Web-conference by PTC India Financial Services Limited

INNOVATIVE CAPITAL STRUCTURING

Trends & Considerations in Renewable Power Sector in India

By BMR Advisors

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SECTOR ATTRIBUTES – FINANCIAL

ATTRIBUTES

- Upfront capital cost with low operating expense
- Stable revenues in project SPV as per PPA
- Regulations may require de minimus capitalisation/ shareholding
- Relatively higher rate of depreciation available – Results in low tax outgo initially

FUNDING INSTRUMENTS –

- OPTIONS
- KEY CONSIDERATIONS
- INSTRUMENTS

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FUNDING INSTRUMENTS - OPTIONS

- Equity instruments
  - Equity shares
- Quasi – equity instruments
  - Compulsorily convertible debentures (“CCD”)
  - Compulsorily convertible preference shares (“CCPS”)
- Pure debt instruments
  - Non-convertible debentures
  - External Commercial Borrowings
  - Rupee Denominated Bonds

FUNDING INSTRUMENTS – KEY CONSIDERATIONS

- Control over SPV
- Exchange control
- Repatriation of cash
- Tax considerations
- Net worth criteria (Qualification requirements under State / Central Government policy

FUNDING INSTRUMENTS – EQUITY (1/3)

Parameters	Framework
Control over SPV	Equity instruments would give the desired control over the SPV in which investments are being made depending on the commercial objective / arrangement and amount of investments
Exchange control and regulatory requirements	- 100 percent FDI is permitted
Repatriation of Cash	Possible modes of repatriation are – - Regular repatriation in the form of Dividend - Liquidation - Buy back / capital reduction
Net worth Criteria	Equities would be considered while calculating the net worth requirements under the qualification criteria for the bidders bidding for the energy projects under State / Central Government policy
End Uses	Can be used for all the purposes

FUNDING INSTRUMENTS – EQUITY (2/3)

Tax Considerations	Domestic	Jurisdiction - Treaty Benefits
Repatriation by way of Dividend		
Tax in the hands of SPV and shareholders	Dividend Distribution Tax ("DDT") payable by SPV at ~20.48 percent and exempt in the hands of the shareholders	- Whether DTAA benefits could be claimed on such income is debatable and not dispute free - Depending on the jurisdiction, credit for such DDT could be claimed in the residence country

FUNDING INSTRUMENTS – EQUITY (3/3)

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Tax Considerations	Domestic	Jurisdiction - Treaty Benefits
Repatriation by way of Buyback / Capital Reduction / Liquidation		
Tax in the hands of SPV	- Buyback Tax would be deducted on distributed income by SPV at ~23.07 percent - No tax on Liquidation / capital reduction	- Whether DTAA benefits could be claimed on such income is debatable and not dispute free
Tax in the hands of Shareholders	- Income in the hands of equity shareholders is exempt if SPV has deducted tax under buyback - On liquidation / capital reduction, tax at ~20 percent if distributable profit exists else capital gains	Depending on the jurisdiction such as Singapore, Mauritius, benefits under treaty could be claimed on Capital gains
Ceiling on Buyback	25% cap - Subject to conditions specified in the Companies Act, 2013	NA

FUNDING INSTRUMENTS – CCPS (1/3)

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Parameters	Framework
Control over SPV	Quasi instruments would not give the desired control over SPV until instruments are converted into equity
Exchange control and regulatory requirements	- 100 percent FDI is permitted
Repatriation of Cash	Compulsory Convertible instruments similar to Equity. Possible modes of repatriation are – - Regular repatriation in the form of Dividend - Liquidation - Buy back / capital reduction
Net worth Criteria	Quasi Equities may be considered while calculating the net worth requirements under the qualification criteria for the bidders bidding for the energy projects under State / Central Government policy

FUNDING INSTRUMENTS – CCPS (2/3)

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Tax Considerations	Domestic	Jurisdiction - Treaty Benefits
Repatriation by way of Dividend		
Ceiling on Dividend rate	Maximum dividend is 300 basis points over State Bank of India ("SBI") Prime Lending Rate ("PLR")	NA
Other tax considerations same as that of Equity shares		

FUNDING INSTRUMENTS – CCD (1/3)

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Parameters	Framework
Control over SPV	Quasi debt instruments would not give the desired control over SPV until instruments are converted into equity
Exchange control and regulatory requirements	- 100 percent FDI is permitted
Repatriation of Cash	Compulsory Convertible instruments similar to Equity. Possible modes of repatriation are – - Regular repatriation in the form of Interest (pre conversion) - Dividend (post conversion) - Liquidation (post conversion) - Buy back / capital reduction (post conversion)
Net worth Criteria	Quasi instruments may be considered while calculating the net worth requirements under the qualification criteria for the bidders bidding for the energy projects under State / Central Government policy
End Uses	Can be used for all the purposes

FUNDING INSTRUMENTS – CCD (2/3)

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Tax Considerations	Domestic	Jurisdiction - Treaty Benefits
Repatriation by way of Interest / Dividend		
Tax in the hands of SPV	- TDS on interest at the rate of 43.26 percent on gross amount, as per the Act	- Depending on the jurisdiction, benefits under treaty could be claimed on interest
Tax in the hands of Investor	- Interest will be taxable at the rate of 43.26 percent on gross amount, as per the Act	Depending on the jurisdiction, benefits under treaty could be claimed on interest
Ceiling on interest rate	- No maximum rate specified. Reasonable to consider the maximum rate prescribed in respect of preference shares as the maximum rate (SBI PLR plus 300 basis points) - Rate of interest would also be capped in case of loans between associated enterprises - Under transfer pricing regulations	NA

FUNDING INSTRUMENTS – NCD (1/2)

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Parameters	Framework
Control over SPV	Pure Debt Instrument – No equity control
Exchange control and regulatory requirements	- A Foreign portfolio investor ("FPI") may invest in the listed or unlisted NCDs under FPI route in the infrastructure sector
Repatriation of Cash	Possible modes of repatriation are – - Regular repatriation in the form of Interest - Redemption of NCDs
Net worth Criteria	Such instruments may be considered while calculating the net worth requirements under the qualification criteria for the bidders bidding for the energy projects under State / Central Government policy
Recognised investors	FPI
Maturity	Not exceeding 30 years for secured debentures
All-in-Cost	No restriction
End Use	Can be used for all the purposes

FUNDING INSTRUMENTS – NCDs (2/2)

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Tax Consideration	Domestic tax	Jurisdiction – Treaty Benefits
Interest		
In the hands of the SPV	- Deductible Expense - Withholding of tax at the rate of 5 percent (Upto July 1, 2017) - Under the Income-tax Act, 1961 - Taxed at a reduced rate of 5 percent. However, applicable only upto July 1, 2017 - Post which it will be withheld at normal rates	Å Tax rates may be reduced subject to applicable jurisdictional treaty such as 15 percent in case of Singapore
In the hands of the investor	- For non-resident, interest is taxable in the respective jurisdiction as business income or other income - Taxes withheld by the SPV, could be claimed as a credit - For a resident, interest received may be taxable at 30 percent	Å Taxes withheld by the SPV, could be claimed as a credit
Capital Gains		
In the hands of the investor	- Residents – would be taxable at normal rates - Non-residents – taxable at normal rates	Å Tax rates may be reduced subject to applicable jurisdictional treaty

FUNDING INSTRUMENTS - RUPEE DENOMINATED BONDS (1/2)

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Parameters	Framework
Eligibility	Any Company, body corporate, REITs, Infrastructure Investment Trusts (“Invits”)
Permitted instruments	- Plain Vanilla bonds issued in a Financial action Task Force (“FATF”) compliant financial centre - Could be privately placed or listed on a stock exchange as per host country regulations
Recognised lenders	Any investor in FATF compliant jurisdiction except Indian Banks
Maturity	Minimum – 5 years. Call and put option cannot be exercised before the completion of minimum maturity
All – in – cost	- Should be commensurate with the prevailing market conditions - Subject to review

End – uses	- Can be used for all purposes except
	  - real estate activities other than for development of integrated township / affordable housing projects
	  - Investing in capital markets and using the proceeds for making equity investments domestically
	  - prohibited activities under FDI guidelines
	  - on – lending to other entities for any of the above objectives; and
	  - purchase of land

Conversion rate	Rupee conversion at market rate on the date of settlement
Amount	USD 750 million per annum under the automatic route

FUNDING INSTRUMENTS - RUPEE DENOMINATED BONDS (2/2)

Tax Considerations	Existing Policy	Off-shore Policy
	Interest on rupee denominated bonds of an Indian Company paid up to July 1, 2017 is subject to withholding tax at the rate of 5 per cent	Å CBDT has issued a press release clarifying that interest on rupee denominated offshore bonds would be subject to tax at the rate of 5 per cent Å Further, capital gains arising in case of appreciation of rupee between the date of issue and the date of redemption against the foreign currency in which the investment is made would be exempted from capital gains tax Å Legislative amendment relating to the capital gains has been proposed through the Finance Bill, 2016 Å However, no changes are currently proposed in relation to lower rates of withholding

PROS AND CONS

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PROS

- Currently, rupee denominated bonds such as NCDs enjoy beneficial tax treatment at 5% only till July 1, 2017
- Post which tax would be subject to tax at normal rate after taking into consideration the rate applicable under the Double Taxation Avoidance Treaty
- Tax rates under Treaties are in the range of 10 – 15%, thereby resulting in a significant tax saving
- No capital gains on exchange difference

CONS

- Minimum maturity period of 5 years could be a deterrent

FUNDING INSTRUMENTS – EXTERNAL COMMERCIAL BORROWINGS

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- The frame work on raising loans through External Commercial Borrowings ("ECBs") comprises of three tracks:
  - Track 1 – Medium term foreign currency denominated ECB with minimum average maturity of 3-5 years
  - Track 2 - Medium term foreign currency denominated ECB with minimum average maturity of 10 years
  - Track 3 – Rupee denominated ECB with minimum average maturity of 3-5 years
- Companies in infrastructure sector eligible to borrow under Track II

Parameters	Framework
Eligibility	Any Company, body corporate, REITs, Infrastructure Investment Trusts ("Invits")
Route	- Automatic Route – Loans including bank loans, securitized instruments, Buyers' credit, Suppliers' credit, Foreign Currency Convertible Bonds, Financial Lease - Approval Route – Foreign Currency Exchangeable Bonds
Average Maturity Period	10 years
Recognised lenders	Any investor in FATF compliant jurisdiction except Indian Banks
All – in – cost	- Maximum spread over the benchmark will be 500 basis points per annum

FUNDING INSTRUMENTS – EXTERNAL COMMERCIAL BORROWINGS

Parameters	Framework

End – uses	- Can be used for all purposes except
	  - real estate activities
	  - Investing in capital markets and using the proceeds for making equity investments domestically
	  - on – lending to other entities for any of the above objectives; and
	  - purchase of land
	- Holding companies can use ECB proceeds for providing loans to infrastructure SPVs

Amount	USD 750 million per annum under the automatic route

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