatory and Development Authority **(PFRDA)** regulates the operations of entities dealing in such funds and having operations in IFSC

Subsequent to the below regulatory developments India has set up first IFSC in Gujarat International Finance Tec-City Company Limited (GIFT City), Gandhi Nagar, Gujarat, India. For more details of GIFT city, the reader may refer to the website http://giftgujarat.in

## What are the services an IFSC can provide?

- Fund-raising services for individuals, corporations and governments
- Asset management and global portfolio diversification undertaken by pension funds, insurance companies and mutual funds
- Wealth management
- Global tax management and cross-border tax liability optimization, which provides a business opportunity for financial intermediaries, accountants and law firms.
- Global and regional corporate treasury management operations that involve fund-raising, liquidity investment and management and asset-liability matching

- Risk management operations such as insurance and reinsurance
- Merger and acquisition activities among trans-national corporations

**What does an IFSC require?**

IFSCs such as Dubai International Financial Centre and Shanghai International Financial Centre, which are located within SEZs, have six key building blocks:

- Rational legal regulatory framework
- Sustainable local economy
- Stable political environment
- Developed infrastructure
- Strategic location
- Good quality of life

Keeping the above issue in sight, the Indian Government has made many changes and is making efforts to create sustainable and conducive environment to attract the global players to India.

**Brief of Regulatory Developments in India**

| | |
|---|---|
| 01-03-2015 | Press Release issued by PIB for setting up first IFSC in Gandhi Nagar, Gujarat |
| 02-03-2015 | RBI has issued FEMA (IFSC) Regulations, 2015 |
| 27-03-2015 | SEBI has issued SEBI (IFSC) Guidelines, 2015 |
| 27-03-2015 | Ministry of Finance (Department of Financial Services) has issued notification for giving many relaxations to the Insurance Companies from various provisions of Insurance Act, 1938 |
| 27-03-2015 | Ministry of Finance (Department of Financial Services) has issued notification IRDAI (Regulation of Insurance Business in Special Economic Zone) Rules, 2015 for permitting insurance companies to set up operations in IFSC |
| 01-04-2015 | RBI has framed schemeto all Scheduled Commercial banks (including foreign banks)for setting up IFSC Banking Units (IBU) |
| 06-04-2015 | IRDAI has issued guidelines titled IRDAI (IFSC) Guidelines, 2015 |
| 08-04-2015 | Ministry of Commerce and Industry has issued notification permitting setting up of IFSC under SEZ Act, 2005 and rules made thereunder and also notified suitable application form for setting up such IFSC units |
| 17-03-2016 | SEBI has amended the guidelines to include the Commodity Derivatives for IFSC operations |
| 28-11-2016 | SEBI has issued guidelines to Stock Exchanges and Clearing Corporation to set up their operations in IFSC |
| 10-04-2017 | RBI has issued Directions to the IBUs to carry on the clearing operations in IFSC without forming separate entity and also permitted to open SNRRA for local expenses |
| 13-04-2017 | SEBI has further amended the guidelines to include the Derivatives on Equity Shares for IFSC operations |
| 27-04-2017 | SEBI has further amended the guidelines to permit IBUs to carry on TCM and PCM activities for Stock exchanges/ Clearing Corporation in IFSC as well as domestic activities |

**FEMA Regulations:**

RBI,inter alia, has framed around 27 Regulations under FEMA, concerning various activities between Residents in India and Non Residents.

Foreign Exchange Management (International Financial Service Centre) Regulations, 2015 ("FEMA Regulations") deals with the permissible transactions in IFSC as per Foreign Exchange Management Act, 1999

As per Regulation 3 of FEMA Regulations, any financial institution or branch of a financial institution set up in the IFSC and permitted/recognized as such by the Government of India or a Regulatory Authority shall be treated as a person resident outside India and accordingly any transaction taken place between such IFSC entity and Residents in India needs to comply with other regulations framed under FEMA, 1999

As per Regulation 4 of FEMA Regulations, a financial institution or branch of a financial institution shall conduct such business in such foreign currency and with such persons, whether resident or otherwise, as the concerned Regulatory Authority may determine

As per Regulation 5 of FEMA Regulations read with Section 1(3) of FEMA, 1999 all other regulations framed under FEMA are not applicable to the IFSC in case the activities are carried with in the IFSC and subject to these FEMA Regulations.

Commercial banks are allowed to open IBUs within IFSC, which are deemed as overseas branches. Such IBUs can trade in foreign currencies in overseas markets and also with Indian banks, raise funds in foreign currency as deposits and borrowings from non-resident sources and provide loans and liability products for clients.

**SEBI Regulations**

As per SEBI (IFSC) Guidelines, 2015 any intermediary located in IFSC viz., a stock broker, a merchant banker, a banker to an issue, a trustee of trust deed, a registrars to an issue, a share transfer agent, an underwriter, an investment adviser, a portfolio manager, a depositary participant, a custodian of securities, a foreign portfolio investor, a credit rating agency, or any other intermediary or any person associated with the securities market, as may be specified by the Board from time to time, can deal in securities, commodities and their derivatives in a Foreign Jurisdiction [as defined in clause 2(f)]

All the entities willing to set up operations in IFSC shall be first registered with SEBI as an intermediary as per respective regulations framed by SEBI and shall comply with all the applicable regulations including IFSC regulations.

In case of Stock Exchanges, Clearing Corporations and Depositories, willing to carry on IFSC activities shall form separate Subsidiary Companies (holding at least 51% of paid-up Equity 'share capital) and the balance shares can be held by any other stock exchange, clearing corporation or Depository, (whether Indian or foreign jurisdiction),as the case may be.

The stock exchange shall have minimum networth of Rs. 25 Crores initially and shall enhance it to Rs. 100 Crores over a period of 3 years from the date of approval. Similarly Clearing Corporation shall have initial networth of Rs. 50 Crores and to be enhanced to Rs. 300 Crores, over a period of 3 years. Also the Depository shall have initial networth of Rs. 25 Crores and shall enhance it to Rs. 100 Crores over a period of 3 years.

Many provisions of SEBI related to depositories, stock exchanges, clearing corporations operating in IFSC are not applicable as per exemptions given under Rule 6 of SEBI Guidelines

Pursuant to the IFSC Guidelines, depositories, stock exchanges, clearing corporations operating in IFSC shall adopt the broader principles of governance prescribed by International Organization of Securities Commissions (IOSCO) and principles for Financial Market Infrastructures (FMI) and such other governance norms as may be specified by the SEBI, from time to time

As per clause7, the stock exchanges operating in IFSC are permitted to deal in following types of securities and products in such securities in any currency other than Indian rupee, with a specified trading lot size on their trading platform subject to prior approval of the SEBI:

(i) Equity shares of a company incorporated outside India;
(ii) Depository receipt(s);
(iii) Debt securities issued by eligible issuers;
(iv) Currency and interest rate derivatives;
(v) Index based derivatives;
(vi) Such other securities as may be specified by the Board.

SEBI has prescribed Commodity Derivatives as “other securities” under the aforesaid clause. Also SEBI has prescribed Derivatives on equity shares of a company incorporated in India, by Foreign Portfolio Investors as “other securities” under the aforesaid clause

Further, it also provides that SEBI registered Foreign Portfolio Investors (FPIs), operating in IFSC, and eligible entities, which are incorporated and operating in IFSC, shall be eligible to trade in such derivatives on equity shares.

Market Wide Position Limit (MWPL) for such derivatives on equity shares shall be as prescribed by SEBI from time to time.

Earlier this year, the SEBI simplified the IFSC onboarding process for FPIs and eligible foreign investors as under:

- No additional documentation and/or prior approval required for SEBI registered FPIs
- A trading member may rely on the due diligence already carried out by :
  -a SEBI registered intermediary for FPIs
  - a bank operating in IFSC for eligible foreign investors

As per latest amendment dated 27-04-2017, SEBI has permitted IBUs to carry on the operations both in Domestic market and Foreign Jurisdiction as Single entity, thereby paving way for more IBUs to enter into the IFSC operations. Also the IBUs are permitted to open Special Non-Resident Rupee Account in India to meet the administrative expenses in INR

**Conclusion:**

While many reforms in the area of IFSC have been brought by India, there are certain things still to be done. Some of these issues have been addressed in speech titled "Macro and Micro Drivers of Business Potential of IFSCs in India", by Dr. Urjit R. Patel, Governor of RBI – January 11, 2017[2] – at Gandhinagar, Gujarat, regarding other steps to be taken, inter alia, micro ecosystem in IFSC, a modern complementary legal infrastructure that is sufficiently supportive of the swift resolution of conflicts and disputes arising from the settlement/enforcement of complex international financial contracts. The contract should be of international standard and enforceable in the court of law and preferably similar to ISDA documentation

In addition he has opined to have a unified financial regulatory framework providing for a single regulator for IFSC could contribute to better regulation and supervision of the financial entities in the IFSC. While individual regulators can supervise the entities initially when the size of the business is small, a unified regulator would be necessary to pay undivided attention to the IFSC. Work on the design of such a framework should begin soon so as to be able to implement this in time.

Once India implements many of the above reforms and pave the way for effective economic and regulatory reforms, India is poised to play key role in the global economic activity and also provide lot of support for the Economic Development in India and employment generation to the tune of 1 Million [3] Jobs in India.

[2]Source: https://www.rbi.org.in/Scripts/BS_SpeechesView.aspx?Id=1031

[3]Source: presentations available at http://giftgujarat.in/download.aspx

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DIRECT TAX

## SERVICES OF NON-RESIDENT AGENTS- IMPLICATIONS UNDER DIRECT TAX

Contributed by CA Ramprasad T

**Scheme of Taxation of Non-Residents:**

Section 5 of the Income Tax Act, 1961 provides for taxability of income in the hands of Non-Resident. Total Income of the Non-Resident includes all the income ***which is received or deemed to be received in India by or on behalf of such person or income accrues or arises or is deemed to accrue or arise in India to the Non-Resident.***

Section 7 ibid provides for when income is deemed to be received in India. Section 9 ibid provides for when the income is deemed to accrue or arise in India. Section 9(1)(i) ibid provides that all income accruing or arising, whether directly or indirectly, through or from any business connection in India is deemed to accrue or arise in India.

**Concept of Agency and its relevance to Business Connection:**

As per Explanation 2 to section 9(1)(i) ibid 'business connection' shall include:

- any business activity carried out through a person who, acting on behalf of the non-resident has habitually exercise in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident or
- has no such authority, but habitually maintain in India stock of goods or merchandise from which he regularly delivers goods on behalf of the non-resident or
- habitually secure orders in India, mainly or wholly for the non-resident or for the non-resident and other non-residents …….

*business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an* ***independent status,*** *if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business (first proviso)*

To establish the business connection toit is not necessary that all the operations of the business are to be carried in India to constitute business connection. As per Explanation 1 to section 9(1)(i) provides in case where all the operations of the business are not carried out in India the income of the business is deemed to accrue or arise in India to the extent it reasonably attributable to the operations carried out in India.

Combined reading of Explanation 1 and Explanation 2 there exists a business connection through agents, other that of independent status, who undertake activities on behalf of non-resident (Agency PE-Permanent Establishment).

In nutshell, if the activities of agent (dependent) in India contributes to the income of the non-resident, such income is deemed to accrue or arise in India and chargeable to tax accordingly.

The deciding factor in agency is the extent of dependency in carrying on activities in India or on behalf of non-resident in India for determining the chargeability of income in India.

In this context, we analyse two Judicial pronouncements to arrive at a reasonable conclusion on agency transactions of non-residents.

**Galileo International Inc vs DCIT 19 SOT 257- ITAT DELHI**

**Facts:**

Galileo International was a tax resident of USA. It was engaged in the business of maintaining and operating a Computerized Reservation System (CRS). The said system would receive, process, store and disseminate data about flight schedules, room availability, fare information and provision for booking capabilities, etc. The assessee entered into a Participating Carrier Agreement (PCA) with various participating airlines for providing them with said CRS services.

To market and distribute the CRS services to the travel agents (TAs) in India, Galileo International (assessee) entered into a Distribution Agreement (DA) with an Indian company. The Indian company in turn entered in to a subscriber's agreement with various TA to provide them with the access code, equipment, communication link and support services.

The communication between the master computer system of the assessee in USA and TA in India arranged by another organization. The assessee paid remuneration to Indian company for acting as a distributor and to the other company which provided the communication channel.

The assessee was remunerated outside India by the airlines and it did not receive any remuneration from the travel agents.

The assessee filed its return declaring nil income on the ground that it had no operations in India and hence no income is accrue or arise in India.

**Department's contention:**

All the activities in respect of bookings made by the TAs in India were completed in India through the hardware installed by assessee at travel agent's premises; that on that basis income accrued or arose in India under section 5 of Income Tax Act, 1961.

Even under the DTAA, the assessee had a PE in India under article 5 and so the income was taxable as business income under article 7; that the assessee earned income on each segment booked through the computers installed in India and, therefore, the same constituted a PE.

The Assessing Officer further held that 'Indian Company' was a PE of the assessee within the meaning of article 5(4) because it was ***economically dependent*** on the assessee for its source of business and its activities were devoted wholly and exclusively for the assessee, and further, it entered into and concluded contracts on the assessee's behalf.

On appeal the CIT(A) upheld the impugned findings. Second appeal made before ITAT.

**ITAT Ruling:**

The ITAT held that the Indian Company was totally dependent upon the assessee in respect of services to the CRS subscribers in India.

It further held that *the booking would take place in India on the basis of the presence of such seamless CRS. On the basis of booking made by the TAs in India, the income generated to the assessee. But for the booking, no income accrued to the assessee. The assessee was not to receive the payment only for display of information but the income would accrue only when the booking was completed at the desk of the subscriber's computer. In such a situation, there was a continuous seamless process involved, at least part of which was in India and, hence, there was a business connection in India.*

*The assessee operates the CRS system which was the source of revenue and part of such system existed in India thus there was a business connection established in India and hence the income in respect of the booking which took place from the equipment in India could be deemed to accrue or arise in India and hence taxable in India.*

**Key observation:**

*Since part of the booking function was operated in India which directly contributed to the earning of revenue, the activities carried out by the assessee in India were in no way of 'preparatory or auxiliary' character. Thus, the exception provided in article 5(3) would not apply and the assessee would be deemed to have a PE in India*

**Points to be pondered:**

If an agent works exclusively for a single principal, it would establish that the agent is economically dependent on the principal, though it is not conclusive, which could result in existence of dependent agency or agency PE.

**DCIT vs Elitecore Technologies (P) Ltd 80 taxmann.com 6 – ITAT AHMEDABAD**

**Facts:**

The assessee is engaged in the business of developing software products. It has utilized the services of non-resident agents for marketing of the products and assistance in procuring sales orders abroad. Assessee has not deducted tax at source on commission paid to non-resident agents on the contention that it is not chargeable to tax in India.

The Assessing Officer was not satisfied with genuineness of commission payment on the ground that there was no material to justify the reasonableness of commission payment and evidence pertaining to services rendered by the non-resident agents having nexus with the assessee business was not available. [though there is no agreement with non-resident agents the invoices and purchase order raised by the them are available]

**Assessing Officer Contention:**

In view of the provisions of Section 9(1)(i) of Income Tax Act, 1961, income of the non-resident from though or from any business connection in India or any source in India is deemed to accrue or arise in India, and under section 5(2)(b)ibid income deemed to accrue or arise in India is also taxable in India. Since the right to receive the commission income accrued in India, the income is deemed to accrue or arise in India.

**CIT(A) observations:**

The Supreme Court in CIT vs Toshoku Ltd 125 ITR 525 and CIT vs R.D. Aggarwal and Co 56 ITR 20 held that commission paid to non-residents for securing orders outside India is not taxable in India and hence no tax is required to be withheld on the same. Further, Hon'ble Supreme Court in GE India Technology Center Pvt Ltd 372 ITR 456 held that the provisions of section 195 of Income Tax Act,1961 are not applicable if the payments are not taxable in India. As the payment of foreign commission is not taxable in India, the provisions of section 195ibid are not applicable.

**ITAT observations:**

Relied on the judgement in DCIT vs Welspun Corporation Ltd 77 taxmann.com 165- ITAT Ahd where it was held that *the consideration for which the payment made to the commission agent is obtaining of the orders and not any services per se. The consideration is computed on the basis of business procured. Obviously, if there are no business generated for the principal, the agent gets nothing.*

*The consideration paid to the agent is also based on the business procured and the agency agreements do not provide for any independent, standalone or specific consideration for these services. The services rendered under the agreement cannot, therefore, be considered to be technical services in nature or character.*

*Deeming fiction under section 9(1)(i) read with proviso thereto holds the key, and lays down that only to the extent that which the operations of such a business is carried out in India, the income from such a business is taxable in India. When no operations of the business are carried on in India, there is no taxability of the profits of such a business in India either.*

*The profits of such a business can have taxability in India only to the extent such profits relate to the business operations in India, but then, as are the admitted facts of this case, no part of operations of business were carried out in India. The commission agents employed by the assessee, therefore, did not have any tax liability in India in respect of the commission agency business so carried out.*

**Points to be pondered:**

Generating business or securing orders is an entrepreneurial activity and cannot, by any stretch of logic, be treated as a technical service per se. The point of time when commission agent's right to receive the commission fructifies is irrelevant to decide the scope of Explanation 1 to section 9(1)(I).

**Conclusion:**

Amount paid to non-resident agents who operate independently/ who carries on activity of procuring orders outside India doesn't leads to business connection or rendering of technical services in India.

*This article is contributed by CA Ram Prasad Partner of SBS and Company LLP, Chartered Accountant. The author can be reached at caram@sbsandco.com*

## COMPANIES ACT, 2013

### COMPLIANCES UNDER LLP

Contributed by CS D V K Phanindra

All are aware that a Limited Liability Partnership (LLP) is a body corporate, governed by the Limited Liability Partnership Act, 2008 and rules framed thereunder. An LLP has a distinct legal entity separate from that of its partners, it has perpetual succession and any change in the partners shall not affect the existence, rights or liabilities of the LLP. It is a vehicle enabling the Partnerships to enter in to a Corporate frame work with Limited liability, and giving the partners/members the option and flexibility of devising/structuring the control document i.e., LLP agreement, as mutually agreed by the partner/members.

Similar to Companies registered under the Companies Act, 1956/2013, compliances by a Limited Liability Partnership [LLP] can be classified in to **(a)** continuous compliance i.e., compliance as to maintenance of minimum partners/designated partners, **(b)**event based, i.e., happening of an event such as increase of Contribution, Admission of Partners, Resignation of Partners, Shifting of Registered office address of the LLP etc., and accordingly, the LLP will have to file the returns/forms/information with the Registrar of Companies/LLP, in compliance with the said provisions of the LLP Act and **(c)** Time based compliances i.e., based on time, like filing of Annual Return and Statement of Solvency.

An effort has been made to list out the Continuous compliance, Event based and Time based Compliances:

**Continuous Compliances:**

| Sl. No. | Name of the Section of the Act, along with the relevant rule | Compliance with regard to | Penalty for non-Compliance |
|---|---|---|---|
| 1. | **Chapter –II**<br><br>Section 6 (1) & (2) | The LLP shall have a minimum of **Two (02) Partners.** | If at any time, the number of Partner in a LLP is reduced to less than Two(02), and the LLP carried on the business for more than Six (06) months, with the number so reduced, then the remaining Partner shall be liable personally for the obligations of the LLP incurred during the period |
| 2. | **Chapter – II**<br><br>Section 7(1) | The LLP shall have at least **Two (02) Designated Partners** who are individuals and at least one of them shall be resident in India.<br><br>**Explanation: "Resident in India"** means a person who has stayed in India for a period of not less than 182 days during the immediately preceding one year | For non-compliance of the requirement, the LLP and its every Partner, shall be punishable with fine :<br><br>Not less than **Rs.10,000/-**, but which may extend to **Rs.5,00,000/-. [Sec.10(1)]** |
| 3. | **Chapter – III**<br><br>Section – 21 (1) | Invoices, Official Correspondence and publication of the LLP shall bear:<br><br>The name, address of its registered office and registration number of the LLP, and a Statement that it is registered with Limited Liability; and<br><br>A statement that it is registered with Limited Liability. | For non-compliance of the requirement, the LLP shall be punishable with fine :<br><br>Not less than **Rs.2,000/-**, but which may extend to **Rs.25,000/-. [Sec.21 (2)]** |

| Sl. No. | Name of the Section of the Act, along with the relevant rule | Compliance with regard to | Penalty for non-Compliance |
|---|---|---|---|
| 4. | **Chapter – VII**<br><br>Section 34 r/w Rule No.24 of the LLP Rules, 2009. | Maintenance of Books of accounts on cash basis or accrual basis and according to double entry system of accounting, at the registered office of the LLP.<br><br>**Auditing of Accounts:** Applicable to LLPswhose turnover exceeds Rs.40,00,000/- in any financial year, or whose contribution exceeds Rs.25,00,000/-.<br><br>Else auditing not required. | For non-compliance of the requirement, the, **LLP shall be punishable with fine :**<br><br>Not less than **Rs.25,000/-,** which may extend to **Rs.5,00,000/- [Sec.34(5)].**<br><br>**Every Designated Partner shall be punishable with fine:**<br><br>Not less than **Rs.10,000/-** which may extend to **Rs.1,00,000/-[Sec.34(5)].** |

**Time Based Compliance:**

| Sl. No. | Name of the Section of the Act, along with the relevant rule | Compliance with regard to | Compliance with in | Form and attachments | Penalty for non-Compliance |
|---|---|---|---|---|---|
| 1. | **Chapter – VII**<br><br>Section 34 r/w Rule No.24 of the LLP Rules, 2009. | Preparation of Statement of Account and Solvency for the FY, within a period of **Six (06)** months from the end of the Financial year, and filing with ROC. | **Six (06)** months from the end of the FY i.e., 30th September of every year.<br><br>and<br><br>Filing with Registrar with in 30 days of 6 months i.e., 30th October. | **LLP Form No.8,** along with the Statement of Assets and Liabilities and Income and Expenditure and disclosure under provisions of section 22 of the Micro, Small and Medium Enterprises Development Act, 2006,is to be added as attachment. | For non-compliance of the requirement, the, **LLP shall be punishable with fine :**Not less than **Rs.25,000/-,** which may extend to **Rs.5,00,000/- [Sec.34(5)].**<br><br>**Every Designated Partner shall be punishable with fine:** Not less than **Rs.10,000/-** which may extend to **Rs.1,00,000/- [Sec.34(5)]**.<br>+<br>Additional fee of Rs.100/- for each day of delay in filing the return, after 30 days. |

| Sl. No. | Name of the Section of the Act, along with the relevant rule | Compliance with regard to | Compliance with in | Form and attachments | Penalty for non-Compliance |
|---|---|---|---|---|---|
| 2. | **Chapter – VII**<br><br>Section 35 r/w Rule 25 of the LLP Rules, 2009. | Every LLP shall file Annual Return with the Registrar with Sixty (60) days of closure of its financial year<br><br>The annual return of an LLP having turnover uptoRs. 5 Crores, during the corresponding FY or contribution uptoRs. 50 Lakhs, shall be accompanied with a certificate from a designated partner, other than the signatory to the annual return, to the effect that annual return contains true and correct information.<br><br>In all other cases, the annual return shall be accompanied with a certificate from a Company Secretary in practice to the effect that he has verified the particulars from the books and records of the limited liability partnership and found them to be true and correct. | Within Sixty (60) days of closure of its financial year. i.e., 30th May of every year. | **LLP Form No.11,** mentioning the details as to the Partners, Contribution received from them against their obligation, details of any penalties imposed on the LLP/Partner/ Designated Partners, and details of interests of the Partners/Designated Partners in other entities. | For non-compliance of the requirement, the, **LLP shall be punishable with fine :**Not less than **Rs.25,000/-,** which may extend to **Rs.5,00,000/- [Sec.35 (2)].**<br><br>**Every Designated Partner shall be punishable with fine:** Not less than **Rs.10,000/-** which may extend to **Rs.1,00,000/- [Sec.35(2)].**<br>+<br>Additional fee of Rs.100/- for each day of delay in filing the return, after 30 days. |

**Event Based Compliance:**

| Sl. No. | Name of the Section of the Act, along with the relevant rule | Compliance with regard to | Compliance with in | Form and attachments | Penalty for non-Compliance |
|---|---|---|---|---|---|
| 1. | **Chapter – II**<br><br>Section 7(4) and (5) r/wrule 8, 10(8), 22(2) and 22(3) of LLP Rules, 2009 | 7(4) - Notice of appointment, cessation, change in name/ address/ designation of a designated partner or partner. and consent to become a partner/designated partner Notice of appointment, cessation, change in name/ address/ designation. | Within **30 days** from the appointment/ cessation/ Change | **LLP Form No.4**, along with the relevant consent letter/resignation letter, as the case may be. | For non-compliance of the requirement, the LLP and its every Partner, shall be punishable with fine :<br><br>Not less than **Rs.10,000/-,** which may extend to **Rs.1,00,000/- [Sec.10(2)].**<br>+<br>Additional fee of Rs.100/- for each day of delay in filing the return, after 30 days. |
| 2. | **Chapter – III**<br><br>Section 9 | Appointment of Designated partner within 30 days of vacancy. | Within **30 days** from the appointment | **LLP Form No.4,** along with the relevant consent letter/ resignation letter, as the case may be. | For non-compliance of the requirement, the LLP and its every Partner, shall be punishable with fine :<br><br>**Not less than** Rs.10,000/-, which may extend to R**s.1,00,000/- [Sec.10(2)].**<br>+<br>Additional fee of Rs.100/- for each day of delay in filing the return, after 30 days. |

| Sl. No. | Name of the Section of the Act, along with the relevant rule | Compliance with regard to | Compliance with in | Form and attachments | Penalty for non-Compliance |
|---|---|---|---|---|---|
| 3. | **Chapter – III**<br><br>Section 13 (3) r/w with Rule 17 of the LLP Rules, 2009 | Shifting of Registered office of the LLP, and filing of the notice of such change with the Registrar. The change shall take effect only upon such filing | Within **30 days** from the change | **LLP Form 15**, along with the proof of office, Extract of the Resolution + Supplemental Agreement, if the change is requires Suppl. Agreement. | For non-compliance of the requirement, the LLP and its every Partner, shall be punishable with fine :<br><br>Not less than **Rs.2,000/-**, which may extend to **Rs.25,000/- [Sec.13(4)].**<br>**+**<br>Additional fee of Rs.100/- for each day of delay in filing the return, after 30 days. |
| 4. | **Chapter – III**<br><br>Section 17 | Direction received by the LLP from the Central Government to change its name, which is in resemblance with any other LLP or Body Corporate, and likely be mistaken for it. | Within **Three (03)** months from the date of receipt of the Direction | **LLP Form No.1 and LLP Form No.5,** along with the relevant documents | For non-compliance of the requirement, the, **LLP shall be punishable with fine :**<br><br>Not less than **Rs.10,000/-,** which may extend to **Rs.5,00,000/- [Sec.17(2)].**<br><br>**Every Designated Partner shall be punishable with fine:**<br><br>Not less than **Rs.10,000/-** which may extend to **Rs.1,00,000/- [Sec.17(2)].** |

| Sl. No. | Name of the Section of the Act, along with the relevant rule | Compliance with regard to | Compliance with in | Form and attachments | Penalty for non-Compliance |
|---|---|---|---|---|---|
| 5. | **Chapter – IV**<br><br>Section 23 (2), r/w Rule 21 of the LLP Rules, 2009 | Filing of LLP Agreement – In case there is no agreement, then the Mutual Eights and duties of the Partners shall be governed by the First Schedule to the LLP Act.<br><br>Initial as well as Supplemental agreement as to any change in the mutual<br><br>**Note:** LLP Agreement is not a Public document and is not available for inspection. | Within **30 days** from the date of Incorporation (in case of initial LLP Agreement) and also in the case of any change therein. | Form No.3, along with the initial agreement and the Supplemental agreement | Additional fee of Rs.100/- for each day of delay in filing the return, after 30 days. |
| 6. | **Chapter – IV**<br><br>Section 25, r/w Rule 22 of the LLP Rules, 2009 | Intimation of Change in Partners<br><br>As change in Partners requires execution of a Supplemental agreement, the same also needs to be entered into and filed with ROC. | Within **30 days** from the change. | LLP Form No.3 and LLP Form No.4, along with the required documents | For non-compliance of the requirement, the LLP and its every Designated Partner, shall be punishable with fine :<br><br>Not less than **Rs.2,000/-,** which may extend to **Rs.25,000/- [Sec.25(4)].**<br>+Additional fee of Rs.100/- for each day of delay in filing the return, after 30 days, for each form. |

## SECTORAL ANALYSIS

# POWER SECTOR IN INDIA

Contribauted by CA Sandeep Das

### BACKGROUND:

The power sector in India has undergone significant progress after Independence. Energy is one of the key enablers for the country's economic development. With the certainty in policy-level interventions, the economy is bound to proliferate and the demand for energy will inevitably surge. Other than economic growth, human developmental aspects like poverty reduction, employment generation, etc. are also considerably dependent on secure energy supply.

Post India's Independence the country had a power generating capacity of 1,362 MW. Hydro power and coal based thermal power have been the main sources of generating electricity. Generation and distribution of electrical power was carried out primarily by private utility companies. Notable amongst them and still in existence is Calcutta Electric. Power was available only in a few urban centres; rural areas and villages did not have electricity. After 1947, all new power generation, transmission and distribution in the rural sector and the urban centres (which was not served by private utilities) came under the purview of State and Central government agencies. State Electricity Boards (SEBs) were formed in all the states. Nuclear power development is at slower pace, which was introduced, in late sixties. The concept of operating power systems on a regional basis crossing the political boundaries of states was introduced in the early sixties. In spite of the overall development that has taken place, the power supply industry has been under constant pressure to bridge the gap between supply and demand.

### INTRODUCTION:

Power is one of the most critical components of infrastructure crucial for the economic growth and welfare of nations. The existence and development of adequate infrastructure is essential for sustained growth of the Indian economy.

India's power sector is one of the most diversified in the world. Sources of power generation range from conventional sources such as coal, lignite, natural gas, oil, hydro and nuclear power to viable non-conventional sources such as wind, solar, and agricultural and domestic waste. Electricity demand in the country has increased rapidly and is expected to rise further in the years to come. In order to meet the increasing demand for electricity in the country, massive addition to the installed generating capacity is required.

### OBJECTIVES OF THE STUDY

- To study the current scenario of Power Sector in India
- To understand the various challenges and risk in Power Sector
- To suggest solution and remedies to the various problems in Power Sector in India

**Current status of power sector in India**:

*Third largest producer and fourth largest consumer globally:*

With production of 1,278.91 TWh in 2015, India was the 3 rd largest producer & 4 th largest consumer of electricity in the world, with the installed power capacity reaching 305.55 GW by September 2016. The country also has the 5th largest installed capacity in the world.

*Large-scale government initiated expansion plans:*

1. The government targets capacity addition of 88.5 GW under the 12th Five-Year Plan (2012–17) and around 100 GW under the 13th Five-Year Plan (2017–22)
2. Investments of around USD250 billion are planned for the power sector during the 12th Plan Five-Year Plan.

Robust growth in renewables:

1. India energy is estimated to contribute 60 GW, followed by solar power at 100 GW by 2022.
2. The target for renewable energy has been increased to 175 GW by 2022.

***Favourable policy environment:***

100 per cent FDI is allowed under the automatic route in the power segment & renewable energy.

**Policy Initiatives / Decision Taken**

The energy sector in India has seen a transformational change with progressive policy-level changes and effective implementation of directives. These changes promise enormous opportunities for various stakeholders and market players.

The Indian power sector has come a long way since the laying down of the basic framework in 1910 right up to the Electricity Act of 2003, which brought about necessary changes to an evolving sector. Electricity Act 2003 came into force from 15.06.2003. (Electricity Amendment Bill 2014 Under consideration).The proposed amendment will have a profound impact on the Indian power sector. It touches upon different aspects of the sector, right from segregation of carriage and content to renewable energy and open access to tariff rationalisation and so on

**Recent decisions:**

Aiming to empower villages through a hike in MGNREGA funds, poverty alleviation and 100 per cent electrification by May 2018, Finance Minister Arun Jaitley focussed on rural India.

In the Budget speech, Finance Minister said 100 per cent electrification of villages will be achieved by May 1, 2018.

The government has allocated Rs 4,843 crore to electrify the rural areas under the Deendayal Upadhyaya Gram Jyoti Yojana in financial year 2017-18.

The government Five-Year Plans (GW) is targeting capacity addition of around 88.54 GW under the 12th (2012–17) & around 100 GW under the 13th (2017–22) Five-Year Plan The expected investments in the power sector during the 12th Plan (2012–17) is USD250 billion There is a tangible shift in policy focus on the sources of power. The government is keen on promotion of hydro, renewable & gas-based projects, as well as adoption of clean coal technology In March 2017, Bhoruka Power Corp. announced its plans is to raise USD120 million, to increase their hydro & wind renewable energy capacity to 1 gigawatt by 2020

***Government Initiatives***

The Government of India has identified power sector as a key sector of focus so as to promote sustained industrial growth. Some initiatives by the Government of India to boost the Indian power sector:

- The Union Cabinet, Government of India has given its ex-post facto approval for signing of a Memorandum of Understanding (MoU) on Renewable Energy between India and Portugal, which will help strengthen the bilateral cooperation between the two countries.
- The Ministry of New and Renewable Energy plans to introduce a fixed-cost component to the tariff for electricity generated from renewable energy sources like solar or wind, in a bid to promote a green economy.
- The Union Cabinet has approved the ratification of International Solar Alliance's (ISA) framework agreement by India, which will provide India a platform to showcase its solar programmes, and put it in a leadership role in climate and renewable energy issues globally.
- The Government of India plans to introduce a scheme to encourage setting up of biomass plants across the country, which will generate electricity and also help dispose of agricultural waste in a carbon-neutral manner to help tackle growing pollution.
- The Government of India plans to rationalise various categories of electricity consumers across states, which is expected to bring transparency and efficiency in billing, improve tariff collection and improve the health of distribution companies in the country.
- The Government of India plans to set up a US$ 400 million fund, sourced from The World Bank, which would be used to protect renewable energy producers from payment delays by power distribution firms, while at the same time protecting the distribution firms from the shrinking market for conventional grid-connected power, caused by wider adoption of roof-top solar power generation.
- The Ministry of Power plans to set up two funds of US$ 1 billion each, which would give investment support for stressed power assets and renewable energy projects in the country.
- Mr Piyush Goyal, Minister of State with Independent Charge for Power, Coal, New and Renewable Energy and Mines, launched an online portal for star rating of mines, which will bring all mines to adopt sustainable practices, and thereby ensure compliance of environmental protection and social responsibility by the mining sector.
- The Ministry of New and Renewable Energy (MNRE), which provides 30 per cent subsidy to most solar powered items such as solar lamps and solar heating systems, has further extended its subsidy scheme to solar-powered refrigeration units with a view to boost the use of solar-powered cold storages.

- ❖ Mr Piyush Goyal, Minister of State with Independent Charge for Power, Coal, New and Renewable Energy and Mines, inaugurated the Tarang (Transmission App for Real Time Monitoring & Growth) mobile app and web portal for electronic bidding for transmission projects, which is expected to enhance ease, accountability, transparency, and boost investor confidence in power transmission sector.
- ❖ The Ministry of Shipping plans to install 160.64 MW of solar and wind based power systems at all the major ports across the country by 2017, thereby promoting the use of renewable energy sources and giving a fillip to government's Green Port Initiative.
- ❖ The Government of India and the Government of the United Kingdom have signed an agreement to work together in the fields of Solar Energy and Nano Material Research, which is expected to yield high quality and high impact research outputs having industrial relevance, targeted towards addressing societal needs.
- ❖ The Ministry of Petroleum and Natural Gas is seeking to enhance India's crude oil refining capacity through 2040 by setting up a high-level panel, which will work towards aligning India's energy portfolio with changing trends and transition towards cleaner sources of energy generation.
- ❖ The Government of India plans to start as many as 10,000 solar, wind and biomass power projects in next five years, with an average capacity of 50 kilowatt per project, thereby adding 500 megawatt to the total installed capacity.
- ❖ Mr Piyush Goyal, Minister of State (Independent Charge) for Power, Coal and New & Renewable Energy outlined Government of India's goal to provide electricity to every home in India by 2020, while also focussing on ensuring the cost of power is affordable to everyone.
- ❖ Government of India has asked states to prepare action plans with year-wise targets to introduce renewable energy technologies and install solar rooftop panels so that the states complement government's works to achieve 175 GW of renewable power by 2022.
- ? The Government of India announced a massive renewable power production target of 175,000 MW by 2022; this comprises generation of 100,000 MW from solar power, 60,000 MW from wind energy, 10,000 MW from biomass, and 5,000 MW from small hydro power projects.
- ❖ Ujwal DISCOM Assurance Yojana (UDAY) is the financial turnaround and revival package for electricity distribution companies of India (DISCOMs) initiated by the Government of India with the intent to find a permanent solution to the financial mess that the power distribution is in.It allows state governments, which own the discoms, to take over 75 percent of their debt as of September 30, 2015, and pay back lenders by selling bonds. Discoms are expected to issue bonds for the remaining 25 percent of their debt.

**FINANCING CHALLENGES**

**Power financing faces the following major challenges:**

1. Power Sector Exposure Limit: Most banks have already reached their exposure limits in power sector set by them in pursuance of the RBI guidelines. In addition, there is continual asset liability mismatch due to the long term nature of power plant projects. These factors cause tightness in liquidity and borrowing costs. Refinancing of loans or take-out financing may mitigate asset liability mismatch.

2. Lack of Payment Security / SEB Health: Deteriorating financial health of the state utilities makes the lenders uncomfortable in financing state sponsored solar power projects. As a result lenders tend to place power projects in high risk categories and that increases cost of borrowing.

   The decision of the project promoter to go for the combination of equity and debt finance depends upon various factors such as availability of finance, fiscal incentives available and return on equity as also the cost of debt vis-a-vis equity. In case of foreign loan it is generally required that supplier's credit is guaranteed by export credit agencies from the country of export. The export credit agencies, in turn, seek guarantee from Indian lenders (financial Institutions and banks) since foreign banks and credit institutions continue to be unwilling to take the credit risk in view of the weak financial condition of State Electricity Boards.

**THE FINANCING OPTIONS AND RELATED CONSTRAINTS REMAIN AS FOLLOWS:**
**EQUITY/ CAPITAL MARKET INSTRUMENTS:**

The government policy allows a debt equity ratio of 4:1. However, the lending institutions are comfortable with a debt equity ratio closer to 7:3 as a prudent measure for lending. The gap in the equity infusion needs to be filled up. It is imperative that some specialised infrastructure funding agencies and special purpose mutual funds are set up for this purpose to bridge the equity gap in large Power projects.

i. Capital Market : Presently, interest rates are deregulated and credit rating is mandatory if the maturity of instrument exceeds 18 months debentures (convertible/ non-convertible)/bonds can be issued by power companies to augment the resources for power sector in the capital market. NCDs with option of buyback, debentures with equity warrants, floating rate bonds and deep discount bonds are some of the innovative instruments which can be floated in the capital market.

ii. Private placement: Rule 144 A allows for private placement of debt to financial institutions known as QIB, without the kind of stringent disclosure requirements needed for equity issues. Long tenure of bonds and less restrictive covenants make this proposition conducive for financing power projects.

**DEBT FINANCE** :

The capital intensive nature of power projects requires raising debt for longer tenor (more than 15 years) which can be supported by the life of the power project (around 25 years). However, banks face a difficulty in long term lending due to wide disparity between the maturity profiles of assets and liabilities of banks exposing them to Asset Liability Maturity mismatch (ALM).

Accordingly, the longest term of debt available from any bank or financial institution is for 15 years (door-to-door) which creates mismatch in cash flow of the power project and sometimes affect the debt servicing.

Though maturity profiles of funds from insurance sector and pension funds are more suited to long gestation power projects, only a minuscule portion is deployed in power sector. Appropriate fiscal incentives need to be explored to channelize savings. New debt instruments and sources of funds, viz., Infrastructure Debt Fund, Special Energy Funds etc. may be identified for the purpose. Options like re-financing may be explored to make funds available for the power project for a long tenor.

**Syndicated Loans :** Since the fund requirements for power sector are large and the gestation period is much longer , the loan syndication concept needs to be in place for closure of finance requirement. This also helps in sharing of risk among the lenders apart from saving on efforts and cost because appraisal can be done by only the lead institution.

The constraints in syndicated loans are that all lenders are not comfortable with longer period repayment; specific to the requirements of the borrowers to suit their projects. The floating rate of interest is another concern for the project as this brings the element of uncertainty in project financials.

**Foreign Funding :** Cost of Rupee funding is high as compared to foreign currency funding. In a competitive bidding scenario, higher cost of borrowing could adversely affect the profitability and debt servicing of loans. While raising debt for financing power projects, the cost of funds need to be at a low level so that the ultimate cost of electricity will be cheaper for the consumers.

The need to tap international markets becomes inevitable which is characterized by longer tenure of maturities and availability of various modes of finances.

**Multilateral Institutions :** Institutions like World Bank, IFC Washington, ADB, and Commonwealth Development Corporation (CDC) are tapped for financing infrastructure in developing countries. However usually the financing is available with restrictive covenants. The co-financing facility extended by some of the multilateral institutions are also a recourse. However in most of these loans, sovereign guarantee is solicited by the Lenders, which again requires government support.

**Export Credit Agencies (ECA) :** ECAs can be important sources of bilateral funding. ECAs have a long history of providing finance for all types of power generating equipment. However, there are certain limitations in ECA financing like exposure limit, exchange risk transfer, guarantee requirements and cost of insurance etc. The fee for these services are quite expensive (levied on principal and future interest). Apart from interest costs and guarantee fees, other costs of financing are the lenders upfront fee, a fee for amount committed but remained unused, third party assessment and closing fees. In most cases upfront and unused fees are calculated on the committed amount and not on the total drawn amount. Third party costs include legal and consultancy fees.

**External Commercial Borrowing (ECB) :** External Commercial Borrowings (ECBs) for power projects involves issues relating to tenor, hedging costs, exposure to foreign exchange risks etc. Project financing by multilateral agencies (World Bank, Asian Development Bank) has been low due to issues like soundness of power purchase agreements.

While bond offerings are a lower cost option to raise funds visà- vis syndicated loans, corporate bond market for project financing is virtually absent in India. The funds like Global Bonds, Yankee Bonds, Samurai Bonds, Euro Currency loan, UD 144A Private placement, Global Registered Notes (GRNs) can lend for large sized projects. However weak finances of the SEB's remain a critical issue.

The credit rating of the power projects being set up under SPV structure is generally lower than investment criterion of bond investors and there is a need for credit enhancement products. As a result of the credit enhancement, the SPV's rating is expected to improve to AA, making it investment grade which is the minimum acceptable level for pension and insurance funds. With the participation of pension and insurance funds, the twin benefits of longer tenor and stable interest rate could accrue to power projects while the ALM issues of banks could also be resolved.

**RISKS AND MITIGATION MEASURES**

Despite excess demand for electricity, many existing and commissioned thermal power plants are operating well below designed capacity and/or are losing money. The reasons range from risks like excessive financial leverage at a higher than optimum rate of interest, power purchase agreements that are priced too low to leave a profit margin, under-utilisation due to inability to source domestic coal, and unavailability of finance at a low cost.

**Market risk:** The market risk includes demand risk and price risk.

Demand risk can be avoided by the 'take or pay' stipulation of the PPAs, according to which the SEB agrees to pay the power generator the 'Availability rate' regardless of the power purchased. Similarly, the price risk is avoided by the tariff structure in which all costs of producing power – fixed (interest, depreciation, O & M, insurance, taxes) and variable (fuel), plus a return on equity (ROE) are assured.

**Weak finances of SEBs:** State Electricity Boards (SEB) are usually the sole purchasers of the power that a private sector generator generates. That being the case, the private sector runs the risk of not being paid by SEBs (who are in poor financial health). Risk can be mitigated as follows:

i)An escrow account guaranteeing payment on behalf of the SEBs – Cash inflows of the SEB are deposited and to which the generating agency (say an independent power producer) would have first access in case of defaults by the SEB.
ii) An irrevocable letter of credit, favouring the IPP on certain conditions being met and issued by a highly rated bank/financial institution.
iii) An agreement by which the IPP could supply electricity directly to buyers, through the existing lines.
iv) Counter guarantee from the central government. In fact this was sought from the central government and was eventually obtained in the case of six of the eight 'fast-track' projects.

**PPAs:** The risks exposure of the private producers are usually sought to be addressed in the PPAs. But the power purchase agencies( Read SEBs) insist on a one-sided PPA agreement loaded in their favour.

**Fuel-supply risk:** This is the risk of not obtaining timely supply of adequate quantity of fuel. To counter this risk, power generators may either sign long-term contracts with the public sector supplier or acquire a captive source (for example, a captive coal mine).

**GST - Impact on Power Sector**

Power generation companies may see a rise in costs since all inputs are included in GST but electricity is not. Power generation companies can procure goods at a concessional rate of 2 percent, however the rate might go up to 12 percent or 18 percent and the cost might be passed on to the consumer if GST is implemented.

The strong government thrust to promote power sector and ambitious target of achieving 175 GW of renewable energy capacity by 2022 with equal distribution across the country will be directly affected by impact of GST. It is necessary to rationalise the tax treatment under new tax reform for this sector.

Reduced cost of projects will improve financial health of power sector and will encourage for new investment in this sector. Since electricity is one of the major inputs for manufacturing therefore any increase in cost of electricity will directly hit the cost of other products, which will result in overall inflation.

**Power Sector at a Glance ALL INDIA**

**1.Total Installed Capacity:**

| Sector | MW | % of Total |
|---|---|---|
| State Sector | 103,192 | 32.72% |
| Central Sector | 76,852 | 24.36% |
| Private Sector | 135,382 | 42.92% |
| **Total** | **315,426** | |

*Note: Data as on 17-03-2017*

| Fuel | MW | % of Total |
|---|---|---|
| **Total Thermal** | 215,215 | 68.2% |
| Coal | 189,048 | 59.9% |
| Gas | 25,329 | 8.1% |
| Oil | 838 | 0.3% |
| **Hydro** (Renewable) | 44,413 | 14.0% |
| **Nuclear** | 5,780 | 1.8% |
| **RES**** (MNRE) | 50,018 | 15.9% |
| **Total** | **315,426** | |

Renewable Energy Sources(RES) include SHP, BG, BP, U&I and Wind Energy
SHP= Small Hydro Project ,BG= Biomass Gasifier ,BP= Biomass Power,
U & I=Urban & Industrial Waste Power, RES=Renewable Energy Sources

**ELECTRICITY GENERATION PERFORMANCE**

Indian power sector is undergoing a significant change that has redefined the industry outlook. Sustained economic growth continues to drive electricity demand in India. The Government of India's focus on attaining 'Power for all' has accelerated capacity addition in the country. At the same time, the competitive intensity is increasing at both the market and supply sides (fuel, logistics, finances, and manpower).

Total installed capacity of power stations in India stood at 315,426.32 Megawatt (MW) as of February 28, 2017.

The Ministry of Power has set a target of 1,229.4 billion units (BU) of electricity to be generated in the financial year 2017-18, which is 50 BU's higher than the target for 2016-17. The annual growth rate in renewable energy generation has been estimated to be 27 per cent and 18 per cent for conventional energy.

The Government has added 8.5 GW of conventional generation capacity during the April 2016-January 2017 period. Under the 12th Five Year Plan, the Government has added 93.5 GW of power generation capacity, thereby surpassing its target of 88.5 GW during the period.

Programme, actual achievement and growth in electricity generation in the country during 2009-10 to 2016-17 :-

| Year | Energy Generation from Conventional Sources (BU) | % of growth |
|---|---|---|
| 2009-10 | 771.551 | 6.6 |
| 2010-11 | 811.143 | 5.56 |
| 2011-12 | 876.887 | 8.11 |
| 2012-13 | 912.056 | 4.01 |
| 2013-14 | 967.150 | 6.04 |
| 2014-15 | 1048.673 | 8.43 |
| 2015-16 | 1107.822 | 5.64 |
| 2016-17* | 1057.746 | 4.69 |

* Provisional (Upto February, 2017)

The electricity generation target for the year 2016-17 was fixed at 1178 BU comprising of 999.000 BU thermal; 134.000 BU hydro; 40.000 nuclear; and 5.000 BU import from Bhutan.

**Plant Load Factor (PLF): The PLF in the country during 2009-10 to 2016-17 is as under:**

| Year | PLF | Sector-wise PLF (%) | | |
|---|---|---|---|---|
| | % | Central | State | Private |
| 2009-10 | 77.5 | 85.5 | 70.9 | 83.9 |
| 2010-11 | 75.1 | 85.1 | 66.7 | 80.7 |
| 2011-12 | 73.3 | 82.1 | 68.0 | 69.5 |
| 2012-13 | 69.9 | 79.2 | 65.6 | 64.1 |
| 2013-14 | 65.60 | 76.10 | 59.10 | 62.10 |
| 2014-15 | 64.46 | 73.96 | 59.83 | 60.58 |
| 2015-16 | 62.29 | 72.52 | 55.41 | 60.49 |
| 2016-17* | 59.93 | 71.26 | 54.08 | 56.55 |

* Provisional (Upto February, 2017)

**Power Supply Position**

The power supply position in the country during 2009-10 to 2016-17 :

| Year | Energy | | | | Peak | | | |
|---|---|---|---|---|---|---|---|---|
| | Requirement | Availability | Surplus(+)/Deficits(-) | | Peak Demand | Peak Met | Surplus(+) / Deficts(-) | |
| | (MU) | (MU) | (MU) | (%) | (MW) | (MW) | (MW) | (%) |
| 2009-10 | 8,30,594 | 7,46,644 | -83,950 | -10.1 | 1,19,166 | 1,04,009 | -15,157 | -12.7 |
| 2010-11 | 8,61,591 | 7,88,355 | -73,236 | -8.5 | 1,22,287 | 1,10,256 | -12,031 | -9.8 |
| 2011-12 | 9,37,199 | 8,57,886 | -79,313 | -8.5 | 1,30,006 | 1,16,191 | -13,815 | -10.6 |
| 2012-13 | 9,95,557 | 9,08,652 | -86,905 | -8.7 | 1,35,453 | 1,23,294 | -12,159 | -9.0 |
| 2013-14 | 10,02,257 | 9,59,829 | -42,428 | -4.2 | 1,35,918 | 1,29,815 | -6,103 | -4.5 |
| 2014-15 | 10,68,923 | 10,30,785 | -38,138 | -3.6 | 1,48,166 | 1,41,160 | -7,006 | -4.7 |
| 2015-16 | 11,14,408 | 10,90,850 | -23,558 | -2.1 | 1,53,366 | 1,48,463 | -4,903 | -3.2 |
| 2016-17 * | 10,44,326 | 10,37,165 | -7,160 | -0.7 | 1,59,542 | 1,56,934 | -2,608 | -1.6 |

**REMEDIES AND SOLUTIONS**

It is evident that the deficit in power availability in India is a significant impediment to the smooth development of the economy. In this context, bridging the gap in demand and supply has become critical and consequently, large projects are being undertaken in different segments of the sector; Generation, Transmission and Distribution. As India has not witnessed such a large scale of implementation before, there is a need to review and enhance project execution capabilities to help ensure targets are met. The table below summarizes the key implementation challenges and remedies and solutions for successfully achieving the implementation of power generation plans.

| Key Challenges | Measures being adopted | Resulting issues | Solutions and Remedies |
|---|---|---|---|
| Addition of significant generation capacity | UMPP | Technical and financial capability to execute such large projects | Project execution Costs/Cash flow management |
| | | Risks increase manifold | Risk Management strategy and planning |
| Ensuring fuel availability and quality | Purchase and development of coal mines abroad | Risks in operating in different geographies. Eg. - political risks | Risk management through effective contracting, supply diversification, etc. |
| | | Uncertainties in logistics operations | Control over supply infrastructure |
| Plant equipment shortage | Procurement from abroad | Vendor reliability | Robust procurement management, vendor monitoring |
| | Setting up of new supply units | Execution timelines | Project scheduling |
| Land acquisition and environment clearances | Speeding up processes | Inadequate communication with stakeholders resulting in mismatch of expectations from project affected persons | Environment and stakeholder management |
| Manpower shortage | Enhance training | | Resource planning and management |

This strongly necessitates employing a comprehensive project management structure to address the major challenges of the power sector projects and to be able to deliver them as per the planned targets. Historical records also indicate the presence of a weak project management structure which does not assess all the key project aspects leads to various issues and challenges. As discussed initially, the overall intent of this paper is to highlight the opportunities and challenges of the electricity sector, and the project management solutions and remedies that are required to address these challenges.

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## LABOUR LAWS

### MATERNITY BENEFIT ACT

Contributed by S V Ramachadra Rao

The Factories and establishments employing ten or more employees are covered under the Employees' State Insurance Act in the notified areas. The employees working in such factories and establishments with a gross monthly wage of Rs. 21,000/- and below are required to be covered under the ESI Scheme and they are entitled to ( i ) Medical Benefit ( ii ) Sickness Benefit ( iii ) Maternity Benefit ( iv ) Disablement benefit ( v ) Dependents benefit ( vi ) Funeral expenses ( vii ) other benefits

When an employees is covered under ESI Act and is entitled to benefits provided by the said Act, he or she shall not be entitled to receive any similar benefit admissible under the provisions of any other enactment [Section 61].

In view of the above, employees covered under ESI Act are not covered under The Maternity Benefit Act, 1961 and Employee Compensation Act 1923.

The Maternity Benefit Act is applicable to every factory, mine or plantation and to shops and establishments employing ten or more employees. In such factories and establishments, employees who are not covered under ESI Act employed directly or through any agency will only be covered under the Maternity Benefit Act.

To become entitled for maternity benefit, the employee should have worked eighty days in the twelve months immediately preceding the date of her expected delivery in an establishment of the employer.

The amendments to the Maternity Benefit Act have come inforce with effect from 1st April 2017 are summarised hereunder:

1. The Act now mandates that the employer of the establishment should inform a women all benefits made available under the law, at the time of her appointment. Such information must be given in writing and electronically.

2. Every establishment employing fifty or more employees shall provide crèche facilities within a prescribed distance and the woman should be allowed four visits to the crèche in a day. However, this includes her rest interval. However, this provision will come into force with effect from 1st July 2017.

   Whereas, creche is required to be provide and maintained only if a factory employs more than thirty women employees under Section 48 of the Factories Act. In view of the amended maternity benefit act, if the factory is employing fifty or more employees, they are required to provide crèche facility even though the number of women employees are thirty.

3. After completion of the statutory maternity benefit period with wages, an employer can permit a woman to work from home, if the nature of work assigned permits her to do so for a duration that is mutually decided by the employer and the woman employee. Though it is not mandatory, the law made it open to the women employee to make a request in this regard.

4. Now the Maternity Benefit Act provides leave up to twelve weeks for a woman who adopts a child below the age of three months. The period of leave will be calculated from the date the child is handed over to the adoptive mother.

5. In surrogacy, the surrogate mother carries a child for another person after an agreement made before conception of the child. The person wishing to adopt and foster the child is called the commissioning person/couple. The amended legislation provides leave up to 12 weeks for commissioning mothers also.

6. The maximum period for which any woman shall be entitled to maternity benefit shall be twenty six weeks of which not more eight weeks shall precede the date of her expected date of delivery.Provided that the maximum period entitled to maternity benefit by a women having two or more surviving children shall be twelve weeks of which not more than six weeks shall precede the date of her expected delivery.

   Thus women employees having two or more children will continue to get the maternity benefit as earlier.

7. Woman who have already availed 12 weeks of maternity benefit on or before 31st March 2017 will not be entitled to the enhanced benefits mentioned above. However, woman who are on maternity benefit of 12 weeks and the period of 12 weeks ends on or after 1st April 2017 will be entitled to the enhance maternity benefit of twenty six weeks in place of twelve weeks.

It is essential to recognise that the act has not defined 'employee' and extended the benefits to 'woman'.Thus the intent of the legislature is to cover all categories of personnel whether be it casual, temporary, outsourced, contractual, full time consultants, trainees, probationers etc.,

When a woman absents herself from work in accordance with the provisions of the maternity benefit act, the employer is retrained from terminating her services during the said period. Over two decades ago, in 1991, the Supreme Court had ruled in favour of pregnant employees in the matter of Neera Mathur Vs Life Insurance Corporation of India. The facts of the matter are Ms. Mathur was appointed on September 25, 1989. She was put on probation for six months and during the probationary period she applied for maternity leave on December 27, 1989. On February 13, 1990, she was discharged from service during her period of probation. The reason cited for termination was that she had deliberately withheld the fact of being pregnant at the time of filling up a declaration form prior to being appointed. The court ordered her reinstatement. The apex court judgement further reinforces the fact that though the contract of employment provides for termination of employment during the probationary period, the employer will not be in a position to implement the same, if it is in violation of provisions of the applicable laws.

Similarly, in accordance with the Section 73 of the ESI Act employer shall not dismiss, discharge or reduce or otherwise punish an employee during the period when he / she is in receipt of sickness benefit or maternity benefit and also during the period in receipt of disablement benefit for temporary disablement or is under medical treatment for sickness or is absent from work as a result of certified illness arising out of pregnancy or confinement. During the said period no notice of dismissal or discharge or reduction shall be served on an employee.

In view of the amended legislation, the HR professionals are required to have a relook at their HR manual and also the contract of employment to comply with the amended maternity benefit act.

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**TECHNICAL SESSIONS:**

| S.No. | Event | Date | Speaker | Venue |
|---|---|---|---|---|
| 1 | Regulations pertaining to International Financial Service Centre | 05/05/2017 | CA Murali Krishna G | SBS - Hyd |
| 2 | Insolvency and Bankruptcy Code - Perspectives from Companies Act & Bankers | 12/05/2017 | CS Phanindra DVK & CA Rajesh D | SBS - Hyd |
| 3 | Advance Authorisation, Duty Free Import Authorisation | 26/05/2017 | CA Manindar K | SBS - Hyd |
| 4 | Practical Issues related to Taxation in MSME | 02/06/2017 | CA Suresh Babu S | SBS - Hyd |

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***Derivatives vis-a-vis FEMA Regulations - CA Murali Krishna G***

***Session on Companies Amendment Bill, 2013 - CS Phanindra DVK***

***Session on Demonitisation vis-a-vis Auditor's Report - CA MHS Bhyrav***

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