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BUDGET ANALYSIS

IMPACT ON TMT

February 2017
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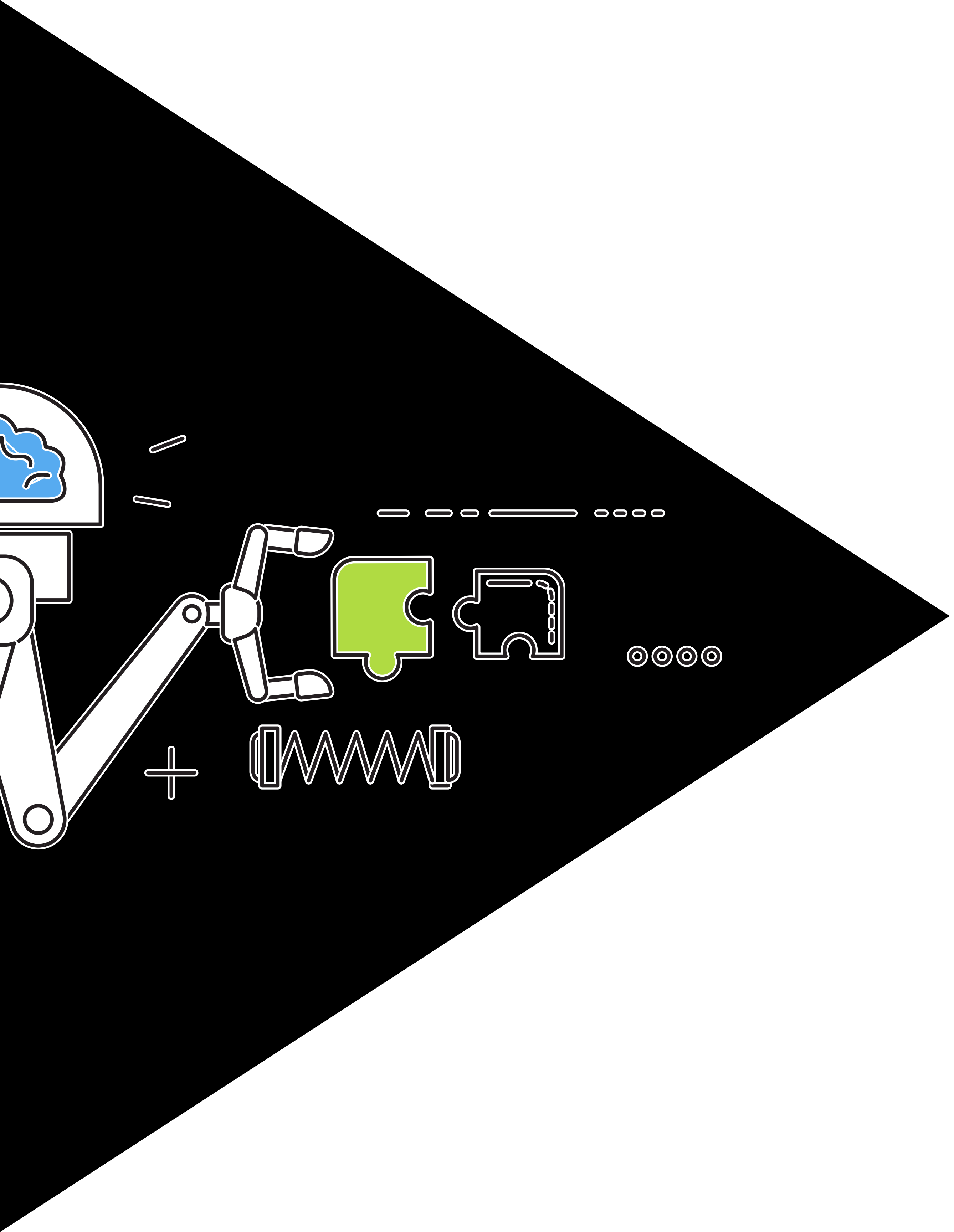


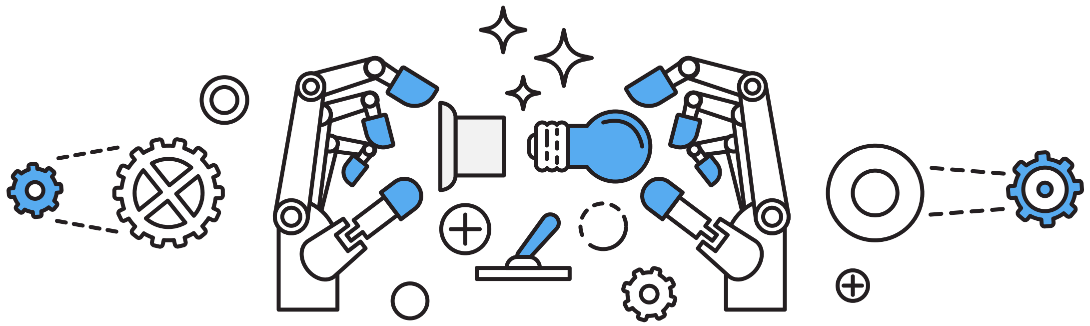
Foreword

The convergence of content, media and communications enabled by broadband connectivity and delivered using digital tools has opened up opportunities for leveraging digital platforms. Digital economy being one of the key themes of the budget, large scale technology investments have envisioned to enable this paradigm shift. Some of the examples are Digital India, smart cities program, digital payments infrastructure, Aadhar Pay and Bharatnet Project for rural broadband connectivity. These along with digital content and media ecosystem will form the basis for bringing digital services to the masses. To that effect, India's TMT sector could be considered as the platform that will accelerate our country's economic growth in the coming years.

The industry is not without its set of challenges. The USD 143 billion primarily export driven, IT/ITeS sector is currently going through a fundamental shift due to increasing commoditization of traditional services, changing geo-political discourse on globalization, and adoption of automation technologies that may negatively impact low skilled jobs in the short to medium term. The USD 37 billion telecom sector is continuously required to invest in the latest 4G/5G technologies to improve Quality of Experience (QoE) for mobile internet users, when majority of their revenue is derived from Voice - realizations for which are among the lowest in the world. The resultant overleveraging of telco balance sheets due to increasing capital expenditures in equipment and spectrum curtails the operators' ability for investment. In addition, provision and creation of cyber security for the nation's digital assets becomes an area of importance.

These challenges notwithstanding, the overall direction for TMT sector from the union budget is positive, given the focus on digital economy, built on digital transactions to broaden the tax base, and the opportunities for technology interventions across sectors such as infrastructure, financial services, education, healthcare, governance, and public services. Such large scale digitization of economy across the spectrum could positively impact the domestic technology and big-data analytics industry as data assumes center stage in policy decisions. At a time when the sector is facing global headwinds, budget 2017 lays out opportunities for the industry to focus on localized innovation, as digital services seek to cater to the larger population. Budget's impact on TMT sector should be assessed in this context to understand how it enables the industry achieve its potential and support nation building.

Policy Updates

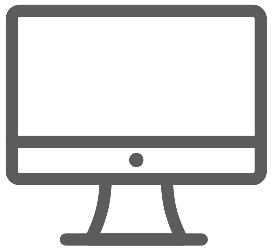


Summary

The budget proposals seek to move India towards a more transparent economy. The key agenda for the Budget is to transform the quality of governance, invigorate the youth and vulnerable, and teliminate corruption, black money and non-transparent political funding and promoting regulatory efficiency.

Key Highlights

Emphasis on digital economy with a view to formalize the economy and weed out corruption and Black money..



Proposed amendments to key laws to facilitate digital payments and eliminate cash transactions.

Tax proposals to encourage start-ups in continuation of the Start-up India initiative.

Key budget announcements

- With new Bharat Interface for Money (BHIM) app, the Government will soon launch two new schemes to promote the usage of BHIM; these are, Referral Bonus Scheme for individuals and a Cashback Scheme for merchants.
- To promote digital transactions, and to ensure that payees of dishonoured cheques are able to realise payments, it is proposed to make necessary amendments to the Payments and Settlements Systems Act and the Negotiable Instrument Act.
- The Foreign Investment Promotion Board (FIPB) will be abolished during the year FDI Policy will be further liberalized and necessary announcements will be made in due course.

FIPB will be abolished and FDI Policy will be further liberalized.

Recent policy changes

Technology

- The contribution of the IT sector to India's GDP rose to approximately 9.5% in financial year 2014-15 from 1.2% in financial year 1997-98. The Indian IT sector is expected to grow at a rate of 12-14% for financial year 2016-17 in constant currency terms. The sector is also expected to triple its current annual revenue to reach USD 350 billion by financial year 2025. India ranks third among global start-up ecosystems with more than 4,200 start-ups.

To promote digital transactions, necessary amendments would be made in various laws and new schemes expected.

- For the Technology industry, 100% Foreign Direct Investment (FDI) is permitted under the automatic route. The sector ranks third in the list of top ten sectors receiving highest FDI in India. The total FDI inflows during April 2016 to September 2016 in the technology sector was USD 1,032 million.

Startup India

- Startup India is a flagship initiative of the Government of India, intended to build a strong eco-system for nurturing innovation and startups in the country that will drive sustainable economic growth and generate large scale employment opportunities.
- Startup India Hub was operationalized on 1 April 2016 to resolve queries and provide handholding support to startups.
- The Finance Act, 2016 has made provision for startups to get income tax exemption for
- 3 years in a block of 5 years, if they are incorporated between 1 April 2016 and
- 31 March 2019. To avail these benefits, one must get a Certificate of Eligibility from the Inter-Ministerial Board of DIPP.
- Startups falling under the list of 36 category industries have been exempted from compliances under 3 Environment Laws viz. The Water (Prevention & Control of Pollution) Act, 1974; The Water (Prevention & Control of Pollution) Cess (Amendment) Act, 2003 and The Air (Prevention & Control of Pollution) Act, 1981. Apart from these, compliance regime for startups has been liberalized to undertake self-certification.

Digital India

- Digital India was launched by the Government in 2015 with an objective of connecting rural areas with high-speed Internet network and improving digital literacy. The vision of Digital India is centered on three key areas – Digital Infrastructure as a Utility to Every Citizen, Governance & Services on Demand and Digital Empowerment of Citizens.
- The 2016 Union Budget of India announced 11 technology initiatives including the use data analytics to nab tax evaders, creating a substantial opportunity for IT companies to build out the systems that will be required. The major services offered under the digital India program are Digital Locker, Attendance.gov.in and Mygov.in platforms, Swachh Bharat Mission App and e-sign framework.

Enactment of the Aadhar (Targeted Delivery of Financial and Other Subsidies, Benefit and Services) Act, 2016

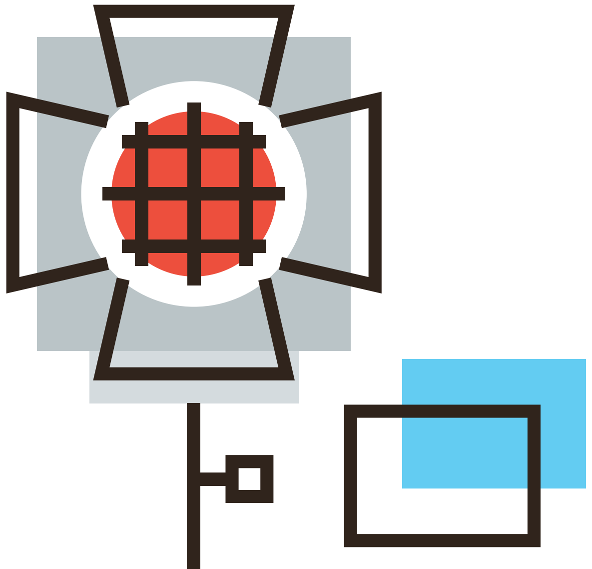
- In March 2016, the Aadhar (Targeted Delivery of Financial and Other Subsidies, Benefit and Services) Act, 2016 has been enacted as law.
- This Act provides for use of identification number issued by the Unique Identification Authority of India (UIDAI), to deliver State subsidies directly into the bank accounts of the beneficiaries under the various subsidies and monetary schemes offered by the Government of India to the economically weaker section of the Society.
- Amendment in Modified Special Incentive Package Scheme
- In January 2017, the Union Cabinet has given its approval for amendment in the Modified Special Incentive Package Scheme (M-SIPS) to further incentivize investments in Electronic Sector and moving towards the goal of 'Net Zero imports' in electronics by 2020.
- The applications will be received under the scheme up to 31 December 2018 or till such time that an incentive commitment of INR 100,000 million is reached, whichever is earlier. The incentives will be available for investments made within 5 years from the date of approval of the project.
- Approvals will normally be accorded to eligible applications within 120 days of submission of the complete application.

Media

Liberalization of foreign direct investment (FDI) policy

Sector	Earlier sectoral cap	Current sectoral cap
Broadcasting		
• Teleports • Direct to home • Cable networks • Mobile TV • Headend-in-the sky broadcasting services	• 100% Automatic route up to 49% • Government route beyond 49%	• 100% Automatic route

However, Government approval is required for infusion of fresh foreign investment beyond 49% in a company not seeking license/permission from sectoral Ministry, resulting in change in ownership pattern or transfer of stake by existing investor to new foreign investor.

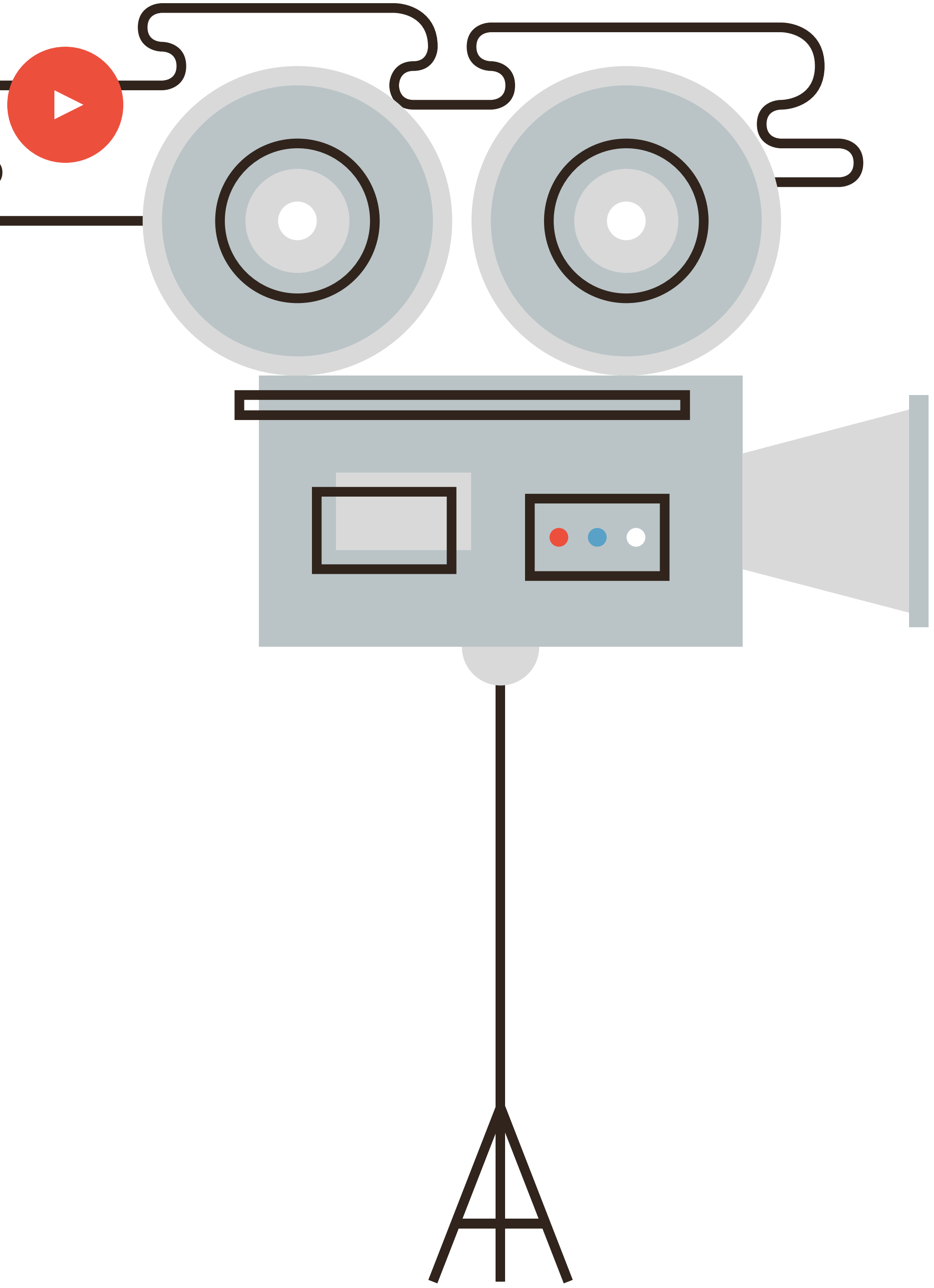


Currently, a Government (i.e. Foreign Investment Promotion Board) approval is required for the following sectors:

Sector	Earlier sectoral cap
Broadcasting	
• Terrestrial Broadcasting FM (FM Radio)	49%
• Up-linking of 'News & Current Affairs' TV channels	49%
Print	
• Publishing of newspaper and periodicals dealing with news and current affairs	26%
• Publication of Indian editions of foreign magazines dealing with news and current affairs	26%
• Publishing / printing of scientific and technical magazines / specialty journals / periodicals	100%
• Publication of facsimile edition of foreign newspapers	100%

Digitisation of cable TV

- The Cable Television Networks (Regulation) Amendment Act, 2011 makes it mandatory for switch-over of the existing analogue cable TV networks to Digital Addressable System in four phases. Digital switch over has already taken place in Phase-I (i.e. in Delhi, Mumbai, Kolkata, Chennai) and Phase-II (in cities with population more than one million) areas. The Ministry of Information and Broadcasting has extended the timelines for Phase-III (i.e. all other urban areas) and Phase-IV areas (i.e. rest of India) to switch over to digitisation by 31 January 2017 and 31 March 2017, respectively.



Advertisement airtime on television channels

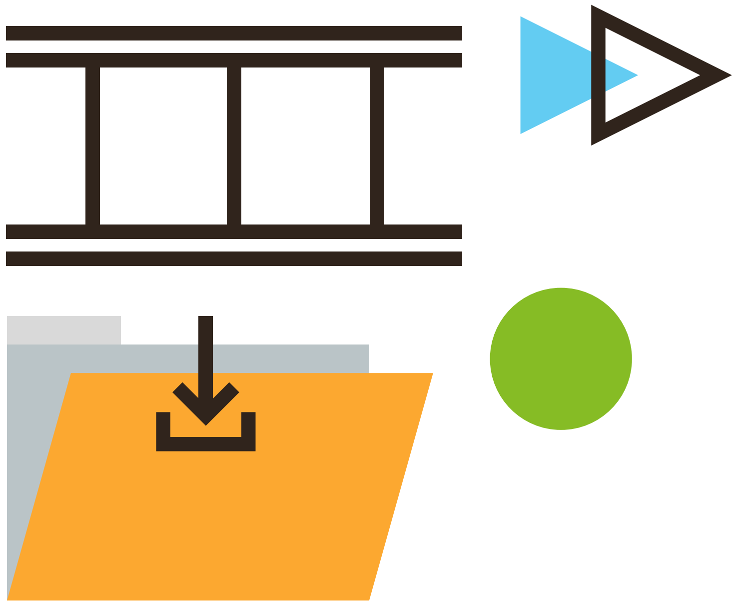
- The Telecom Regulatory Authority of India (TRAI) had issued a notification amending Standards of Quality of Service (Duration of Advertisements in Television Channels) (Amendment) Regulations, 2013, restricting duration of advertisements to 12 minutes for each hour of television programming.
- News Broadcasters Association and other stakeholders had filed a case against the above restriction which is pending before the Delhi High Court and the next hearing is scheduled on 20 April 2017.

Promoting India as a filming destination

- As part of providing a single window mechanism for facilitating shooting in India, the Ministry of Information and Broadcasting has set up the Film Facilitation Office (FFO).
- FFO would act as a facilitation point for film producers and assist in obtaining requisite permissions, disseminate information on shooting locales as well as the facilities available with the Indian film industry for production/post-production and work closely with state Governments in assisting them to set up similar facilities. Filmmakers can expect clearance between six to eight weeks, depending on the shooting location.

Auction of radio Phase-III channels

- Recently, the Ministry of Information and Broadcasting conducted auctions for radio Phase-III channels. Such auctions proposed to award 266 FM radio channels in 92 cities. These results areyet to be announced.



Telecom

e-KYC

- e-KYC through Aadhaar for telecom subscriber verification would be beneficial to all the stakeholders.
- For telecom companies, it would bring down the cost of subscriber acquisition significantly as companies would not be required to spend on physical transportation of forms, its verification, scanning and storage. It would also enable easier compliance and reduction in litigation on account of audit carried out by term cell.
- For subscribers, it would reduce time to SIM activation as KYC is verified instantly and reduce paper work requirement.
- For government, it would keep audit trail and ensure national and personal security of citizens.

Mobile Banking QoS

- TRAI has lowered ceiling tariff for USSD-based service to a third, at 50 paise per session. Revised Mobile Banking (QoS) (Amendment) regulation 2013 will help to increase the use of USSD based mobile transactions.

Discriminatory tariff

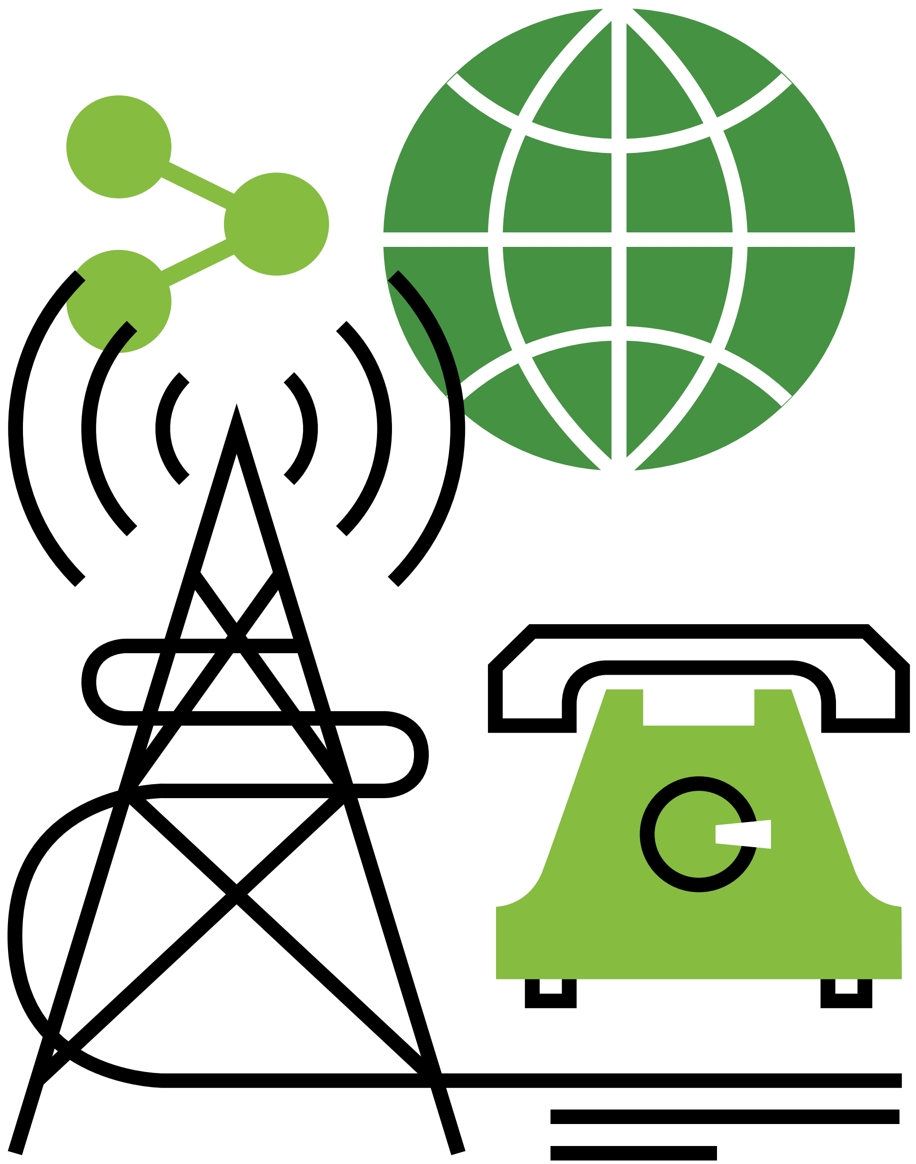
- Service providers cannot offer or charge discriminatory tariffs for data services on the basis of content.
- Service providers cannot enter into agreements, arrangements with any person, natural or legal that has the effect of discriminatory tariffs for data services being offered or charged to the consumer on the basis of content.

MVNO

- In May 2016, the Department of Telecommunication (DoT) issued guidelines for grant of Unified License Virtual Network Operators (UL VNOs).
- For obtaining UL VNO, companies will have to pay a one-time non-refundable entry fee for an authorization of each service they want to provide and for each service area where they wish to operate. The VNOs will be treated as extension of telecom service providers and, hence, would not be allowed to install equipment interconnecting with network of any other telecom service providers.

Audio conferencing/ Audiotex/ Voice Mail Services

- TRAI has issued recommendations on the licensing framework for Audio Conferencing/ Audiotex / Voice Mail Services.
- An additional service authorization for Audio Conferencing/ Audiotex/ Voice Mail Services to be added in the Unified License (UL) with duration of 20 years for Pan India license.
- License fee to be levied at 8% of Adjusted Gross Revenue (AGR) on both existing as well as the new authorisation under Unified License.



Right of Way (RoW)

- The Department of Telecommunications (DoT) has released Indian Telegraph Right of Way Rules, 2016 for regulating Right of Way for underground infrastructure (optical fibre) and over ground infrastructure (mobile towers).
- The appropriate Authority (Central, respective state governments and local authorities designated by central or state government) will grant or reject the application within 60 days with reasons recorded in writing.
- For underground infrastructure, the right of way fees shall not exceed one thousand rupees per kilometer & for overhead infrastructure it shall not exceed INR 10,000.

Sharing of Active Infrastructure

- In February 2016, DoT permitted the sharing of active infrastructure.
- As per the guidelines, sharing of active infrastructure amongst service providers based on mutual agreements entered amongst them is permitted.
- Active infrastructure sharing will be limited to antenna, feeder cable, Node B, Radio Access Network (RAN) and transmission system only.

Telecommunication (Broadcasting and Cable Services) Interconnection Regulations, 2016

- As per the Draft Telecommunication (Broadcasting and Cable Services) Interconnection (Addressable Systems) Regulations, 2016, a common interconnection rule when implemented would foster competition, promote orderly growth and result in better quality of services at affordable prices to subscribers.

Direct Tax

Corporate Tax

- The Finance Minister has clarified that deduction under section 10AA of the Act will be allowed against the total income of the assesse i.e., after set-off of losses and unabsorbed depreciation. This proposal will in effect overrule the recent Supreme Court decision in the context of section 10A of the Act wherein it was held that deduction will be allowed against the total income of the undertaking of an taxpayer i.e., before set off of losses and unabsorbed depreciation.

Deduction under section 10AA of the Act after set-off of losses and unabsorbed depreciation.

- In respect of eligible start-ups referred to under section 80-IAC of the Act, a concession has been allowed for carry forward of losses incurred in the first 7 years from the date of incorporation if all the shareholders of such company who held shares carrying voting power on the last day of the year or years in which the loss was incurred continue to hold those shares in the year of set-off. In other words, the concession has been allowed for dilution in the ownership of a start-up which happens by issuing additional share capital from time to time (ultimately leading to a 51% change in ownership) will not impact carry forward of loss provided the original shareholders have not reduced their shareholding.

For start-ups, the condition of continuous holding of 51% of voting rights for carry forward of losses has been relaxed subject to specified conditions. The profit linked deduction available to the start-ups is being changed to 3 years out of 7 years.

With the objective to further boost the start-up ecosystem in India, the time limit for claiming the profit linked deduction available to the eligible start-ups referred to under section 80-IAC of the Act has been increased to 7 years from the current 5 years. However, the tax holiday continues to be available for any 3 consecutive assessment years out of 7 years.

- The income tax for smaller companies with annual turnover up to INR 500 million is proposed to be reduced to 25%, in order to make micro, small and medium enterprises (MSMEs) more viable and also to encourage firms to migrate to company format.
- A new section 94B is proposed to be introduced by the Budget, to tackle thin capitalization in Multi-National Enterprises. The new section provides that the interest paid or payable to Associated Enterprises in excess of INR 10 million, will be allowable only to the extent of 30% of EBITDA. The interest expense disallowed will be eligible to be carried forward for 8 years. This is in line with the recommendations of the Organization for Economic Cooperation and Development on Base Erosion and Profit Shifting and the tax rules in the other countries.
- While there was an expectation that rate of MAT should be reduced in line with reduction of corporate tax rates, this has not happened. However, the carry forward period of MAT credit has been increased to 15 years from 10 years thus providing the companies an additional 5 years to carry forward the MAT credit entitlement. This is a positive measure and will help many IT/ ITeS companies availing tax holidays.

Carry forward of MAT credit extended from 10 to 15 years.

- In case of companies paying tax under MAT and claiming FTC, the amount of MAT credit shall be computed after considering the lower of the FTC as per MAT provisions and normal provisions.

Direct Tax

- It is proposed to amend section 194J of the Act and reduce the rate of withholding tax on payments made to a person engaged only in the business of a call center to 2% from the existing 10%. This proposal will have a positive impact on domestic BPO operations.
- In order to promote the digital economy, the Finance Minister has proposed various measures, including reduction of the existing rate of deemed total income of 8% to 6% in respect of turnover from non-cash means, , restriction of permissible threshold of cash transactions etc.

- The concessional rate of 5% withholding tax on interest payments under section 194LC of the Act is proposed to be extended in respect of eligible ECBs made before 1 July 2020 (i.e. the sunset date is proposed to be moved from 1 July 2017 to 1 July 2020).
- The concessional rate of 5% withholding tax on interest payments under section 194LD of the Act (on rupee denominated bonds of an Indian company/ government security) is proposed to be extended in respect of interest payable before 1 July 2020 (i.e. the sunset date is proposed to be moved from 1 July 2017 to 1 July 2020).

Transfer Pricing

Introduction of Section 92CE for Secondary Adjustments

- Taxpayers would now need to make a corresponding secondary adjustment to their books of accounts to give effect to any primary adjustment made to their transfer price (either sue moto by the taxpayer himself, made by the Assessing Officer and accepted by the taxpayer; or determined by way of advance pricing agreement/ Safe Harbour Rules/Mutual Agreement Procedure). In cases where there is an increase in income or decrease in losses to the Indian taxpayer on account of primary transfer pricing adjustment and the excess money is not repatriated to India, the same would be treated as an advance made to the Associated Enterprise on which an arm's length interest has to be charged. The move is aligned with international best practices and the OECD Transfer Pricing Guidelines.
- Secondary adjustments would be applicable prospectively and only if the quantum of primary adjustment is greater than INR 10 million.

Amendment to Section 92BA or provision for Specified Domestic Transaction ("SDT"):

- The FM has proposed to amend the definition of SDT which will substantially reduce the compliance burden for domestic taxpayers across industries. Going forward, the provisions of SDT would be only applicable to domestic transactions between related parties, where one of the entities is availing certain tax benefits. Under the existing provisions, expenditure in the nature of interest, royalty, cost of goods & services, directorial remuneration etc. made to persons specified under Section 40A(2)(b) of the Act is covered under the ambit of SDT. SDT provisions would no longer be applicable if none of the domestic related parties are enjoying any kind of profit linked tax exemption.
- The relief would be a welcome move, especially for taxpayers who had only SDT and no international transactions. The proposed amendments would relieve such taxpayers from the requirement of filing a Form 3CEB and maintaining a transfer pricing documentation.

SDT provision to now apply only in cases where one of the domestic related parties enjoys a profit linked tax exemption.

Secondary Transfer Pricing adjustments introduced in India.

Indirect Taxes

General

- Finance Minister reiterated the readiness of GST. IT systems are on track for GST implementation later this year.
- Trade and industry awareness for new taxation system of GST will start from 1 April 2017
- Research and Development Cess Act, 1986 is proposed to be repealed from 1 April 2017
- Increase in allocation for incentive schemes like M-SIPS and EDF to make India a global hub for electronics manufacturing

Service Tax

- On repeal of R & D Cess, exemption of service tax to a taxable service on import of technology will be withdrawn and full service tax along with cesses would be applicable on such services from 1 April 2017 and such service tax paid will be available as credit.

Customs (changes effective 2 February 2017)

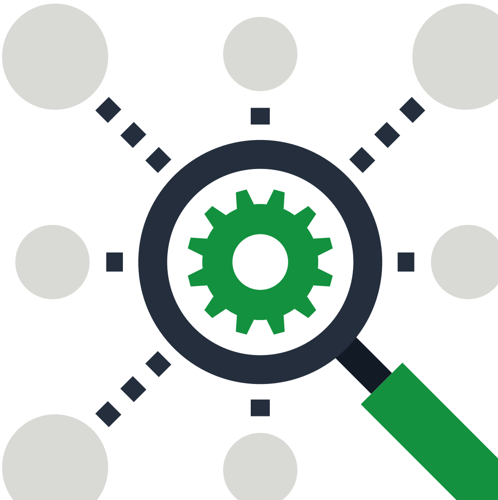
- Special Additional Duty has been increased to 2% for populated Printed Circuit Boards (PCBS) for manufacture of mobile phones subject actual user conditions
- Applicable Basic Customs Duty (BCD), Countervailing Duty (CVD) and Special Additional Duty (SAD) is exempt for Miniaturized POS card reader for m-POS (not including mobile phones, or tablet computers), micro ATM as per standards version 1.5.1, Finger Print Reader / Scanner or Iris Scanner including parts and components for manufacture of these devices subject to actual user conditions
- 10% concessional BCD is being prescribed on Co-polymer coated MS tape/stainless steel tape for manufacture of telecommunication grade optical fibres or optical fibre cables, subject to actual user condition

Central Excise (changes effective 2 February 2017)

- Exemption from Excise Duty on miniaturized POS card reader for mPOS (other than mobile phone or tablet computer), micro ATMs as per standards version 1.5.1, fingerprint reader / scanner, iris scanner, parts and components for manufacture of these devices, subject to actual user condition

In light of the upcoming implementation of GST, no major changes in the indirect tax structure are proposed.

R&D Cess proposed to be repealed.



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