

## India Seeking to Tax Overseas Transactions to Limit Claims

By Unni Krishnan and Ruth David on March 19, 2012

India will claim capital gains tax on cross-border acquisitions completed in the past six years through an amendment after Vodafone Group Plc (VOD) won a case against such levies, according to Finance Secretary R.S. Gujral.

Finance Minister Pranab Mukherjee on March 16 proposed changing the law two months after the Supreme Court ruled that Vodafone doesn't have to pay \$2.2 billion in tax on its purchase of the local business of Hutchison Whampoa Ltd. (13) in 2007. Taxation experts at firms including KPMG said the changes applicable retrospectively from 1962 may slow foreign investments into the South Asian nation.

Gujral, seeking to reduce concern that the changes will prompt the tax office to claim levies on 50 year-old deals, said the amendment was proposed to clarify the intent of the law. Mukherjee, struggling to rein in the widest budget deficit among major emerging economies, wants the change to ensure the government gets as much as 400 billion rupees (\$8 billion) of tax payments that officials say are under litigation.

"Once the investment decision is made, then only do investors look at issues of taxation," Gujral said in New Delhi yesterday. "I don't think this will discourage FDI."

Nishith Desai, managing partner at law firm Nishith Desai & Associates, called the proposal a "knee-jerk reaction" to the Vodafone lawsuit.

"The budget proposes a number of regressive, retrograde and extraterritorial provisions that would significantly increase tax costs and alter the dynamics of cross-border transactions and M&As," Desai said in an e-mail on March 17. The proposal will "considerably erode India's standing in the eyes of investors," he said.

### \$27.6 Billion

India attracted \$27.6 billion of foreign direct investments in 2011, a 31 percent increase over the previous year, according to data from the trade ministry.

The nation gives foreign investors the guarantee that they will not be taxed doubly, Mukherjee said in an interview to Bloomberg UTV on March 17. "We do not give them the guarantee that they will not have to pay tax in any country. That way we'll simply encourage tax evasion. That is not possible for any government."

The Supreme Court in January dismissed the government's demand for 112.2 billion rupees of taxes from Vodafone, stemming from the 2007 purchase.

Transactions like Vodafone could now be reopened and "assuming that the law holds, the companies will be issued tax notices," said Uday Ved, a partner at the local unit of KPMG.

The government's budget proposal to introduce general anti-avoidance rules, or GAAR, enabling the taxing of companies it believes are structuring deals in a manner to escape taxes, could serve as a roadblock to investments, Desai said.

## 'Pandora's Box'

"The ambiguously worded provisions capture most conventional structures for M&As and investments into India," Desai said. "If implemented, GAAR will open up a Pandora's box of uncertainty and litigation, and investors may be forced to think twice."

While budget amendments to counter Vodafone (VODA) and similar transactions were anticipated, the retrospective aspect of the proposed laws is "surprising," said Pallavi Bakhru, practice leader for tax and regulatory services at Walker Chandiook & Co.

"We suspect that the constitutional validity of such an amendment will be questioned," Bakhru said in an e-mail.

The government on Feb. 17 filed a petition to review the Supreme court's decision on Vodafone, seeking to overturn the ruling. The court had directed the government to return a 25 billion-rupee deposit Vodafone (VODA) made on the contested tax bill, plus 4 percent interest.

The court will hear the government's petition tomorrow, according to a notice posted on the court's website.

## Faith in India

"We are examining this proposed decision with our lawyers, but we do not believe this retrospective change in tax law should have any impact on the final judgment handed down," Vodafone said in an e-mailed statement on March 16. "We continue to have faith in the Indian judicial system."

Newbury, England-based Vodafone (VODA) and Hutchison conducted their \$10.7 billion transaction offshore, with Vodafone's Dutch subsidiary, Vodafone International Holdings BV, acquiring CGP Ltd., a Cayman Islands-based holding company controlled by Hong Kong-based Hutchison.

India's tax department in September 2007 sought the capital gains tax, saying Vodafone should have withheld that amount from its payment to Hutchison.

Vodafone is India's third-largest wireless operator, with 148 million subscribers and a 17 percent share of the country's 894 million mobile-phone accounts at the end of December, according to the nation's telecommunications regulator.

"It is certain that this amendment will be challenged before the Supreme Court by aggrieved parties," said KPMG's Ved. However, such petitions haven't had much success, he said.

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