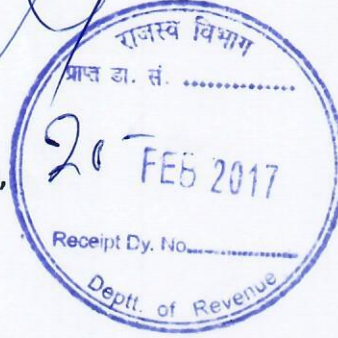



IVCA
IVC ASSOCIATION
THE INDIAN PRIVATE EQUITY & VENTURE CAPITAL ASSOCIATION

To,

Shri. Rajesh Bhoot
Joint Secretary - Tax Policy & Legislation - II,
Central Board of Direct Taxes (CBDT),
Ministry of Finance, North Block,
New Delhi, India

17th February, 2017



Re: Budget 2017 proposals: Clarification and modifications sought on conversion of preference shares into equity shares

Respected Sir,

At the outset, thank you for your time to meet with us yesterday.

On a perusal of the Finance Bill, 2017 ('the Finance Bill'), we invite your kind attention to some of the clarifications relevant to the private equity and venture capital ('VC/PE') sector that arise from the amendments proposed in the Finance Bill. On behalf of the IVCA, we hereby submit the following:

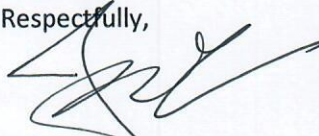
Note: 1) Clarification and modifications sought on conversion of preference shares into equity shares

We humbly request you to consider the above suggestions, which will provide further certainty on the tax proposals in the Finance Bill to the VC/PE sector.

We will like to discuss the above in person and request if you can give us a time of your convenience to meet on in the week of 20th February 2017.

Look forward to hearing from you.

Kind regards,
Respectfully,


Rajat Tandon
President, IVCA
98100 90194

cc: Aakriti Bamniyal, AVP, IVCA, 97 1111 0011; Yogesh Arora 95 400 84999

Attached Note 1

1. **Note1: Conversion of preference shares into equity shares**

Background

- 1.1 The Finance Bill has proposed an amendment to provide that conversion of preference shares into equity shares where the conversion takes place on or after April 1, 2017 shall not be regarded as a 'transfer'. It has further provided that the period of holding of the equity shares received on conversion shall be deemed to include the period for which the preference shares were held by the taxpayer.
- 1.2 This is a welcome move and will help in addressing the concerns raised by the industry in the past.

Concerns

- 1.3 The Memorandum to the Finance Bill mentions that under the existing provisions of the Act, conversion of security from one form to another is regarded as transfer for the purpose of levy of capital gains tax. This implies that the conversion of preference shares into equity shares currently is a taxable transfer and shall continue to be so with respect to all conversions prior to 1 April 2017.
- 1.4 With respect to the above, despite the lack of clarity in the law, we humbly submit that conversion of preference shares into equity shares has been a subject matter of debate and taxpayers have generally not regarded such conversion as a taxable transfer for the following reasons:
- Letter dated 12 May 1964 (F. No. 12/1/64-IT (AI)) provides that conversion of one type of share into other shall not be subject to capital gains tax.
 - Few judicial precedents have applied the above Circular to hold that there is no transfer when one type of share is converted into another type of share.
- 1.5 The proposed amendment creates a doubt on past conversions of preference shares into equity shares, which may have unintended consequences.

Suggestion

- 1.6 While welcoming the above amendment, we request you to clarify by way of amendment to the Finance Bill that the proposed amendment should be applicable retrospectively.
- 1.7 In case the amendment cannot be introduced retrospectively, a suitable clarification through an issue of a Circular should be issued stating that where a tax payer has, relying on the 1964 Letter, in the past prior to the amendment of the Act by the Finance Act 2017, taken a position that conversion of preference shares into equity shares is a tax neutral conversion, then no adverse action would be taken by the field assessing officers in this regard.