

Circular No.28/2017

**F.No. 500/10/2017-FT&TR-IV
Government of India
Ministry of Finance
Department of Revenue
Central Board of Direct Taxes**

Dated, the 7th of November, 2017.

Sub: Clarification on Indirect Transfer provisions in case of redemption of share or interest outside India under the Income-tax Act, 1961

Under the provisions contained in section 9(1)(i) of the Income-tax Act, 1961 ('Act'), all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India or through the transfer of a capital asset situate in India, shall be deemed to accrue or arise in India. Explanations 5, 6 and 7 of section 9(1)(i) further define the scope of said provision.

2. Concerns have been expressed by investment funds, including private equity funds and venture capital funds, that on account of the extant indirect transfer provisions in the Act, non-resident investment funds investing in India, which are set up as multi-tier investment structures, suffer multiple taxation of the same income at the time of subsequent redemption or buyback. Such taxability arises firstly at the level of the fund in India on its short term capital gain/ business income and then at every upper level of investment in the fund chain on subsequent redemption or buyback. The Board has received representations to exclude investors above the level of the direct investor, who is already chargeable to tax in India on such income, from the ambit of indirect transfer provisions of the Act.

3. Addressing such concerns in his Budget speech on 1st February, 2017, the Finance Minister had stated that Category I and Category II Foreign Portfolio Investors (FPI) will be exempted from indirect transfer provisions. It was also stated that a clarification will be issued that indirect transfer provisions shall not apply in case of redemption of shares or interests outside India as a result of or arising out of redemption or sale of investment in India which is chargeable to tax in India.

4. Vide Finance Act, 2017, Category I and Category II FPIs have already been exempted from indirect transfer provisions of the Act through insertion of proviso to *Explanation 5* to section 9(1)(i) of the Act, with effect from 01.04.2015.

5. There could be situations in multi-tiered investment structures, where interest or share held indirectly by a non-resident in an Investment Fund or a Venture Capital Company or a Venture Capital Fund (hereinafter referred to as 'specified funds'), is redeemed in an upstream entity outside India in consequence of transfer of shares or securities held in India by the specified funds, the income of which have been subject to tax in India. In such cases, application of indirect transfer provisions on redemption of share or interest in the upstream entity may lead to multiple taxation of the same income. In respect of Category I and Category II FPIs though, such multiple taxation will not take place on account of the insertion of proviso to *Explanation 5* to section 9(1)(i) of the Act, vide Finance Act, 2017.

6. The matter has been examined by the Board and it has been decided that the provisions of section 9(1)(i) of the Act read with *Explanation 5* thereof shall not apply in respect of income accruing or arising to a non-resident on account of redemption or buyback of its share or interest held indirectly (i.e. through upstream entities registered or incorporated outside India) in the specified funds if such income accrues or arises from or in consequence of transfer of shares or securities held in India by the specified funds and such income is chargeable to tax in India. However, the above benefit shall be applicable only in those cases where the proceeds of redemption or buyback arising to the non-resident do not exceed the pro-rata share of the non-resident in the total consideration realized by the specified funds from the said transfer of shares or securities in India. It is further clarified that a non-resident investing directly in the specified funds shall continue to be taxed as per the extant provisions of the Act.

For the purposes of this Circular,

- (i) "Investment fund" shall have the meaning assigned to it in clause (a) of *Explanation 1* to section 115UB of the Act.
- (ii) "Venture capital company" and "venture capital fund" shall have the meanings respectively assigned to them in *Explanation* to clause (23FB) of section 10 of the Act.


(Amrit Agrahari)

Under Secretary [FT&TR-IV(1)]

Copy to:-

- 1. PS to FM/OSD to FM/OSD to MoS(R)
- 2. PS to Revenue Secretary
- 3. The Chairman, Members and officers of the CBDT of the rank of Under Secretary and above

4. All Pr. Chief Commissioners of Income Tax, Pr. Directors General of Income Tax with a request to circulate amongst all officers in their region/charges.
5. Pr. DGIT (NADT), Pr. DGIT (Systems), Pr. DGIT (Vigilance), Pr. DGIT (Admn.), Pr. DGIT (L&R)
6. CIT (M&TP), CBDT
7. C&AG, New Delhi
8. Web Manager for uploading on incometaxindia.gov.in & placing on public domain
9. Data Base Cell for uploading on irsofficersonline.gov.in
10. Guard File